INSURANCE AUSTRALIA GROUP LIMITED
PRELIMINARY FINAL REPORT FOR THE YEAR ENDED 30 JUNE 2016

APPENDIX 4E (ASX Listing rule 4.3A)

## RESULTS FOR ANNOUNCEMENT TO THE MARKET

| | UP / DOWN | % CHANGE | **2016 $m** | 2015 $m |
|---|---|---|---|---|
| Revenue from ordinary activities | Up | 11.8 % | **16,772** | 15,008 |
| Net profit/(loss) after tax from ordinary activities attributable to shareholders of the Parent | Down | 14.1 % | **625** | 728 |
| Net profit/(loss) attributable to IAG shareholders | Down | 14.1 % | **625** | 728 |

| **DIVIDENDS - ORDINARY SHARES** | **AMOUNT PER SECURITY** | **FRANKED AMOUNT PER SECURITY** |
|---|---|---|
| Final dividend | 13.0 cents | 13.0 cents |
| Interim dividend | 13.0 cents | 13.0 cents |
| Special dividend | 10.0 cents | 10.0 cents |

| **FINAL DIVIDEND DATE** | |
|---|---|
| Record date | 7 September 2016 |
| Payment date | 5 October 2016 |

The Company's Dividend Reinvestment Plan (DRP) will operate by acquiring shares on-market with no discount applied. The last date for the receipt of an election notice for participation in the Company's DRP is 8 September 2016. The DRP Issue Price will be based on a volume weighted average price for a 10 day trading window from 9 September 2016 to 22 September 2016 inclusive.

Eligible shareholders may now lodge their DRP elections electronically by logging on to IAG's share registry, Computershare, on their website at www.computershare.com.au.

Additional Appendix 4E disclosure requirements can be found in the Annual Report of Insurance Australia Group Limited for the year ended 30 June 2016 (Attachment A). This report is also to be read in conjunction with any public announcements made by Insurance Australia Group Limited during the reporting year in accordance with the continuous disclosure requirements of the Corporations Act 2001 and the ASX Listing Rules.

The report is based on the consolidated financial statements which have been audited by KPMG.

ATTACHMENT A

INSURANCE AUSTRALIA GROUP LIMITED AND SUBSIDIARIES

ANNUAL REPORT 30 JUNE 2016

# NUMBERS.

**INSURANCE AUSTRALIA GROUP LIMITED**
ANNUAL REPORT 2016

ABN 60 090 739 923

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## KEY DATES

| | |
|---|---|
| 2016 financial year end | 30 June 2016 |
| Full year results and dividend announcement | 19 August 2016 |
| Notice of meeting mailed to shareholders | 6 September 2016 |
| Final dividend for ordinary shares | |
| Record date | 7 September 2016 |
| Payment date | 5 October 2016 |
| Annual general meeting | 21 October 2016 |
| Half year end | 31 December 2016 |
| Half year results and dividend announcement | 16 February 2017* |
| Interim dividend for ordinary shares | |
| Record date | 1 March 2017* |
| Payment date | 30 March 2017* |
| 2017 financial year end | 30 June 2017 |
| Full year results and dividend announcement | 23 August 2017* |

* Please note: dates are subject to change. Any changes will be published via a notice to the Australian Securities Exchange (ASX)

### ABOUT THIS REPORT

The 2016 annual report of Insurance Australia Group Limited (IAG, or the Group) includes IAG's full statutory accounts, along with the Directors' and remuneration reports for the 2016 financial year. This year's corporate governance report is available in the About Us area of our website (www.iag.com.au).

The financial statements have been reorganised this year, with the notes to the accounts being grouped into relevant sections to improve the clarity of the disclosures that are considered most relevant to users' understanding of the operations, results and financial position of IAG.

This report should be read with the 2016 annual review, which provides a summary of IAG's operating performance, including the Chairman's, CEO's and CFO's reviews.

If you do not receive a printed copy of the annual review, you can access an interactive version online from the home page of our website at www.iag.com.au.

The annual review also includes information about the Group's shared value strategy and performance. Detailed information about IAG's non-financial performance is available from www.iag.com.au.

If you would like to have a copy of the annual report or annual review mailed to you, contact IAG's Share Registry using the contact details on page 87.

All figures are in Australian dollars unless otherwise stated.

### 2016 ANNUAL GENERAL MEETING

IAG's 2016 annual general meeting will be held on Friday, 21 October 2016, at the Wesley Conference Centre, 220 Pitt Street, Sydney, commencing at 10.00am. Details of the meeting, including information about how to vote, will be contained in our notice of meeting, which will be mailed to shareholders, and available on line at www.iag.com.au, from Tuesday, 6 September 2016.

The covers for this year's annual report and annual review feature NRMA Insurance customer, Vicki Uriarte, with Maggie and Marco from her Urban Cooking Collective business in Maroubra, Sydney. Vicki took out an NRMA Business Pack policy in 2014.

In keeping with the Closer theme for this year's reporting suite, Vick Uriarte and her Urban Cooking Collective will provide the catering for our 2016 annual general meeting.

# DIRECTORS' REPORT

The Directors present their report together with the financial report of Insurance Australia Group Limited and the consolidated financial report of Insurance Australia Group Limited and its subsidiaries for the financial year ended 30 June 2016 and the Auditor's Report thereon.

The following terminology is used throughout the financial report:
- IAG, Parent or Company - Insurance Australia Group Limited; and
- Group or Consolidated - the Consolidated entity consists of Insurance Australia Group Limited and its subsidiaries.

## DIRECTORS OF INSURANCE AUSTRALIA GROUP LIMITED

The names and details of the Company's Directors in office at any time during or since the end of the financial year are as follows. Directors were in office for the entire period unless otherwise stated.

### CHAIRMAN

**ELIZABETH (EB) BRYAN AM**

**BA (Econ), MA (Econ), age 69 - Chairman and Independent Non-Executive Director**

INSURANCE INDUSTRY EXPERIENCE

Elizabeth Bryan was appointed as a Director of IAG on 5 December 2014, and became Chairman on 31 March 2016. She is the Chairman of IAG's People and Remuneration Committee and Nomination Committee, and a member of the Risk Committee. Elizabeth is also the Chairman of Insurance Manufacturers of Australia Pty Limited.

OTHER BUSINESS AND MARKET EXPERIENCE

Elizabeth brings extensive leadership, strategic and financial expertise to the position of Chairman.

She has over 32 years of experience in the financial services industry, government policy and administration, and on the boards of companies and statutory organisations.

In addition to her role as Chairman of IAG, Elizabeth is also currently Chairman of Virgin Australia and a Director of Westpac Banking Corporation.

Previous roles include Chairmanship of Caltex Australia Limited and UniSuper Limited.

Directorships of other listed companies held in the past three years:
- IAG Finance (New Zealand) Limited (a part of the Group), since 2016;
- Virgin Australia, since 2015;
- Westpac Banking Corporation, since 2006; and
- Caltex Australia Limited (2002-2015).

### MANAGING DIRECTOR

**PETER (PG) HARMER**

**Age 56, Managing Director and Chief Executive Officer, Executive Director**

INSURANCE INDUSTRY EXPERIENCE

Peter Harmer was appointed Managing Director and Chief Executive Officer of IAG on 16 November 2015. He is a member of IAG's Nomination Committee.

Peter joined IAG in 2010 and has held a number of senior roles, most recently as Chief Executive of the IAG Labs division, responsible for driving digital and innovation across IAG and its brands, and creating incubator areas which will specifically explore innovative opportunities across the fintech landscape.

Before this, Peter held the role of Chief Digital Officer with a remit to develop a group-wide digital strategy. He was formerly Chief Executive of the Commercial Insurance division created in July 2014 when IAG implemented its new operating model. He joined IAG as Chief Executive Officer, CGU Insurance.

Peter was previously Chief Executive Officer of Aon Limited UK and a member of Aon’s Global Executive Board, and spent seven years as Chief Executive Officer of Aon’s Australian operations.

He has over 35 years experience in the insurance industry, including senior roles in underwriting, reinsurance broking and commercial insurance broking as Managing Director of John C. Lloyd Reinsurance Brokers, Chairman and Chief Executive of Aon Re and Chairman of the London Market Reform Group.

Peter has completed the Harvard Advanced Management Program.

Directorships of other listed companies held in the past three years:
- IAG Finance (New Zealand) Limited (a part of the Group), since December 2015.

## OTHER DIRECTORS

### ALISON (CA) DEANS

**BA, MBA, GAICD, age 48 - Independent Non-Executive Director**

INSURANCE INDUSTRY EXPERIENCE

Alison Deans was appointed as a Director of IAG on 1 February 2013. She is a member of IAG's People and Remuneration Committee and Nomination Committee.

OTHER BUSINESS AND MARKET EXPERIENCE

Alison was formerly CEO of netus, a technology based investment company focused on building consumer web businesses in Australia and acquired by Fairfax in 2012. She has over 20 years experience in general management and strategy consulting roles focused on e-business and media/entertainment in Australia.

She was appointed as an Independent Non-Executive Director of Westpac Banking Corporation in April 2014, of Kikki-K in October 2014 and of Cochlear Limited in January 2015. Alison has also held Chief Executive roles at eBay Australia and New Zealand, eCorp and Hoyts Cinemas.

She is a recipient of the Centenary Medal for services to the business community.

Directorships of other listed companies held in the past three years:

- Cochlear Limited, since 1 January 2015; and
- Westpac Banking Corporation, since 1 April 2014.

### HUGH (HA) FLETCHER

**BSc/BCom, MCom (Hons), MBA, age 68 - Independent Non-Executive Director**

INSURANCE INDUSTRY EXPERIENCE

Hugh Fletcher was appointed as a Director of IAG on 1 September 2007 and Chairman of IAG New Zealand Limited on 1 September 2003. He is a member of IAG's Audit Committee, Risk Committee and Nomination Committee.

Hugh was formerly Chairman (and Independent Director since December 1998) of New Zealand Insurance Limited and CGNU Australia.

OTHER BUSINESS AND MARKET EXPERIENCE

Hugh is a Non-Executive Director of Rubicon Limited and Vector Limited and a trustee of The University of Auckland Foundation. Hugh was formerly Chief Executive Officer of Fletcher Challenge Limited, a New Zealand headquartered corporation with assets in the global building, energy, forestry and paper industries. He retired from an Executive position in December 1997 after 28 years as an Executive, 11 of which he served as Chief Executive.

Hugh is a former Deputy Chairman of the Reserve Bank of New Zealand, former member of the Asia Pacific Advisory Committee of the New York Stock Exchange, former Non-Executive Director of Fletcher Building Limited, and has been involved as an Executive and Non-Executive Director in many countries in Asia, including China, India, Singapore, Indonesia, Malaysia and Thailand.

Directorships of other listed companies held in the past three years:

- IAG Finance (New Zealand) Limited (a part of the Group), since 31 August 2008;
- Vector Limited, since 25 May 2007; and
- Rubicon Limited, since 23 March 2001.

### RAYMOND (SKR) LIM

**BEcon, BA, LLM, age 57 - Independent Non-Executive Director**

INSURANCE INDUSTRY EXPERIENCE

Raymond Lim was appointed as a Director of IAG on 1 February 2013. He is a member of IAG's People and Remuneration Committee and Nomination Committee.

OTHER BUSINESS AND MARKET EXPERIENCE

Raymond is Chairman of APS Asset Management and Senior Advisor to the Swire Group. He also serves on several Boards including the GIC Pte Ltd, Hong Leong Finance and Raffles Medical Group. He is an adjunct professor at the Lee Kuan School of Public Policy, National University of Singapore and the Nanyang Centre for Public Administration, Nanyang Technological University, Singapore.

Raymond is a former Cabinet minister in the Singapore Government (2001-2011). Prior to that, he held various senior positions in the financial industry including as a Managing Director of Temasek Holdings, Chief Executive Officer of DBS Vickers Securities and Chief Economist of ABN AMRO Asia Securities.

He is a Rhodes Scholar and has degrees in economics and law from the universities of Adelaide, Oxford and Cambridge.

Directorships of other listed companies held in the past three years:

- None.

**JONATHAN (JON) (JB) NICHOLSON**
**BA, age 60 - Independent Non-Executive Director**
INSURANCE INDUSTRY EXPERIENCE
Jon Nicholson was appointed as a Director of IAG on 1 September 2015. He is a member of IAG's Audit Committee, Risk Committee and Nomination Committee.

OTHER BUSINESS AND MARKET EXPERIENCE
Jon is Non-Executive Chairman of Westpac Foundation, a trustee of Westpac Bicentennial Foundation and a Non-Executive Director of Cape York Partnerships and QuintessenceLabs.

He previously spent eight years with Westpac Banking Corporation, first as Chief Strategy Officer and later as Enterprise Executive. He retired from Westpac in 2014.

Jon's executive career has included senior roles with a variety of financial and corporate institutions, including the Boston Consulting Group. He also held various roles with the Australian government, including Senior Private Secretary to the Prime Minister of Australia (Bob Hawke) and senior positions in the Department of the Prime Minister and Cabinet.

Directorships of other listed companies held in the past three years:
- None.

**TOM (TW) POCKETT**
**CA, BCom, age 58 - Independent Non-Executive Director**
INSURANCE INDUSTRY EXPERIENCE
Tom Pockett was appointed as a Director of IAG, effective 1 January 2015. He is Chair of IAG's Audit Committee and a member of the Risk Committee and the Nomination Committee.

OTHER BUSINESS AND MARKET EXPERIENCE
Tom is a Non-Executive Director of Stockland Corporation Limited, a Director of Sunnyfield Independence Association and of O'Connell St Associates. He previously spent over 11 years as Chief Financial Officer and over seven years as Finance Director with Woolworths Limited, and retired from these roles in February 2014 and July 2014 respectively. Tom was a former Director of ALH Group Pty Ltd from 2014 to 2016, Hydrox Holdings Pty Ltd from 2014 to 2016 and Chairman and Director of The Quantium Group Holdings Pty Limited from 2014 to 2016. Tom has also held senior finance roles at the Commonwealth Bank, Lend Lease Corporation and Deloitte.

Directorships of other listed companies held in the past three years:
- Stockland Corporation Limited, since 1 September 2014; and
- Woolworths Limited (2006-2014).

**PHILIP (PJ) TWYMAN**
**BSc, MBA, FAICD, age 72 - Independent Non-Executive Director**
INSURANCE INDUSTRY EXPERIENCE
Philip Twyman was appointed as a Director of IAG on 9 July 2008. He is Chair of IAG's Risk Committee, and a member of the Audit Committee and the Nomination Committee.

Philip was formerly Group Executive Director of Aviva plc, one of the world's largest insurance groups, based in London. He has also been Chairman of Morley Fund Management and Chief Financial Officer of General Accident plc, Aviva plc and AMP Group. While at Aviva plc and its predecessor groups between 1996 and 2004, Philip had executive responsibility for the Group's insurance operations in Asia, Australia, Europe and North America. He has also been responsible for starting and nurturing new insurance businesses in China, India, Indonesia and Hong Kong. Overall, Philip has had over 20 years of both board and executive level general insurance experience.

Philip is on the Boards of Swiss Re in Australia. He was formerly an Independent Non-Executive Director of Perpetual Limited from 2004 to 2012, Medibank Private Limited from 2007 to 2012 and Insurance Manufacturers of Australia Pty Limited, a general insurance underwriting joint venture with RACV Limited from April 2007 to July 2008.

OTHER BUSINESS AND MARKET EXPERIENCE
Philip is also on the Board of Tokio Marine Management (Australasia) Pty Ltd.

Directorships of other listed companies held in the past three years:
- None.

## DIRECTORS WHO CEASED DURING THE FINANCIAL YEAR

- Brian Schwartz was a Director from 1 January 2005 to 31 March 2016;
- Michael Wilkins was a Director from 26 November 2007 to 16 November 2015; and
- Yasmin Allen was a Director from 10 November 2004 to 30 September 2015.

## SECRETARY OF INSURANCE AUSTRALIA GROUP LIMITED

### CHRIS (CJ) BERTUCH

**BEc, LLB, LLM**

Chris Bertuch was appointed Group General Counsel & Company Secretary on 11 May 2011. Prior to joining IAG, he held the position of Group General Counsel & Company Secretary at CSR Limited. Chris joined CSR as a corporate lawyer in 1993 and prior to that was a partner in the law firm Gadens Lawyers in Sydney. He brings to IAG more than 28 years of experience in corporate, commercial and trade practices law and dispute resolution. Chris has also completed the Advanced Management Program at Harvard Business School.

## MEETINGS OF DIRECTORS

The number of meetings each Director was eligible to attend and actually attended during the financial year is summarised below:

| DIRECTOR | BOARD OF DIRECTORS Scheduled | | BOARD OF DIRECTORS Unscheduled | | PEOPLE AND REMUNERATION COMMITTEE | | AUDIT COMMITTEE | | RISK COMMITTEE | | BOARD SUB COMMITTEE | | NOMINATION COMMITTEE | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Total number of meetings held | 8 | | 7 | | 4 | | 4 | | 4 | | 3 | | 2 | |
| | Eligible to attend | Attended | Eligible to attend | Attended | Eligible to attend | Attended | Eligible to attend | Attended | Eligible to attend | Attended | Eligible to attend | Attended | Eligible to attend | Attended |
| Elizabeth Bryan[(a)] | 8 | 8 | 7 | 6 | 4 | 4 | - | - | 3 | 3 | 1 | 1 | 2 | 2 |
| Yasmin Allen[(b)] | 3 | 3 | 2 | 2 | 1 | 1 | 1 | 1 | 1 | 1 | - | - | - | - |
| Alison Deans[(c)] | 8 | 8 | 7 | 7 | 3 | 3 | 1 | 1 | 1 | 1 | - | - | - | - |
| Hugh Fletcher[(d)] | 8 | 8 | 7 | 7 | - | - | 4 | 4 | 4 | 4 | 2 | 2 | - | - |
| Peter Harmer[(e)] | 4 | 4 | 3 | 3 | - | - | - | - | - | - | 1 | 1 | - | - |
| Raymond Lim[(d)] | 8 | 8 | 7 | 5 | 4 | 4 | - | - | - | - | - | - | - | - |
| Jonathan Nicholson[(f)] | 6 | 6 | 7 | 7 | - | - | 3 | 2 | 3 | 3 | - | - | - | - |
| Tom Pockett[(d)] | 8 | 8 | 7 | 7 | - | - | 4 | 4 | 4 | 4 | - | - | - | - |
| Brian Schwartz[(g)] | 6 | 6 | 6 | 6 | 3 | 3 | - | - | - | - | 3 | 3 | 1 | 1 |
| Philip Twyman | 8 | 8 | 7 | 7 | - | - | 4 | 4 | 4 | 4 | - | - | 2 | 2 |
| Michael Wilkins[(h)] | 4 | 4 | 3 | 3 | - | - | - | - | - | - | 2 | 2 | - | - |

(a) Elizabeth Bryan was appointed to the Risk Committee on 18 September 2015.

(b) Yasmin Allen was a member of the Board of Directors until 30 September 2015, the People and Remuneration Committee and Audit Committee until 30 September 2015 and the Risk Committee until 18 September 2015.

(c) Alison Deans was appointed to the People and Remuneration Committee on 18 September 2015 and the Nomination Committee on 5 April 2016. She was a member of the Audit Committee and Risk Committee until 18 September 2015.

(d) Hugh Fletcher, Raymond Lim and Tom Pockett were all appointed to the Nomination Committee on 5 April 2016.

(e) Peter Harmer was appointed to the Board on 16 November 2015 and the Nomination Committee on 5 April 2016.

(f) Jonathan Nicholson was appointed to the Board on 1 September 2015, the Audit Committee and Risk Committee on 18 September 2015, and the Nomination Committee on 5 April 2016.

(g) Brian Schwartz was a member of the Board, People and Remuneration Committee and Nomination Committee until 31 March 2016.

(h) Michael Wilkins was a member of the Board until 16 November 2015.

## PRINCIPAL ACTIVITY

The principal continuing activity of the Group is the underwriting of general insurance and related corporate services and investing activities. The Group reports its financial information under the following business divisions:

| DIVISION | OVERVIEW | PRODUCTS |
|---|---|---|
| Consumer Division (Australia)<br><br>51% of Group gross written premium (GWP) | Consumer insurance products are sold in Australia through branches, call centres, the internet and representatives, under the following brands:<br><br>■ NRMA Insurance in NSW, ACT, Queensland and Tasmania;<br>■ SGIO in Western Australia;<br>■ SGIC in South Australia;<br>■ RACV in Victoria, via a distribution agreement with RACV;<br>■ Coles Insurance nationally, via a distribution agreement with Coles; and<br>■ CGU through affinity and financial institution partnerships and broker and agent channels.<br><br>Consumer Division also includes travel insurance, life insurance, income protection and funeral products which are underwritten by third parties. | Short tail insurance<br>■ Motor vehicle<br>■ Home and contents<br>■ Lifestyle and leisure, such as boat, veteran and classic car and caravan<br>Long tail insurance<br>■ Compulsory Third Party (motor injury liability) |
| Business Division (Australia)<br><br>26% of Group GWP | Business insurance products are sold in Australia through a network of around 2,000 intermediaries, such as brokers, agents, motor dealerships and financial institutions. Business Division is a leading provider of business and farm insurance, and also provides workers' compensation services in every state and territory, except South Australia and Queensland.<br><br>Business Division operates across Australia under the following brands:<br><br>■ CGU Insurance;<br>■ Swann Insurance;<br>■ WFI;<br>■ NRMA Insurance;<br>■ RACV;<br>■ SGIC; and<br>■ SGIO. | Short tail insurance<br>■ Business packages<br>■ Farm and crop<br>■ Commercial property<br>■ Construction and engineering<br>■ Niche, such as consumer credit<br>■ Commercial motor and fleet motor<br>■ Marine<br><br>Long tail insurance<br>■ Workers' compensation<br>■ Professional indemnity<br>■ Directors' and officers'<br>■ Public and products liability |
| New Zealand<br><br>19% of Group GWP | The New Zealand business is the leading general insurance provider in the country in both the direct and broker/agent channels. Insurance products are provided directly to customers primarily under the State and AMI brands, and indirectly through insurance brokers and agents, under the NZI and Lumley Insurance brands. Personal products and simplified commercial products are also distributed through agents and under third party brands by corporate partners, which include large financial institutions. | Short tail insurance<br>■ Motor vehicle<br>■ Home and contents<br>■ Commercial property, motor and fleet motor<br>■ Construction and engineering<br>■ Niche, such as pleasure craft, boat, caravan and travel<br>■ Rural and horticultural<br>■ Marine<br><br>Long tail insurance<br>■ Personal liability<br>■ Commercial liability |
| Asia<br><br>4% of Group GWP | The Group has interests in five general insurance businesses in Asia, which comprises primarily the direct and intermediated insurance business underwritten through subsidiaries in Thailand, Vietnam and Indonesia and the share of the operating result from the investment in associates in Malaysia and India. The businesses offer personal and commercial insurance products through local brands. | |
| Corporate and other | Corporate and other comprises other activities, including corporate services, capital management activity, placement of the Group's reinsurance program, inward reinsurance from associates and all investment activities. | |

# OPERATING AND FINANCIAL REVIEW

## OPERATING RESULT FOR THE FINANCIAL YEAR

IAG has delivered a sound operating performance in the current year. This was achieved in an environment of challenging operating conditions in IAG's core markets in Australia and New Zealand. Pressures on profitability were particularly apparent in commercial markets, from a prolongation of soft conditions, although growing ability to increase rates was evident, particularly in Australia, as the year progressed. Long tail Compulsory Third Party (CTP) profitability (notably in NSW) remained under pressure from the higher frequency of minor severity, legally represented claims.

IAG's short tail personal lines franchises in Australia and New Zealand continued to report strong profitability and sound growth, as they successfully responded to evolving customer behaviours and needs via a full range of customer propositions complemented by digital and new product initiatives. Moderate rate increases have countered modest underlying claims inflation.

Benefits from the integration of the former Wesfarmers business and the implementation of a revised Australian operating model were realised in line with plan, with a pre-tax run rate of $180 million of non-reinsurance benefits met by the conclusion of the financial year.

The contribution from Asia increased, with strong performances from the established businesses in Thailand and Malaysia. Proportional GWP registered growth in excess of 7%. Asia remains an important long term growth option for the Group.

The profit and loss for the current year is inclusive of the first time effects of the whole-of-account quota share and a run-off portfolio reinsurance protection arrangement. Further details of these transactions are outlined below:

### Berkshire Hathaway (BH) Quota Share

IAG entered into a 20% whole-of-account quota share arrangement with BH, commencing 1 July 2015 for a minimum term of ten years. This underpins the strategic relationship with BH announced in June 2015. Since its inception, this agreement has:

- reduced IAG's earnings volatility, via the percentage-based fee BH pays to access IAG's strong core franchise;
- enhanced IAG's underlying margin by approximately 250 basis points;
- lowered IAG's regulatory capital requirement by about $400 million; and
- promoted new and complementary business opportunities.

### Run-off portfolio reinsurance protection

During the second half of the financial year, the Group announced an innovative reinsurance transaction that materially mitigates its exposure to the Canterbury earthquakes and asbestos. This comprises:

- an adverse development cover (ADC) that provides NZ$600 million of protection in excess of NZ$4.4 billion for the February 2011 Canterbury earthquake event. After inclusion of the ADC and applicable risk margin, the February 2011 event is now covered to the extent of NZ$5 billion; and
- a reinsurance arrangement in respect of liability and workers' compensation risks with exposure to asbestos. These primarily relate to policies written by the Australian Business Division in the 1970s and 1980s.

The combination of the overall premium paid and the reinsurance from the asbestos portfolio has resulted in a small net loss, which is recognised in the 'Net corporate expense' line in the management reported results.

### Net profit after tax

The Group's net profit after tax for the financial year was $702 million (2015-$830 million). After adjusting for non-controlling interests, the net profit attributable to shareholders of the Company was $625 million (2015-$728 million). This included:

- a significantly lower contribution from investment income on shareholders' funds, which reflected relatively weak equity market returns;
- a $139 million post-tax charge in respect of accelerated amortisation and impairment of capitalised software assets discussed in further detail in the section below; and
- an approximately $100 million increase in tax expense, following a significantly reduced favourable effect from earthquake related reinsurance recoveries in a lower tax jurisdiction.

Total Gross Written Premium (GWP) of $11,367 million represented a 0.6% reduction compared to the prior year and was consistent with IAG's 'relatively flat' full year guidance. This outcome was characterised by:

- sound growth in short tail personal lines from a mixture of rate and volume, in both Australia and New Zealand;
- flat long tail personal lines GWP in Australia, as volume reduction was offset by necessary rate increases to address claim frequency issues;
- lower commercial lines GWP, driven by lower volumes from the strict application of underwriting disciplines and the effect of lower average rates in soft market conditions; and
- sound growth in Asia, principally in Thailand, which was amplified by a favourable foreign exchange translation effect.

The discussion of operating performance in this section is presented on a management reported basis unless otherwise stated. Management reported results are non-IFRS financial information and are not directly comparable to the statutory results presented in other parts of this Annual Report.

There are two elements of the statutory results for the year that are not expected to be a feature of the Group's future sustainable earnings profile. As a result and to ensure consistency of the reporting of key insurance measures and metrics, these items have been shown in the 'Net corporate expense' line in the management reported view of the current year results. This view is consistent with the approach adopted in IAG's Investor Report.

Reconciliation between the statutory results (IFRS) and the management reported (non-IFRS) results is presented below:

| CONSOLIDATED | STATUTORY RESULTS (IFRS) | RUN-OFF PORTFOLIO REINSURANCE PROTECTION | CAPITALISED SOFTWARE ACCELERATED AMORTISATION AND IMPAIRMENT | MANAGEMENT RESULTS (NON-IFRS PER INVESTOR REPORT) |
|---|---|---|---|---|
| | $m | $m | $m | $m |
| Gross earned premium | 11,411 | - | - | 11,411 |
| Outwards reinsurance premium expense | (3,883) | 700 | - | (3,183) |
| Net earned premium | 7,528 | 700 | - | 8,228 |
| Net claims expense | (4,702) | (695) | - | (5,397) |
| Net commission and underwriting expense | (2,116) | - | - | (2,116) |
| Underwriting profit | 710 | 5 | - | 715 |
| Net investment income on assets backing insurance liabilities | 463 | - | - | 463 |
| Insurance profit before capitalised software accelerated amortisation and impairment | 1,173 | 5 | - | 1,178 |
| Capitalised software accelerated amortisation and impairment | (198) | - | 198 | - |
| Insurance profit | 975 | 5 | 198 | 1,178 |
| Net corporate expense | (18) | (5) | (198) | (221) |
| Net other operating income/(expenses) | (37) | - | - | (37) |
| Profit before income tax | 920 | - | - | 920 |

Outlined below are the adjustments to the reported underwriting and insurance results:

- Run-off portfolio reinsurance protection – as discussed above; and
- Accelerated amortisation and impairment of capitalised software – during the current financial year, a review has been undertaken of the Group's capitalised software platforms in the context of both the growing impact of digital disruption and IAG's commencement of a programme that will significantly simplify its information technology systems in future years. As a result of this review, a reduction in the carrying value of capitalised software expenditure of $198 million pre-tax (2015-nil) has been recognised. The assets have a lower recoverable amount reflecting the rapid changes in technology and the reduced useful life of software assets. The expenses have been recognised within the 'Net corporate expense' line in the management reported results. To aid transparency, this item has been separately identified on the face of the statement of comprehensive income which is provided on page 37 of the Annual Report. The change in capitalised software treatment has no impact on IAG's regulatory capital ratios, as capitalised software is already deducted from regulatory capital. This item has been excluded from cash earnings for determination of the dividend, but included when determining executive long term incentive entitlements.

Unless otherwise stated, the insurance and underwriting profits commentary provided below refers to the Group's management reported results and is non-IFRS financial information.

The guidance provided in Australian Securities and Investments Commission Regulatory Guide 230 'Disclosing non-IFRS financial information' ('RG 230') has been followed when presenting the management reported results.

### Insurance margin

IAG's current year management reported insurance profit of $1,178 million (2015-$1,103 million) was nearly 7% higher than the prior year. Alongside the positive BH quota share effect, the higher reported insurance margin of 14.3% (2015-10.7%) included:

- higher than expected prior period reserve releases of $207 million, equivalent to 2.5% of Net Earned Premium (NEP), up from $167 million (1.6% of NEP) in the prior year;
- net natural peril claim costs of $659 million, which exceeded allowance by $59 million following a higher than originally anticipated loss from the east coast low event in June 2016. This compares to the $1,048 million of natural perils claims costs incurred in the prior year; and
- an adverse credit spread impact of $37 million, compared to a favourable effect of $33 million in the prior year.

The prior period reserve release outcome comprised two distinct and partially offsetting elements:

- higher than expected releases from Australian long tail classes, principally CTP; and
- a NZ$150 million increase to risk margin in respect of the February 2011 Canterbury earthquake event, as recognised in the first half of the 2016 financial year.

### Underlying margin

IAG continued to demonstrate relatively strong underlying profitability in the current year. Aside from the quota share impact, the underlying margin of 14.0% (2015-13.1%) contained:

- strong profitability in short tail personal lines in Australia and New Zealand, but with some adverse impact from increased claim frequency;
- pressure on returns in the equivalent commercial lines markets, reflecting lower volumes and the cumulative effect of past rate reductions;
- ongoing pressure on NSW CTP profitability from elevated claim frequency levels; and
- lower like-for-like expenses, as further benefits from the Wesfarmers integration and revised Australian operating model were realised.

IAG defines its underlying margin as the management reported insurance margin adjusted for:
- net natural peril claim costs less the related allowance for the period;
- reserve releases in excess of 1% of NEP; and
- credit spread movements.

| | **2016** | | 2015 | |
|---|---|---|---|---|
| INSURANCE MARGIN | **$m** | **%** | $m | % |
| Management reported insurance margin* | **1,178** | **14.3** | 1,103 | 10.7 |
| Net natural peril claim costs less allowance | **59** | **0.7** | 348 | 3.3 |
| Reserve releases in excess of 1% of NEP | **(125)** | **(1.5)** | (64) | (0.6) |
| Credit spread movements | **37** | **0.5** | (33) | (0.3) |
| Underlying insurance margin | **1,149** | **14.0** | 1,354 | 13.1 |

* Management reported insurance margin is the insurance profit as a percentage of NEP as disclosed in the Investor Report. Based on the statutory results, the equivalent statutory insurance margin for the current year is 13.0%.

Similar to the management reported results, the underlying insurance margin is a non-IFRS measure that is designed to present, in the opinion of management, the results from ongoing operating activities in a way that best and most appropriately reflects the Group's underlying performance.

### Tax Expense

IAG reported a tax expense of $218 million (2015-$119 million), representing an effective tax rate of 23.7% (2015-12.5%). For 2016, while markedly higher than the prior year, this lower than normal tax rate was largely driven by the favourable resolution of a tax audit associated with IAG's former UK operations. The low tax rate for the prior year was driven by reinsurance recoveries relating to the 2011 Canterbury earthquake events in New Zealand, which were recorded by IAG's reinsurance captive in Singapore.

Other contributory elements reconciling the effective tax rate to the prevailing Australian corporate rate of 30% are:
- differences in tax rates applicable to IAG's foreign operations, principally in New Zealand, Singapore and Malaysia; and
- franking credits generated from IAG's investment portfolio.

It is IAG's expectation that the effective tax rate will revert to a more normal (high 20's) level in future periods.

### Investment income on shareholders' funds

Investment income on shareholders' funds was a profit of $113 million, a decrease of over 51% on the profit of $231 million in the corresponding prior year. This included a relatively weak local equity market performance in the current year, with the broader Australian index (S&P ASX200 Accumulation) delivering a return of 0.6% (2015-5.7%). At 30 June 2016 the weighting to growth assets (equities and alternatives) within shareholders' funds stood at approximately 48% (2015-41%).

## A. CONSUMER DIVISION (AUSTRALIA)

The Consumer Division accounted for 51% of Group GWP and produced a strong underlying margin of 16%. Long tail CTP contributed flat GWP, while its profitability suffered from current accident year claim frequency issues in the NSW market.

### I. Premiums

The Consumer Division's GWP increased by 3.3% to $5,801 million in the current year (2015-$5,614 million), driven by growth in short tail home and motor lines. CTP GWP was relatively flat. Short tail home and motor lines represented approximately 85% of divisional GWP, and grew by 4%. Short tail premium growth was dominated by rate movements, in response to higher claim frequency and repair costs. This was augmented by volume gains in motor, while home volumes were reasonably flat.

The larger established brands generated sound growth in what remained a very competitive environment. While coming off a much smaller base, Coles Insurance continued to record strong double digit growth. The current year also included a small initial contribution from the underwriting of Steadfast personal lines, secured as part of the BH agreement.

### II. Insurance profit

The Consumer Division reported an insurance profit of $805 million, compared to $788 million in the prior year. This equates to a higher reported insurance margin of 19.8% (2015-15.9%), which included:
- enhancement from the BH quota share;
- the benefit of higher reserve releases;
- a reduced negative effect from net natural peril claim costs exceeding the associated allowance; and
- absorption of an adverse credit spread movement of $40 million compared to the prior year.

## B. BUSINESS DIVISION (AUSTRALIA)

The Business Division represented 26% of Group GWP. Strict adherence to underwriting disciplines contributed to lower volumes, while the impact of lower average rates diminished from the end of the first half as modest rate rises were progressively implemented. A slightly lower underlying margin reflected pressures on profitability that were not fully offset by the realisation of further synergies from the Wesfarmers integration and the favourable quota share effect.

### I. Premiums
The Business Division reported GWP of $2,979 million, representing a contraction of 6.7% compared to the prior financial year (2015-$3,192 million) due to tough commercial market conditions. Retention levels were consistent through the year across most portfolios, with overall GWP reflecting lower average rates, reduced new business volumes, strong competition in property and strata, tough market conditions in workers' compensation and specific business transfers.

In the face of the prolonged soft market conditions, the Business Division has maintained its strict underwriting discipline through targeted portfolio reviews. The division has also consolidated its leading position in the Australian commercial insurance market, with retention levels applicable to the acquired former Wesfarmers business remaining within the expected range.

### II. Insurance profit
The Business Division reported a higher insurance profit of $230 million (2015-$93 million). This equates to a reported insurance margin of 10.0% (2015-3.0%).

The higher reported margin reflects the net effect of:

- enhancement from the BH quota share;
- lower net natural peril claim costs;
- higher prior period reserve releases; and
- an adverse credit spread movement of $30 million.

### III. Fee based business
Business Division generates fee income by acting as an agent under both the NSW and Victorian workers' compensation schemes that are underwritten by the respective State governments. A secondary source of fee income is Business Division's interest in authorised representative brokers, via its ownership of National Adviser Services (NAS). Net income from fee based operations was $4 million, compared to $16 million in the previous financial year. The overall reduction partly reflects a revision to the remuneration model in relation to the Victorian scheme.

## C. NEW ZEALAND
New Zealand represented 19% of Group GWP and continued to perform well, registering a strong underlying margin of 16.9%, despite increased pressure on the commercial side of its business. The modest premium growth in direct personal lines was more than offset by the impact of tougher market conditions in the commercial segment.

### I. Premiums
New Zealand's GWP of $2,182 million represented a decrease of 3.7% over the prior year (2015-$2,267 million). The local currency GWP fell by 2.6% from the combination of:

- softer premium rates and volume loss in commercial lines, in the face of increased industry capacity; and
- partially offsetting GWP growth in the private motor vehicle portfolio from a combination of volume and rate increases.

### II. Insurance profit
The New Zealand business produced a lower insurance profit of $135 million in the current year (2015-$216 million). This equates to a reported insurance margin of 8.6% (2015-10.8%) and reflects the combination of:

- enhancement from the BH quota share;
- the NZ$150 million increase to risk margin for the February 2011 earthquake event, as recognised in the first half of the current year;
- increased competition in the commercial lines market, where a continued focus on pricing and underwriting disciplines remained a priority; and
- the realisation of benefits from the Lumley integration, disciplined cost management and continued focus on expense savings.

### III. Canterbury Rebuild
At 30 June 2016 the New Zealand business had completed over NZ$5.7 billion of claim settlements in respect of the Canterbury earthquakes. Approximately 93% of all claims by number had been fully settled at that date. IAG continued to receive new claims from the Earthquake Commission (EQC) over the course of the current year, as they exceeded the EQC cap of NZ$100,000 (plus GST). It is expected that the rebuild component will be largely complete by the end of calendar year 2016. Certain shared properties, newly received over-cap claims from the EQC and claims subject to dispute or litigation may take longer to settle.

As referred above, the Group now has reinsurance protection in place that effectively provides it with cover up to NZ$5 billion in relation to the February 2011 event. This compares to the current reserved position of NZ$4.4 billion, including risk margin.

## D. ASIA
Asia represents an important source of long term growth for IAG, with a presence established in five markets: Thailand, Malaysia, India, Vietnam and Indonesia. During the year, IAG determined not to pursue further investment in China. As such, the interest held in Bohai Property Insurance Company Ltd (Bohai) has been transferred to IAG's shareholders' funds investment portfolio.

### I. Divisional result
The division contributed a total profit of $26 million, including shares of associates and allocated costs. This compares to a $21 million profit in the prior financial year, and comprises:

- sound underlying performances by the established businesses in Thailand and Malaysia, where combined profitability increased by over 16% compared to the prior year;
- higher, but still relatively modest, losses from the developing businesses, comprising a similar loss in India compared to the prior year, the absence of earnings from the loan protection run-off portfolio in Vietnam, which consequently moved to a small overall loss and the first time inclusion of a full year's result from Indonesia, which posted a small loss; and
- modestly lower regional support and development costs of $31 million (2015-$32 million).

### II. Controlled entities

GWP from the Group's controlled entities was $386 million, which was an increase of over 9% on the corresponding prior financial year (2015-$353 million), within this:

- the Thai business (Safety Insurance) reported an increase in GWP of 8% to $362 million from $334 million for the prior year, comprising local currency growth of 3% and a favourable foreign exchange translation effect. The GWP movement reflects the combined effect of increased focus on the used car market, improved renewal retention, introduction of a new carbon emission excise tax which adversely affected new car volumes and a softening of rates in the commercial motor and property segments;
- AAA Assurance in Vietnam recorded GWP equivalent to $17 million (2015-$18 million); and
- Parolamas in Indonesia, which was consolidated by IAG from May 2015, recorded GWP equivalent to $7 million (2015-$1 million).

The insurance profit delivered by the controlled entities for the current year was $21 million (2015-$17 million) excluding allocated costs. Within this:

- the Thai business reported an insurance profit of $23 million, compared to $15 million in the corresponding prior year. The increase reflects the combined effects of strong discipline in portfolio management and underwriting controls, the relatively benign claims environment, higher reinsurance-related recoveries and prior period reserve releases and weaker investment income on technical reserves;
- AAA Assurance contributed an insurance loss of $1 million (2015-$2 million profit). The weaker result reflected an increase in the loss ratio in line with the higher mix of motor business and a significantly reduced loan protection business which carries a low expected loss ratio and a higher expense ratio due to increased acquisition costs; and
- Parolamas in Indonesia contributed an insurance loss of $1 million.

### III. Share of net profit/(loss) of associates

The Group's share of associates was a profit of $36 million (2015-$36 million), excluding allocated costs and before amortisation. This result includes AmGeneral Holdings Berhad (AmGeneral) in Malaysia and SBI General Insurance Company Limited (SBI General) in India. AmGeneral accounts for the majority of the Group's share of net profit from associates. IAG's share of AmGeneral's profit for the current year increased marginally to $40 million (2015-$39 million) and reflected a combined effect of favourable prior period reserve releases, adverse impact of non-claimable input tax expenses associated with GST implementation and higher business acquisition costs reflecting intense market competition.

## E. CORPORATE AND OTHER

A pre-tax loss of $282 million was reported, which compares to a loss of $189 million in the corresponding prior year. This primarily reflects the $198 million non-cash accelerated amortisation and impairment charge on capitalised software assets as referenced above.

Further details on the operating segments are set out in note 1.3 segment reporting within the Financial Statements.

## REVIEW OF FINANCIAL CONDITION

## A. FINANCIAL POSITION

The total assets of the Group as at 30 June 2016 were $30,030 million compared to $31,402 million at 30 June 2015. Movements within the overall decrease of $1,372 million include:

- a decrease in investments of $2,589 million from the funds outflow associated with the run-off portfolio reinsurance protection placement, net settlements on the BH quota share, payment of the 2015 final dividend and 2016 interim and special dividends, claim payments from natural peril events and New Zealand earthquake claims partially offset by sound operating performance for the year and the net proceeds received from the issue of the NZD convertible notes;
- reinsurance and other recoveries on outstanding claims has increased by $976 million, predominantly relating to the run-off portfolio reinsurance protection placement and recoveries relating to the BH Quota share; and
- a decrease in goodwill and intangible assets of $151 million primarily as a result of the reduction in the carrying value of capitalised software expenditure following a review of the Group's software platforms as described in note 5.1 goodwill and intangible assets.

The total liabilities of the Group as at 30 June 2016 were $23,245 million compared to $24,384 million at 30 June 2015. The decrease in liabilities of $1,139 million is mainly attributable to:

- a decrease in outstanding claims liability of $946 million predominantly due to claim settlements relating to the prior financial year natural peril events and the New Zealand earthquakes; and
- an increase in interest bearing liabilities relating to the issuance of NZ$350 million of unsecured subordinated convertible notes in June 2016; partially offset by the take up on the re-investment offer in respect of existing 2011 unsecured subordinated bond holders.

IAG shareholders' equity (excluding non controlling interests) decreased from $7,018 million at 30 June 2015 to $6,785 million at 30 June 2016, reflecting the combined effect of:

- a sound earnings performance for the year, resulting in a net profit attributable to shareholders of $625 million; and
- payment of the final 2015 dividend and 2016 interim and special dividends totalling $948 million.

**B. CASH FROM OPERATIONS**

The net cash outflows from operating activities for the year ended 30 June 2016 were $1,946 million compared to net cash inflows of $698 million for the prior corresponding year. The movement is mainly attributable to the net effect of:

- an increase in claim costs paid of $711 million, mainly attributable to the settlement of various natural peril events that occurred in the 2015 financial year. The overall quantum of natural peril losses in that year was unusually high;
- an increase in outwards reinsurance premium expense paid of $2,602 million which predominantly relates to the BH quota share and the run-off portfolio reinsurance protection placement; partially offset by
- an increase in reinsurance and other recoveries received of $232 million, primarily attributable to the BH quota share; and
- an increase in other operating receipts of $698 million in respect of cost recoveries under the BH quota share.

**C. INVESTMENTS**

The Group's investments totalled $12.9 billion as at 30 June 2016, excluding investments held in joint ventures and associates, with over 67% represented by the technical reserves portfolio. Total investments at 30 June 2015 were $15.5 billion. Movements of note since 30 June 2015 are:

- reduced technical reserves as the 20% BH quota share serves to progressively reduce related insurance liabilities;
- increased funds reflecting the sound operating performance of the Group during the year; and
- significant dividend payments in October 2015 ($389 million) and March 2016 ($559 million).

As at 30 June 2016, the Group's overall investment allocation remains conservatively positioned and the credit quality of the investment book remains strong, with 77% (2015-81%) of the fixed interest and cash portfolio rated in the 'AA' category or higher.

Technical reserves as at 30 June 2016 accounted for $8.7 billion (2015-$11.0 billion) of the Group's investments, and were invested in fixed interest and cash.

The Group's allocation to growth assets was 48% of the $4.2 billion of shareholders' funds at 30 June 2016 (2015-41%). Included within the Group's allocation to growth assets are Australian and international equities and alternative investments.

**D. INTEREST BEARING LIABILITIES**

The Group's interest bearing liabilities stood at $1,962 million at 30 June 2016, compared to $1,762 million at 30 June 2015. The net increase of $200 million is explained by:

- the issue of NZ$350m of unsecured subordinated convertible notes in June 2016; and
- a NZ$138 million reduction in outstanding 2011 subordinated fixed rate bonds, following acceptance of a re-investment offer in respect of the new issue.

**E. CAPITAL MIX**

The Group measures its capital mix on a net tangible equity basis, i.e. after deduction of goodwill and intangibles, giving it strong alignment with regulatory and rating agency models. It is IAG's intention to have a capital mix in the following ranges over the longer term:

- ordinary equity (net of goodwill and intangibles) 60-70%; and
- debt and hybrids 30-40%.

At 30 June 2016, the Group's capital mix was within the targeted range, with debt and hybrids representing 36.8% (2015-33.8%) of total tangible capitalisation.

**F. CAPITAL MANAGEMENT**

The Group remains strongly capitalised under APRA's Prudential Standards, with regulatory capital of $4,619 million at 30 June 2016 (2015-$4,785 million). The Group has set the following related targeted benchmarks:

- a total capital position equivalent to 1.4 to 1.6 times the Prescribed Capital Amount (PCA), compared to a regulatory requirement of 1.0 times; and
- a Common Equity Tier 1 (CET1) target range of 0.9 to 1.1 times the PCA, compared to a regulatory requirement of 0.6 times.

At 30 June 2016, the Group had a PCA multiple of 1.72 (2015-1.70) and a CET1 multiple of 1.06 (2015-1.14).

Further capital management details are set out in note 3.1 risk and capital management within the Financial Statements.

## STRATEGY

**A. STRATEGIC PRIORITIES**

- At IAG, our purpose is to make your world a safer place.
- IAG's opportunity is to embrace innovation: The way we live our lives is changing at a rapid pace driven by new technologies and shifting demographic trends. This means our customers are faced with new challenges and opportunities every day. IAG will help them navigate through this journey and present them with innovation to make their lives safer and better. IAG will embrace the change and participate in making things better for our customers, whether in Australia, New Zealand or Asia.
- Our objective is to deliver world class customer experiences: All the elements of our strategy are driven by the customer and their needs – to make their lives easier and safer, to improve their interactions with IAG and make the company as successful as possible to reinvest in our leadership position.

IAG's purpose means that whether you are a customer, partner, employee, shareholder or part of the communities IAG serves across Australia, New Zealand or Asia, IAG exists to 'make your world a safer place'. IAG believes its purpose will enable it to become a more sustainable business over the long term, and deliver stronger and more consistent returns for its shareholders.

### Strategic framework

To fulfil its purpose, IAG is focusing on two key strategic themes:

- Leading the change that its customers need and demand. IAG is embracing innovation, to help customers navigate through change to make their lives safer and better. This has the company's customers at its core, and aims to make the experiences they have with IAG world class, through technology and smart ideas, at each individual interaction.
- Fuelling the business so that it can deliver on these opportunities. To fuel the investments in its continued leadership, IAG needs to be leaner and more responsive. This involves tackling necessary changes to the way IAG operates – simplifying processes and systems, and optimising resources, to be more efficient.

## B. BUSINESS RISK AND RISK MANAGEMENT

Managing risk is central to the sustainability of IAG's business, its purpose and delivery of value to shareholders. IAG uses an enterprise approach to risk and its risk management framework is a core part of the governance structure and includes internal policies, key management processes and culture. The Risk Management Strategy (RMS) is reviewed annually or as required by the Risk Committee (RC) before being recommended for approval by the Board. IAG's risk and governance function provides regular reports to the RC on the operation of IAG's risk management framework, the status of key risks, risk and compliance incidents and risk framework changes. IAG's Internal Audit function provides reports to the Audit Committee (AC) on significant audit findings and other audit related matters.

Roles and responsibilities of the Board and its standing committees, the AC, the RC, the People and Remuneration Committee (PARC) and the Nominations Committee, are set out in the Corporate Governance section of the IAG website.

The Group is exposed to multiple risks relating to the conduct of its general insurance business. The following risks noted below are not meant to represent an exhaustive list, but the risks faced by the Group that have been identified in IAG's RMS:

- strategic risk: the risk of not achieving corporate or strategic goals;
- insurance risk: the risk that the Group is exposed to financial loss, as a result of inadequate or inappropriate underwriting, inadequate or inappropriate product pricing, unforeseen, unknown or unintended liabilities that may eventuate, inadequate or inappropriate claims management including reserving or insurance concentration risk (i.e. by locality, segment or distribution);
- reinsurance risk: the risk of insufficient or inappropriate reinsurance coverage, inadequate underwriting and pricing of reinsurance exposures retained by IAG's reinsurance captives, inadequate or inappropriate reinsurance recovery management, reinsurance arrangements not legally binding and reinsurance concentration risk;
- financial risk: the risk of inadequate liquidity, adverse movements in market prices (equities, derivatives, interest rates, foreign exchange, etc) or inappropriate concentration within investment funds, a counterparty failing to meet its obligations and/or inappropriate capital management; and
- operational risk: the risk of loss from inadequate or failed internal processes, people, systems and/or external events.

A disciplined approach to risk management has been adopted and IAG believes this approach provides the greatest long term likelihood of being able to meet the objectives of all stakeholders, including policyholders, lenders, regulators and shareholders.

Detail of the Group's overall risk management framework, which is outlined in the RMS, is set out in note 3.1 risk and capital management within the Financial Statements and in the Corporate Governance Statement, which is available at www.iag.com.au/about-us/corporate-governance.

## C. ECONOMIC, ENVIRONMENTAL AND SOCIAL SUSTAINABILITY RISK

As a general insurer that operates in Australia, New Zealand and throughout Asia, IAG is exposed to economic, environmental and social sustainability risks and opportunities. The IAG Board has overarching responsibility for these areas, which are managed under shared value and sustainability. Performance and risk management is formally reported to the Board twice a year, with ad-hoc updates as required. A cross-functional Shared Value Advisory Council (SVAC) was established in 2014 to fulfil the role of a sustainability committee for IAG and provides advice and input to the organisation's approach to shared value, sustainability and broader community activity. The SVAC meets every 2-3 months, is chaired by the Group Executive Office of the CEO, and is comprised of Senior Leaders from across the business, including the Group Executive for People, Performance and Reputation and the Chief Customer Officer.

The Group has in place a shared value framework that guides decision making and ensures value is being created for both the community and IAG. This framework defines eight focus areas that support our commitment to help make communities Safer, Stronger and More Confident. The Group's sustainability performance is managed within this framework and supported by a number of policies and position statements.

IAG is a signatory to a number of voluntary principles-based frameworks which guide the integration of environmental, social and governance (ESG) considerations into our business practices. These include the United Nations Environment Program Finance Initiative (UNEPFI), Principles for Sustainable Insurance (PSI) and Principles for Responsible Investment (PRI). IAG is also a signatory of the Geneva Association's Climate Risk Statement.

Details of the Group's management of Economic, Environmental and Social Sustainability Risk are outlined in Principle 7.4 of the Corporate Governance Statement, which is available on the IAG website. More detail on IAG's shared value and sustainability performance is outlined in the 2016 Annual Review and Sustainability Report, which is available at www.iag.com.au/shared-value.

## CORPORATE GOVERNANCE

IAG is committed to attaining the highest level of corporate governance to ensure the future sustainability of the organisation and to create long term value for its shareholders. To achieve this, IAG aspires through its spirit to be closer, braver and faster in all its interactions with customers, partners and shareholders, and actively monitors corporate culture.

IAG's Corporate Governance Statement has been approved by the Board. For the financial year ended 30 June 2016, IAG has complied with the Australian Securities Exchange Corporate Governance Council Principles and Recommendations (3rd edition) and is compliant as at 19 August 2016. Further details on IAG's corporate governance practices and the Corporate Governance Statement are available at www.iag.com.au/about-us/corporate-governance.

## OUTLOOK

IAG's GWP growth for the year ended 30 June 2017 is expected to remain relatively flat. The Group's reported margin guidance for the year ended 30 June 2017 is expected to be in the range of 12.5-14.5%. Underlying assumptions behind the reported margin guidance are:

- net losses from natural perils in line with an allowance of $680 million (2016-$600 million);
- prior period reserve releases of at least 1% of NEP; and
- no material movement in foreign exchange rates or investment markets.

## DIVIDENDS

Details of dividends paid or determined to be paid by the Company and the dividend policy employed by the Group are set out in the note 4.4 dividends within the Financial Statements.

Cash earnings are used for the purposes of targeted ROE and dividend payout policy and are defined as:

- net profit after tax attributable to IAG shareholders;
- plus amortisation and impairment of acquired identifiable intangibles; and
- excluding any unusual items (non-recurring in nature).

| CASH EARNINGS | **2016 $m** | 2015 $m |
|---|---|---|
| Net profit after tax | **625** | 728 |
| Acquired intangible amortisation and impairment | **57** | 150 |
| | **682** | 878 |
| **Non-recurring items:** | | |
| Corporate expenses | **221** | 155 |
| Tax effect on corporate expenses | **(36)** | (46) |
| Cash earnings* | **867** | 987 |
| Interim dividend | **316** | 304 |
| Final dividend | **316** | 389 |
| Dividend payable | **632** | 693 |
| Cash payout ratio* | **72.9%** | 70.2% |

* Cash earnings and cash payout ratio represent non-IFRS financial information.

IAG has revised its full year dividend payout policy to pay dividends equivalent to approximately 60–80% (30 June 2015-50-70%) of reported full year cash earnings in respect of any given financial year.

The Board has determined to pay a fully franked final dividend of 13.0 cents per ordinary share (cps) (2015-16.0 cps), bringing the full year dividend to 26 cps (2015-29 cps). In addition, IAG has paid a special fully franked dividend of 10.0 cents per ordinary share in March 2016. The final dividend is payable on 5 October 2016 to shareholders registered as at 5pm on 7 September 2016. The Company's Dividend Reinvestment Plan (DRP) will operate for the final dividend by acquiring shares on market with no discount applied. The DRP Issue Price will be based on a volume weighted average share price as defined in the DRP terms. The last date for the receipt of an election notice for participation in the Company's DRP is 8 September 2016. Information about IAG's DRP is available at www.iag.com.au/shareholder centre/dividends/reinvestment.

## SIGNIFICANT CHANGES IN STATE OF AFFAIRS

During the financial year the following changes became effective:

- On 16 November 2015, the Board appointed Peter Harmer as Managing Director and CEO. Mr Harmer replaced Michael Wilkins who retired as Managing Director and CEO, but remained in an executive capacity until 31 March 2016.
- New structure and leadership team:
  - Effective 9 December 2015, a new organisational structure and leadership team were announced, to drive the Group's future profitability and growth. Roles and responsibilities of the new leadership team are available on the IAG website.
  - In the Australian market IAG has two customer facing divisions responsible for sales, service, and brand and marketing execution. The Consumer Division focuses on individuals and families, and the Business Division focuses on businesses of all sizes.
  - IAG continues to report its financial results using its four reporting segments: Consumer Division, Business Division, New Zealand and Asia.

- On 16 February 2016, the Board appointed Elizabeth Bryan AM as its Chairman, effective 31 March 2016. Ms Bryan succeeded Brian Schwartz AM, who announced his intention to retire from the Board at the Company's annual general meeting in October 2015.
- On 16 February 2016, IAG completed an innovative reinsurance transaction with BH that mitigates the Group's exposure to the Canterbury earthquakes and asbestos related liabilities. The transaction comprised:
  - an ADC which provides NZ$600 million of protection above NZ$4.4 billion for the February 2011 Canterbury earthquake event; and
  - a reinsurance arrangement in respect of IAG's asbestos portfolio.
- On 15 June 2016, the Company issued NZ$350 million of subordinated convertible term notes. The subordinated notes qualify as Tier 2 Capital under the APRA capital adequacy framework for general insurers.

## EVENTS SUBSEQUENT TO REPORTING DATE

Detail of matters subsequent to the end of the financial year are set out below and in note 7.3 events subsequent to reporting date within the Financial Statements. These include:

- On 19 August 2016, the Board determined to pay a final dividend of 13 cents per share, 100% franked. The dividend will be paid on 5 October 2016. The dividend reinvestment plan will operate by acquiring shares on-market for participants with no discount applied.
- On 19 August 2016, IAG announced, as part of the Group's active capital management program, an off-market share buy-back (via a tender process) of up to $300 million. The share buy-back is expected to represent over 2% of IAG's outstanding issued ordinary share capital. The capital component of the share buy-back is expected to be $2.99 and the balance deemed to be a fully franked dividend. The proceeds of the share buy-back are expected to be dispatched to participating shareholders on 17 October 2016.

## NON-AUDIT SERVICES

During the financial year, KPMG performed certain other services for the Group in addition to its statutory duties.

The Directors have considered the non-audit services provided during the financial year by KPMG and, in accordance with written advice provided by resolution of the AC, are satisfied that the provision of those non-audit services by the Group's auditor is compatible with, and did not compromise, the auditor independence requirements of the Corporations Act 2001 for the following reasons:

- all non-audit assignments were approved in accordance with the process set out in the IAG framework for engaging auditors for non-audit services; and
- the non-audit services provided do not undermine the general principles relating to auditor independence as set out in APES 110 Code of Ethics for Professional Accountants of the Chartered Accountants Australia and New Zealand and CPA Australia, as they did not involve reviewing or auditing the auditor's own work, acting in a management or decision making capacity for the Company, acting as an advocate for the Company or jointly sharing risks and rewards.

The level of fees for total non-audit services amounted to approximately $1.5 million (refer to the note 8.3 remuneration of auditors for further details of costs incurred on individual non-audit assignments).

## LEAD AUDITOR'S INDEPENDENCE DECLARATION UNDER SECTION 307C OF THE CORPORATIONS ACT 2001

The lead auditor's independence declaration is set out on page 35 and forms part of the Directors' Report for the year ended 30 June 2016.

## INDEMNIFICATION AND INSURANCE OF DIRECTORS AND OFFICERS

The Company's constitution contains an indemnity in favour of every person who is or has been:

- a Director of the Company or a subsidiary of the Company; or
- a Secretary of the Company or of a subsidiary of the Company; or
- a person making or participating in making decisions that affect the whole or a substantial part of the business of the Company or of a subsidiary of the Company; or
- a person having the capacity to affect significantly the financial standing of the Company or of a subsidiary of the Company.

The indemnity applies to liabilities incurred by the person in the relevant capacity (except a liability for legal costs). That indemnity also applies to legal costs incurred in defending or resisting certain legal proceedings. The indemnity does not apply where the Company is forbidden by statute or, if given, would be made void by statute.

In addition, the Company has granted deeds of indemnity to certain current and former Directors and Secretaries and members of senior management of the Company and its subsidiaries and associated companies. Under these deeds, the Company:

- indemnifies, to the maximum extent permitted by law, the former or current Directors or Secretaries or members of senior management against liabilities incurred by the person in the relevant capacity. The indemnity does not apply where the liability is owed to the Company or any of its subsidiaries or associated companies, or (in general terms) where the liability arises out of a lack of good faith, wilful misconduct, gross negligence, reckless misbehaviour or fraud; and
- is also required to maintain and pay the premiums on a contract of insurance covering the current or former Directors or members of senior management against liabilities incurred in respect of the relevant office except as precluded by law. The insurance must be maintained until the seventh anniversary after the date when the relevant person ceases to hold office. Disclosure of the insurance premiums and the nature of liabilities covered by such insurance are prohibited by the relevant contract of insurance.

# REMUNERATION REPORT
## LETTER FROM THE PEOPLE AND REMUNERATION COMMITTEE CHAIRMAN

Dear Shareholder

IAG is pleased to present its Remuneration Report for the year ended 30 June 2016.

The People and Remuneration Committee (PARC) reaffirms its commitment to delivering remuneration outcomes that reflect both business performance and shareholder returns, as well as ensuring IAG is able to continue to attract and retain high quality executives.

Throughout the year the business strategy has evolved, and remuneration frameworks continue to support the changing needs of the business. The overall organisation results are reflected in the remuneration outcomes received by Executives.

The following table provides a summary of some key highlights for the year ended 30 June 2016:

| CURRENT YEAR HIGHLIGHTS | SUMMARY |
|---|---|
| A new leadership team was appointed | In November 2015, Peter Harmer was appointed as Group CEO and in December 2015 Peter appointed his new Executive team. |
| Fixed pay supports IAG's remuneration principles | The fixed pay for the newly appointed Executive team reflects their experience in the relevant roles, as well as internal and external benchmarks. This supports key principles underpinning IAG's remuneration framework of aligning remuneration to the incumbent's skill and experience, internal relativities of IAG's Executive team and external roles to remain market competitive.<br><br>As a result of difficult market conditions, it was determined by PARC in August 2015 that no fixed pay increases would be provided to our Executive team over the 2016 financial year other than where there was a change in role. |
| Short term performance was sound | In the 2016 financial year, IAG undertook significant changes designed to set up the organisation for continuous growth and profitability into the future. Whilst these changes impacted leadership teams, operating models and organisational structures, IAG's short term business performance remained sound. The business maintained a stable market position, continued to perform well at an underlying level and IAG has received some notable recognition for its leadership in the industry.<br><br>Reflective of the business' short term performance, the average Short Term Incentive (STI) payment was 67% of the maximum achievable for the Executive team. |
| IAG focuses Executives on being Closer, Braver, Faster | The IAG Spirit was introduced in the current financial year and encompasses what is important to IAG; how we serve our customers, partners, shareholders, communities and each other. The IAG Spirit is measured through an individual's commitment and demonstrated behaviour to display IAG's core values of Closer, Braver, Faster.<br><br>To align Executive behaviours with the IAG Spirit, eligibility for a STI payment is now dependent on demonstrating the IAG Spirit. |
| IAG delivers sustained long term performance | IAG once again achieved strong returns, with full vesting of the Return on Equity (ROE) portion of the LTI. IAG ranked at the 52nd percentile of its peer group and achieved 54% vesting of the Total Shareholder Return (TSR) component of the Long Term Incentive (LTI). |
| ROE vesting schedule adjusted to align to market practice | A review was conducted during the 2016 financial year to assess the appropriateness of our LTI performance hurdles. The review confirmed that TSR and ROE continue to appropriately align Executives with IAG's three to four year aspirations, and consequently the current performance hurdles will remain in place for the 2016 LTI awards. The PARC has determined that a more detailed review of the ROE hurdle will take place prior to the 2017 awards to ensure it continues to drive the desired outcomes for shareholders. |
| Shareholder interests are aligned through a mandatory shareholding requirement | As part of IAG's philosophy of aligning the interests of Executive and Non Executive Directors (NEDs) with those of shareholders, all Executive and NEDs are required to hold a proportion of their remuneration as IAG shares. All Executives and NEDs who were required to meet their mandatory shareholding requirement at 30 June 2016 have done so. |
| Review of Balanced Scorecard for the 2017 financial year | IAG is currently undertaking a review of its Executive Remuneration Framework. As part of this review, the incorporation of a Net Promoter Score (NPS) into the balanced scorecard is currently under consideration. A NPS measure focuses Executives' efforts on earning and sustaining loyal customers and vocal promoters of the business, by nurturing a business culture which IAG customers can believe in and rely upon. |

IAG is committed to ensuring the Remuneration Report presents executive remuneration in a consistent, concise and simple manner, as well as complying with the Corporations Act 2001. As in previous years, in this report the Company voluntarily discloses the actual remuneration received by Executives, in addition to meeting our statutory reporting obligations.

The People and Remuneration Committee are confident that IAG's remuneration framework supports the Group's financial and strategic goals now and into the future.

Yours sincerely

**Elizabeth Bryan AM**
Chairman - People and Remuneration Committee

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|---|---|---|


**A. KEY MANAGEMENT PERSONNEL COVERED IN THIS REPORT**

This report sets out the remuneration details of IAG's KMP as listed below:

| NAME | POSITION | TERM AS KMP[(a)] |
|---|---|---|
| **Executives** | | |
| Peter Harmer[(b)] | Managing Director and Chief Executive Officer | Full year |
| Julie Batch | Chief Customer Officer | From 8 December 2015 |
| Chris Bertuch | Group General Counsel & Company Secretary | From 8 December 2015 |
| Ben Bessell | Chief Executive, Australian Business Division | Full year |
| Duncan Brain | Chief Executive, Asia | Full year |
| David Harrington | Group Executive, Office of the CEO | From 8 December 2015 |
| Nicholas Hawkins | Chief Financial Officer | Full year |
| Jacki Johnson[(c)] | Group Executive, People, Performance & Reputation | Full year |
| Anthony Justice | Chief Executive, Australian Consumer Division | From 8 December 2015 |
| Mark Milliner | Chief Operating Officer | From 27 April 2016 |
| Craig Olsen | Chief Executive, New Zealand | From 1 January 2016 |
| Claire Rawlins | Group Executive, Digital & Technology | From 8 December 2015 |
| Clayton Whipp | Chief Risk Officer | Full year |
| **Executives who ceased as key management personnel** | | |
| Michael Wilkins | Managing Director and Chief Executive Officer | Ceased 16 November 2015 |
| Andy Cornish[(d)] | Acting Chief Operating Officer | Ceased 27 April 2016 |
| Alex Harrison | Chief Executive, Enterprise Operations | Ceased 31 August 2015 |
| Leona Murphy | Chief Strategy Officer | Ceased 31 December 2015 |
| **Non-Executive Directors** | | |
| Elizabeth Bryan[(e)] | Chairman, Independent Non-Executive Director | Full year |
| Alison Deans | Independent Non-Executive Director | Full year |
| Hugh Fletcher | Independent Non-Executive Director | Full year |
| Raymond Lim | Independent Non-Executive Director | Full year |
| Jonathan Nicholson | Independent Non-Executive Director | From 1 September 2015 |
| Tom Pockett | Independent Non-Executive Director | Full year |
| Philip Twyman | Independent Non-Executive Director | Full year |
| **Non-Executive Directors who ceased as key management personnel** | | |
| Brian Schwartz | Chairman, Independent Non-Executive Director | Ceased 31 March 2016 |
| Yasmin Allen | Independent Non-Executive Director | Ceased 30 September 2015 |

(a) All remuneration is disclosed from the date the individual was appointed as a KMP (ie. their contract commencement date) to the date of cessation.

(b) Peter Harmer held the position of Chief Digital Officer until 31 July 2015, then Chief Executive IAG Labs until 16 November 2015. He commenced as Managing Director and Chief Executive Officer on 16 November 2015.

(c) Jacki Johnson held the position of Chief Executive, New Zealand until 31 December 2015. She commenced as Group Executive, People, Performance and Reputation on 1 January 2016.

(d) Andy Cornish held the position of Chief Executive Personal Insurance up to 8 December 2015 and acting Chief Operations Officer until 27 April 2016. He ceased employment on 1 July 2016. His termination benefits are disclosed in the current financial year.

(e) Elizabeth Bryan held the position of Deputy Chairman from 5 December 2014 until 31 March 2016, when she commenced as Chairman.

Key terms that are used throughout the report are defined in detail in section J key terms and definitions.

## B. 2016 SNAPSHOT

### I. Actual remuneration received by Executives

For remuneration details provided in accordance with the Accounting Standards refer to section G Statutory remuneration disclosure requirements.

TABLE 1 - ACTUAL REMUNERATION RECEIVED IN 2016 AND 2015

| NAME | FINANCIAL YEAR | FIXED PAY $000 | OTHER BENEFITS AND LEAVE ACCRUALS $000 (1) | TERMINATION BENEFITS $000 (2) | CASH STI $000 | DEFERRED STI VESTED $000 (3) | LTI VESTED $000 (4) | TOTAL ACTUAL REMUNERATION RECEIVED $000 |
|---|---|---|---|---|---|---|---|---|
| **EXECUTIVES** | | | | | | | | |
| Peter Harmer | **2016** | **1,460** | **70** | **-** | **905** | **311** | **1,428** | **4,174** |
| | 2015 | 1,012 | (23) | - | 473 | 432 | 2,152 | 4,046 |
| Julie Batch | **2016** | **343** | **34** | - | **153** | **-** | **-** | **530** |
| Chris Bertuch | **2016** | **400** | **33** | - | **138** | **-** | **-** | **571** |
| Ben Bessell | **2016** | **686** | **31** | **-** | **271** | **83** | **161** | **1,232** |
| | 2015 | 123 | (7) | - | 65 | - | - | 181 |
| Duncan Brain | **2016** | **934** | **261** | **-** | **532** | **154** | **273** | **2,154** |
| | 2015 | 921 | 263 | - | 469 | 210 | 429 | 2,292 |
| David Harrington | **2016** | **346** | **33** | - | **160** | **-** | **-** | **539** |
| Nicholas Hawkins | **2016** | **1,026** | **(48)** | **-** | **593** | **318** | **1,428** | **3,317** |
| | 2015 | 1,012 | 56 | - | 603 | 463 | 2,198 | 4,332 |
| Jacki Johnson[5] | **2016** | **1,053** | **92** | **-** | **585** | **252** | **1,286** | **3,268** |
| | 2015 | 1,096 | (43) | - | 418 | 398 | 1,949 | 3,818 |
| Anthony Justice | **2016** | **372** | **(6)** | - | **156** | **-** | **-** | **522** |
| Mark Milliner | **2016** | **181** | **20** | - | **-** | **-** | **-** | **201** |
| Craig Olsen[6] | **2016** | **330** | **36** | - | **124** | **-** | **-** | **490** |
| Claire Rawlins | **2016** | **341** | **32** | - | **152** | **-** | **-** | **525** |
| Clayton Whipp | **2016** | **784** | **64** | **-** | **415** | **117** | **243** | **1,623** |
| | 2015 | 755 | 64 | - | 341 | 211 | 367 | 1,738 |
| **EXECUTIVES WHO CEASED AS KEY MANAGEMENT PERSONNEL** | | | | | | | | |
| Michael Wilkins | **2016** | **808** | **(46)** | **1,060** | **1,197** | **792** | **3,580** | **7,391** |
| | 2015 | 2,112 | 232 | - | 1,314 | 1,232 | 5,514 | 10,404 |
| Andy Cornish | **2016** | **875** | **49** | **1,086** | **887** | **256** | **1,486** | **4,639** |
| | 2015 | 1,052 | 93 | - | 602 | 469 | 2,290 | 4,506 |
| Alex Harrison | **2016** | **145** | **(6)** | **782** | **-** | **128** | **260** | **1,309** |
| | 2015 | 849 | 51 | - | 611 | 192 | 397 | 2,100 |
| Leona Murphy | **2016** | **466** | **52** | **808** | **410** | **261** | **1,286** | **3,283** |
| | 2015 | 910 | 38 | - | 505 | 411 | 1,981 | 3,845 |

(1) Further details are provided in table 8 in section G Statutory remuneration disclosure requirements.

(2) Includes payment in lieu of notice, redundancy payment and outplacement services.

(3) The deferred STI vesting on 1 September 2015 was valued using the five day weighted average share price $5.14 (1 September 2014: $6.49).

(4) The LTI vested was valued using the five day weighted average share price at vesting date was $5.50 for awards vested on 24 August 2015 and $4.84 for awards vested on 30 September 2015 (20 August 2014: $6.27; 30 September 2014: $6.18).

(5) Remuneration for Jacki Johnson between 1 July 2015 and 1 January 2016 was determined in New Zealand dollars. Full year remuneration is reported in Australian dollars.

(6) Remuneration for Craig Olsen was determined in New Zealand dollars and reported in Australian dollars.

There were no fixed pay increases for Executives during the 2016 financial year except for newly appointed Executives to recognise the increased responsibilities associated with their new roles.

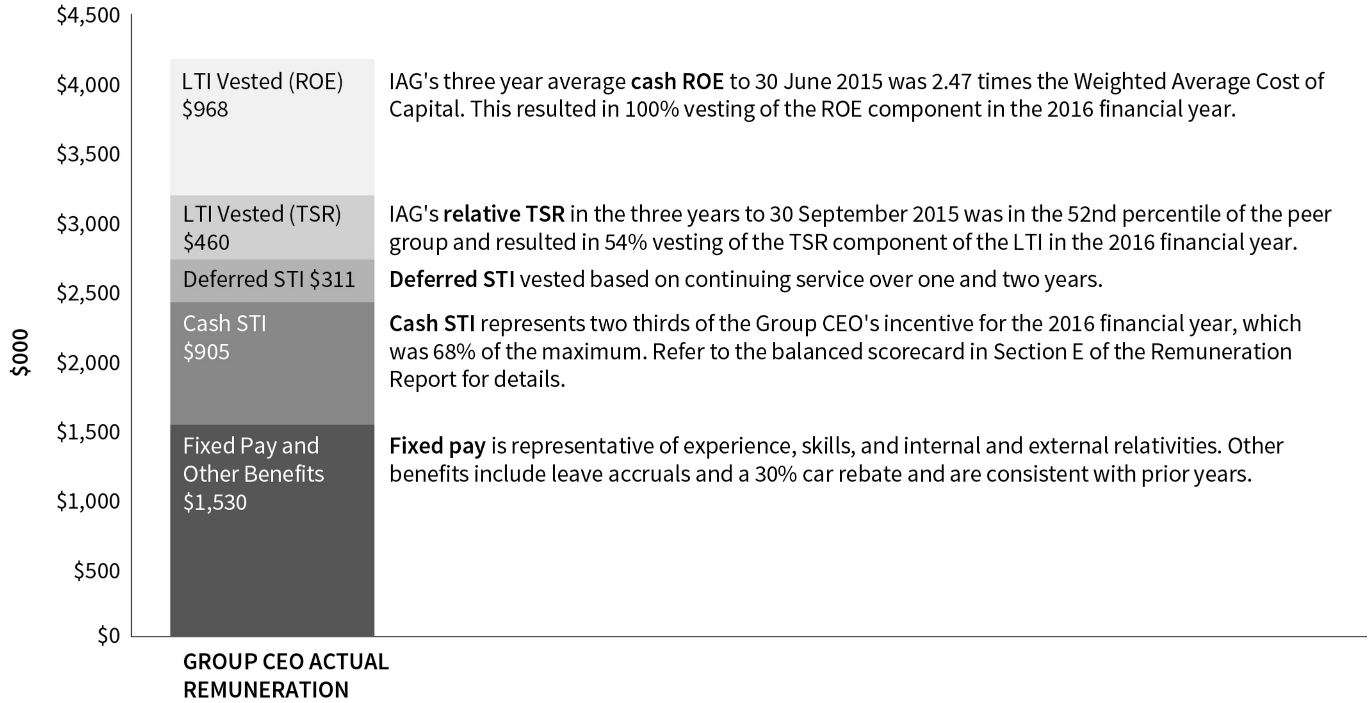
### II. Group CEO remuneration explained

Actual remuneration received is based on the Group's performance over a number of different time periods and is linked explicitly to the performance hurdles and timeframes over which they are achieved.

Using the current Group CEO's remuneration as an example, actual remuneration received has reduced this year from previous years, given the number of rights vested was lower this year than in prior years. This was due to reduced share price movement, TSR performance and no retests occurring for the TSR hurdle.

The following graph illustrates the current Group CEO's remuneration, broken down into the components of his remuneration plan.

**GROUP CEO FY16 PERFORMANCE AND ACTUAL REMUNERATION OUTCOMES**



## C. EXECUTIVE REMUNERATION GOVERNANCE

**BOARD**
Ensures the Group remuneration framework is aligned to the short and long term interests of IAG and its shareholders. Independently considers recommendations made by the PARC before making executive remuneration decisions.

**PARC**
Ensures the remuneration policies and practices support the delivery of IAG's strategic goals.

**Advises the Board on:**
- Group remuneration policy and its effectiveness
- Executive remuneration and contract terms
- IAG Non-Executive Director (NED) remuneration.

**Approves:**
- Exceptions to policy
- Equity-based plans
- Target market positioning
- Annual remuneration reporting
- Subsidiary board NED Remuneration.

**EXTERNAL REMUNERATION CONSULTANTS**
The PARC engages remuneration consultants to provide advice that assists the Board in making remuneration decisions.

**MANAGEMENT**
The Group CEO recommends Executive team remuneration and contract terms to the Board.

Executives may attend PARC meetings, by invitation, to assist the Committee in its deliberations and provide updates on people related strategy and initiatives.

### I. Remuneration guiding principles
IAG's remuneration practices have been designed to achieve the following objectives, being to:
- align remuneration with the interests of IAG's shareholders;
- motivate employees to achieve superior and sustainable performance and discourage underperformance;
- retain market competitiveness to attract and retain high quality people;
- clearly communicate the remuneration policy; and
- encourage constructive behaviours and prudent risk taking that support long term financial soundness.

### II. Use of remuneration consultants
The PARC engaged EY remuneration consultants to provide KMP remuneration benchmarking. The remuneration data provided was used as an input to the remuneration decisions by the Board only. No remuneration recommendations, as defined by the Corporations Act 2001, were provided by EY. The Board considered the data provided, together with other factors, in setting Executives' remuneration.

### III. Adjustment policy
Each year, the Board assesses whether variable remuneration under the Deferred Award Rights (DAR) and Executive Performance Rights (EPR) Plans needs to be adjusted to:
- protect the financial soundness of IAG or an operating segment;
- respond to significant unexpected or unintended consequences that were not foreseen by the Board; or
- respond to other circumstances where the Board determines that an adjustment is necessary, including circumstances where behaviour does not align with a desired risk culture, to ensure that an inappropriate reward outcome does not occur.

In the year ended 30 June 2016, this investigation did not reveal any requirement for the Board to adjust remuneration.

### IV. Mandatory shareholding requirement
The Group CEO is required to accumulate and hold IAG ordinary shares with a value of two times their base salary, and the Executive team one times their respective base salaries. Executives have four financial years from their date of appointment as an Executive to meet their requirement. Holdings are assessed annually at the end of each financial year, using the closing share price at 30 June and the Executive's base salary from four years prior. The shareholding includes Executives' directly held shares and rights vested and unexercised as at 30 June, for entities controlled, jointly controlled or significantly influenced by the Executive. Shares held by the Executives' domestic partner and dependants are not included in the mandatory shareholding requirement calculation. All Executives appointed prior to 30 June 2012 met the mandatory shareholding requirement at 30 June 2016.

## D. EXECUTIVE REMUNERATION STRUCTURE

### I. Summary of remuneration components

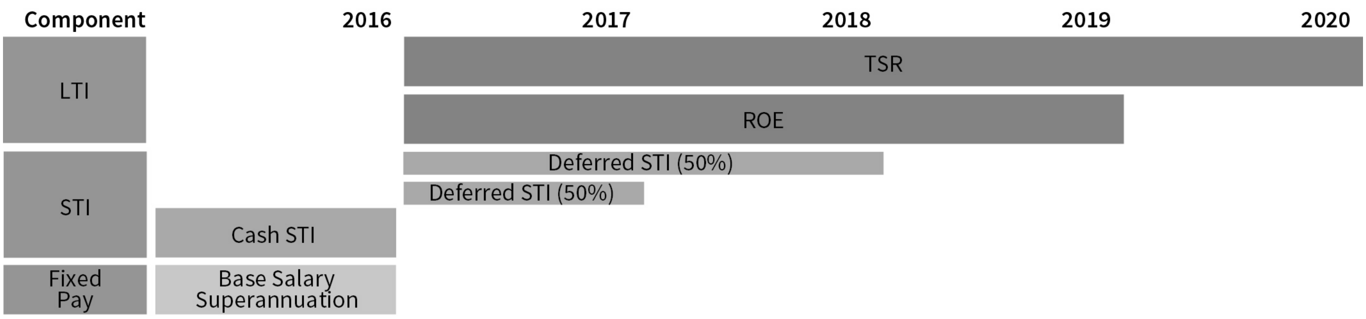
The table below outlines the remuneration components and the strategic objective of each component:

TABLE 2 - REMUNERATION COMPONENTS

| COMPONENT | MEASURE | STRATEGIC OBJECTIVE |
|---|---|---|
| LTI | TSR 50% | TSR provides a direct link between Executive reward and shareholder return by measuring the value created for shareholders through the appreciation of the share price and the value of dividends. |
| | ROE 50% | ROE provides evidence of company profitability and is linked to shareholder return. IAG uses ROE as a key measure of the efficiency of the Group's financial performance. |
| STI | Balanced scorecard | Financial and non-financial measures provide a balance between rewarding the achievement of financial targets and non-financial objectives that drive the execution of IAG's strategy and future growth. |
| Fixed pay | Position description | Fixed pay is market competitive based on the roles' experience, skills, internal relativities of the Executive team and market pay levels of similar external roles. Fixed pay for Australian based Executives is determined by reference to peer groups, including financial services companies in the S&P/ASX 50 Index and companies that are of similar size to IAG. Relevant local market peer groups are referenced for overseas based Executives. |

The remuneration components are structured to reward Executives across different timeframes. The graph below shows the remuneration components and the periods over which performance is assessed:

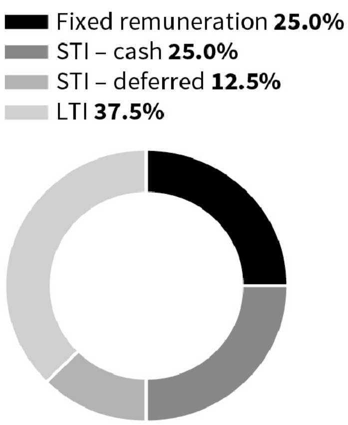
**REMUNERATION COMPONENT TIMEFRAMES**



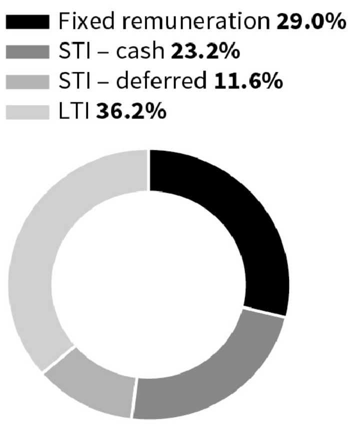

### II. Potential remuneration mix

Total potential remuneration for Executives comprises a mix of fixed pay and maximum potential at-risk remuneration (STI and LTI). The mix, shown in the graph below, is designed to pay Executives competitively based on their performance, while providing strong governance to protect the financial soundness of the business and shareholders' interests.

**POTENTIAL GROUP CEO REMUNERATION MIX**




**AVERAGE POTENTIAL EXECUTIVE TEAM MEMBER REMUNERATION MIX**




Notes:

- Potential remuneration is based on current remuneration at 30 June 2016. STI and LTI are based on maximum opportunities.

### III. At-Risk remuneration

The Board strongly believes that the fundamental driver for executive remuneration should be long term financial performance that generates value for IAG shareholders. The Board further recognises that executive remuneration is guided by regulation and market forces and it regularly reviews IAG's executive remuneration to ensure IAG uses at-risk remuneration components to achieve its remuneration and performance objectives.

#### a. Cash and deferred short term incentive (STI)

Cash and deferred STI is the at-risk remuneration designed to motivate and reward for performance in the financial year. The graph below shows the maximum STI potential, the gateway and the measures that drive the STI outcome for the 2016 financial year:

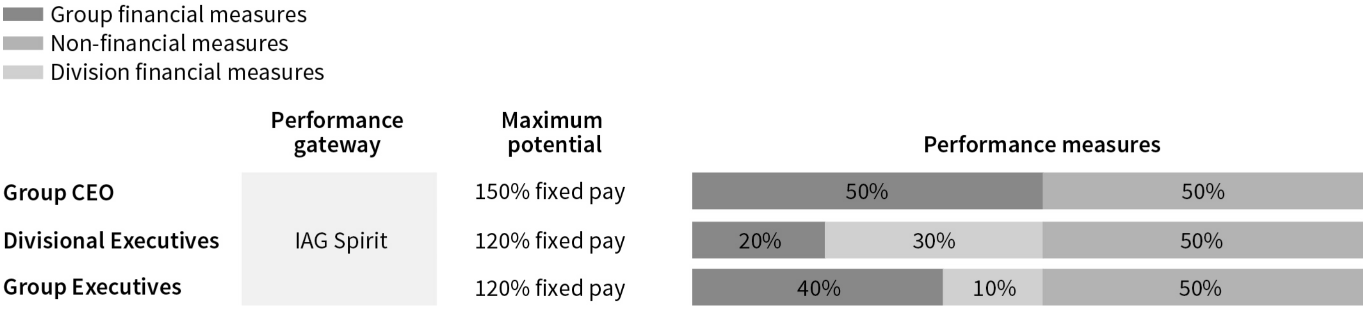



TABLE 3 - STI PLAN

| | |
|---|---|
| Performance gateway | The IAG Spirit describes what is important to IAG; how we serve our customers, partners, shareholders, communities and each other. Eligibility for a STI payment is dependent on demonstrating the IAG Spirit. The IAG Spirit is measured through an individual's commitment and demonstrated behaviour to display IAG's core values of Closer, Braver, Faster. Therefore, if Executives do not demonstrate the behaviours within the IAG Spirit, they will not be eligible for a STI payment. The IAG Spirit gateway is designed to highlight the link between demonstrating the IAG Spirit and the achievement of performance outcomes. |
| Performance measures and evaluation | Performance is measured against a balanced scorecard that uses both financial and non-financial goals (the balanced scorecard is discussed in more detail in table 5). The Group CEO's STI is recommended by the PARC based on their balanced scorecard performance and is approved by the Board.<br><br>The amount of STI paid to members of the Executive team is recommended by the Group CEO to the PARC based on the Executive team members' balanced scorecard performance and subsequently recommended by the PARC for approval by the Board. The Board may apply discretion in determining the STI outcomes to ensure they appropriately reflect an Executive's performance. |
| Instrument | Two-thirds of the STI is paid as cash, with the remaining one third deferred in the form of Deferred Award Rights (DAR) that vest equally over two years. |
| Key terms of the deferred STI | Deferred STI is issued in the form of DAR, which are rights over IAG ordinary shares. They are issued to Executives during the financial year at no cost, to the value of their deferred STI amount. The number of DAR issued is calculated based on the price of an IAG ordinary share at 30 June before the grant date. Executives who participate in this plan become eligible to receive one IAG ordinary share per DAR by paying an exercise price of $1 per tranche of DAR exercised, subject to their continuing employment with the Group for a period determined by the Board. No dividend is paid or payable for any unvested or vested and unexercised DAR. |
| Forfeiture conditions | The Board retains the discretion to adjust downwards the unvested portion of any awards. DAR will be forfeited if the Executive resigns before the vesting date. When an Executive ceases employment in special circumstances, such as redundancy, any unvested rights may be retained on cessation of employment, subject to Board discretion. |

b. Long term incentive (LTI)
LTI grants are determined annually by the Board. The grants are provided in the form of Executive Performance Rights (EPR) with measures aligned to the Group's strategic financial targets. The maximum value of EPR that can be granted to the Group CEO and Executive team members under the LTI plan is 150% and 125% of fixed pay respectively.

TABLE 4 - LTI PLAN

| | RETURN ON EQUITY (ROE) | RELATIVE TOTAL SHAREHOLDER RETURN (TSR) |
|---|---|---|
| Description | ROE - 50% weighting<br><br>Cash return on equity is measured relative to the Group's WACC. | TSR - 50% weighting<br><br>Total shareholder return is measured against that of the top 50 industrials within the S&P/ASX 100 Index. |
| Testing | The ROE portion of the LTI is tested from 1 July of the grant year to 30 June three years later. | The TSR portion of the LTI is tested four years after 30 September of the grant year with no additional opportunity for retesting.<br><br>TSR granted prior to July 2013 is tested after three years and then again at four years and five years. Retesting was removed from subsequent grants of EPR. |
| Vesting | 0% vesting <1.2 x WACC<br><br>20% vesting at 1.2 x WACC<br><br>100% vesting at 1.6 x WACC<br><br>with straight line vesting in between. | 0% vesting if <50th percentile of index group<br><br>50% vesting if aligned to 50th percentile of index group<br><br>100% vesting if aligned to 75th percentile of index group<br><br>with straight line vesting in between. |
| Instrument | Rights granted after 1 July 2013 may be settled with either IAG ordinary shares or with cash if performance hurdles are achieved, as determined by the Board. Rights granted prior to 1 July 2013 are settled with IAG ordinary shares. | |
| Key terms of the LTI | The number of EPR issued is calculated based on the share price of an IAG ordinary share at 30 June. EPR granted during the year will not vest and have no value to the Executive unless the performance hurdles are achieved. No dividend is paid or payable for any unvested or vested and unexercised EPR. | |
| Forfeiture conditions | Under the terms of the LTI, if an Executive ceases employment with the Group voluntarily before the performance hurdles are tested, the unvested EPR will generally lapse. In cases where the Executive acts fraudulently or dishonestly or is in breach of his or her obligations to the Group, the unvested EPR will lapse. | |

## E. LINKING THE GROUP'S PERFORMANCE AND REWARD

**I. Linking IAG's short term performance and short term reward**

The table below provides a summary of key balanced scorecard objectives and outcomes for the Group for the year ended 30 June 2016. The objectives are agreed with the Board at the beginning of each financial year and are designed to stretch the Executives to deliver sustainable value for shareholders.

TABLE 5 - BALANCED SCORECARD OBJECTIVES AND PERFORMANCE REQUIREMENTS

| CATEGORY | OBJECTIVE | WEIGHTING | RESULT | OUTCOME |
|---|---|---|---|---|
| Financial measures | Return on risk based capital | 15% | Met | The Group sets targets to achieve a return on its risk based capital that requires outperformance through the cycle. This return reflects how effectively IAG uses its capital and is directly aligned to the Group's strategic target of achieving a ROE of 1.5 times the weighted average cost of capital. In the current financial year, the Group reported a return on risk based capital that was aligned to budget. |
| | Profitable growth | 10% | Did not meet | To grow profitably and create value for shareholders, IAG continues to develop our products, markets and customer base. In the current financial year, GWP increased for the Australian Consumer Division and Asia, but was below anticipated in the Australian Business Division and New Zealand. |
| | Operating cost efficiencies | 15% | Exceeded | IAG successfully achieved its operating cost efficiencies by focusing on simplifying and streamlining our business and delivering on our synergy commitments. |

| CATEGORY | OBJECTIVE | WEIGHTING | RESULT | OUTCOME |
|---|---|---|---|---|
| | Secure position in chosen markets | 10% | Met | Across the Group, IAG's market position remained stable. While facing a challenging market, IAG was able to maintain market position in three of the four markets. |
| Non-financial measures | IAG is the insurer of choice | 10% | Met | IAG remains committed to our customers and delivering exceptional experiences. This has been reflected in maintaining our strong Net Promoter Scores across both the Australian Consumer Division and New Zealand businesses, proving our customers continue to be advocates for IAG's brands. |
| | IAG sets the market benchmark | 10% | Exceeded | While the Australian Business Division Partner Advocacy score has remained stable, CGU Insurance has received notable recognition from external sources including being voted Insurer of the Year by Insurance Business magazine and winning the NIBA General Insurer of the Year Award. |
| | IAG makes communities safer, stronger and more confident | 5% | Exceeded | IAG is focused on making communities safer, stronger and more confident by investing in partnerships, programs and projects that create shared value for IAG and the community. Over the year, IAG received a number of awards and external recognition for our responsible business and sustainability practices, which cover aspects relating to our Governance and Ethics as well as Social and Environmental performance. We have continued to focus on initiatives that support indigenous programs, corporate sustainability and community disaster resilience. |
| | IAG attracts and nurtures talent, is agile, flexible and a safe place to work | 10% | Did not meet | The organisational culture has not reached the constructive level we aspire to. The 2016 financial year was a time of change: we announced a new operating model, set up different ways of working, and introduced simplification initiatives which impacted our people. However, during this time, IAG continued to drive organisational improvement across safety, agility, flexibility, diversity and inclusion, including continued progress on meeting our target of 38% women in senior management roles by 2020 and positive workplace health and safety performance improvement in Australia and New Zealand. This sets us up well to drive a more constructive culture into the future. |
| | Execute FY16-FY18 strategic priorities | 5% | Met | IAG's strategic priorities focus the business on delivering initiatives that are the most important for our organisation. We successfully progressed our current financial year strategic priorities, including developing and leveraging deep customer insights and accelerating IAG's digital transformation. |
| | Effectively govern and manage risk | 5% | Met | Strategies have been developed to further uplift IAG's Risk Management Framework to manage key organisational risks. Risk management practices contribute strongly to strategic and operational decision making. Overall effectiveness of Risk Management at IAG is supported by external validation. |
| | Build capability and agility for future value | 5% | Exceeded | IAG remains dedicated to building capability and agility that will set the foundation for future success. This includes launching six new ventures (including Sharecover and InsureLite); building Human Centred Design capability and embedding it across all product development and innovation projects; and establishing enterprise-wide customer and digital functions through our Customer Labs and Digital Labs teams. |

**II. STI outcomes for the year ended 30 June 2016**

STI payments made to Executives for the year ended 30 June 2016 are set out below, and were based on achievement against the balanced scorecard measures described in table 5. In line with the overall performance, the STI awarded to Executives are, on average, slightly higher than last year.

TABLE 6 - ACTUAL STI OUTCOMES FOR THE YEAR ENDED 30 JUNE 2016

| | MAXIMUM STI OPPORTUNITY | ACTUAL STI OUTCOME | | CASH STI OUTCOME (2/3 OF OUTCOME) | DEFERRED STI OUTCOME (1/3 OF OUTCOME) |
|---|---|---|---|---|---|
| | (% of fixed pay)[a] | (% of maximum)[b] | (% of fixed pay) | (% of fixed pay) | (% of fixed pay) |
| Peter Harmer | 139 % | 68 % | 94 % | 63 % | 31 % |
| Julie Batch | 103 % | 70 % | 72 % | 48 % | 24 % |
| Chris Bertuch | 103 % | 55 % | 56 % | 38 % | 18 % |
| Ben Bessell | 120 % | 50 % | 60 % | 40 % | 20 % |
| Duncan Brain | 120 % | 72 % | 86 % | 58 % | 28 % |
| David Harrington | 103 % | 70 % | 72 % | 48 % | 24 % |
| Nicholas Hawkins | 120 % | 73 % | 88 % | 58 % | 30 % |
| Jacki Johnson | 120 % | 67 % | 80 % | 54 % | 26 % |
| Anthony Justice | 103 % | 74 % | 76 % | 51 % | 25 % |
| Mark Milliner | 120 % | - % | - % | - % | - % |
| Craig Olsen | 100 % | 68 % | 68 % | 45 % | 23 % |
| Claire Rawlins | 101 % | 73 % | 74 % | 49 % | 25 % |
| Clayton Whipp | 120 % | 67 % | 80 % | 54 % | 26 % |

(a) Executives who had a change in role during the year have their incentive opportunity pro-rated between their prior role and their current role. Therefore, the STI opportunity is less than 150% of fixed pay for Peter Harmer and less than 120% of fixed pay for the newly appointed Executive team members.

(b) The proportion of STI forfeited is derived by subtracting the actual % of maximum received from 100% and was 33% on average for the year ended 30 June 2016 (compared to 39% in 2015).

**III. Linking the Group's long term performance and long term reward**

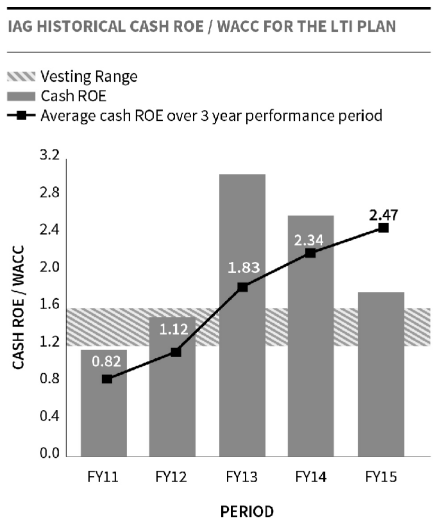
Details of LTI vested during the year are set out below:

**ROE – 100% vesting**

For the performance period ended 30 June 2015, the average cash ROE was 2.47 times WACC. This resulted in full vesting of the ROE portion of the 2012/2013 Series 5 EPR. This strong cash ROE performance has similarly been reflected in the dividend provided to shareholders

**TSR – 54% vesting**

For the performance period ended 30 September 2015, IAG's TSR was ranked at the 52nd percentile of its peer group. This ranking translates to 54% vesting of the TSR portion of the 2012/2013 EPR. A retest will occur on 30 September 2016.




The following table shows the returns IAG delivered to its shareholders for the last five financial years for a range of measures.

TABLE 7 - HISTORICAL ANALYSIS OF SHAREHOLDER RETURN ON LTI

| | YEAR ENDED 30 JUNE 2012 | YEAR ENDED 30 JUNE 2013 | YEAR ENDED 30 JUNE 2014 | YEAR ENDED 30 JUNE 2015 | **YEAR ENDED 30 JUNE 2016** |
|---|---|---|---|---|---|
| Closing share price ($) | 3.48 | 5.44 | 5.84 | 5.58 | **5.45** |
| Dividend paid per ordinary share (cents) | 17.00 | 36.00 | 39.00 | 29.00 | **36.00** |
| Basic earnings per share (cents) | 10.01 | 37.57 | 56.09 | 31.22 | **25.79** |
| Cash ROE (%) | 13.3 | 25.3 | 23.0 | 15.3 | **13.0** |
| ROE to WACC outcome for EPR Plan | 1.12 | 1.83 | 2.34 | 2.47 | **2.00** |
| TSR for the financial year (%)* | 5.3 | 59.2 | 15.6 | 1.8 | **4.3** |

* This represents the TSR performance measured for the 12 months from 1 July to 30 June.

## F. EXECUTIVE EMPLOYMENT AGREEMENTS

All employment agreements for Executives are for unlimited terms but may be terminated by written notice from either party or by IAG making a payment in lieu of notice. The employment agreements outline the components of remuneration paid to each Executive and require annual review of Executives' remuneration, although the agreements do not require IAG to increase base salary, pay STI or offer an LTI in any given year.

All Executive contracts have a 12 month notice period from the relevant company for termination and the Executives must provide six months' notice, with the exception of Nicholas Hawkins who has an employee notice period of three months. Executives are employed by Insurance Australia Group Services Pty Limited, except for Craig Olsen who is employed by IAG New Zealand Limited.

### I. Retrenchment

In the event of retrenchment, Executives (except for Craig Olsen) are entitled to the greater of:

- the written notice period or payment in lieu of notice as provided in their employment agreement; or
- the retrenchment benefits due under the company retrenchment policy.

For Executives based in Australia, the minimum benefit under the retrenchment policy is 11 weeks of base salary with a maximum benefit of 87 weeks of base salary. The maximum benefit is payable to employees with service of 25 years or more.

For Craig Olsen, the retrenchment payment is 12 months of fixed pay.

### II. Termination of employment without notice and without payment in lieu of notice

The employment of an Executive may be terminated without notice and without payment in lieu of notice in some circumstances.

Generally, this could occur where the Executive:

- is charged with a criminal offence that could bring the organisation into disrepute;
- is declared bankrupt;
- breaches a provision of their employment agreement;
- is guilty of serious and wilful misconduct; or
- unreasonably fails to comply with any material and lawful direction given by the relevant company.

### III. Termination of employment with notice or payment in lieu of notice

The employment of an Executive may be terminated at any time by the relevant company with 12 months notice or payment in lieu of notice. Payment in lieu of notice will be calculated based on fixed pay. If an Executive terminates voluntarily they are required to provide six months' notice, with the exception of Nicholas Hawkins who is required to provide three months' notice.

Subject to the relevant legislation in the various jurisdictions, termination provisions may include the payment of annual leave and/or long service leave for the Executives.

### IV. Retired and Retrenched Executives

All termination benefits provided to retired and retrenched Executives were consistent with IAG's termination policy as disclosed in the Remuneration Report and did not exceed the level that would require shareholder approval under the Corporations Act 2001 (Terminations Cap).

Details of the payments received by retired and retrenched Executives are outlined below:

| | Michael Wilkins Retirement $000 (1) | Andy Cornish Retrenchment $000 (2) | Alex Harrison Retrenchment $000 (2) | Leona Murphy Retrenchment $000 (3) |
|---|---|---|---|---|
| Termination benefits | 2,257 | 816 | 565 | 923 |
| Other benefits | - | 270 | 217 | 295 |
| Total benefits | 2,257 | 1,086 | 782 | 1,218 |

(1) Termination benefits for Michael Wilkins include payment in lieu of notice and STI payment made ahead of the annual payment date.

(2) Termination benefits for Andy Cornish and Alex Harrison include contractual payments in lieu of notice that were above the redundancy entitlements required by the relevant statutes, and outplacement services. Other benefits include payment in lieu of notice and redundancy payments aligned to statutory entitlements.

(3) Termination benefits for Leona Murphy include contractual payment in lieu of notice that was above the redundancy entitlements required by the relevant statutes, and STI payment made ahead of the regular annual payment date. Other benefits include payment in lieu of notice and redundancy payment aligned to statutory entitlements.

## G. STATUTORY REMUNERATION DISCLOSURE REQUIREMENTS

### I. Total remuneration for Executives

Statutory remuneration details for Executives as required by Australian Accounting Standards are set out below:

TABLE 8 - STATUTORY REMUNERATION DETAILS (EXECUTIVES)

| | SHORT TERM EMPLOYMENT BENEFITS | | | POST EMPLOY-MENT BENEFITS | OTHER LONG TERM EMPLOY-MENT BENEFITS | TERM-INATION BENEFITS | SUB-TOTAL | SHARE-BASED PAYMENT | | TOTAL | AT-RISK REMUN-ERATION PAID |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | Base salary | Cash STI | Leave accruals and other benefits | Superan-nuation | Long service leave accruals | | | Value of deferred STI | Value of rights granted | | as a % of total reward |
| | $000 | $000 | $000 | $000 | $000 | $000 | $000 | $000 | $000 | $000 | % |
| | (1) | (2) | (3) | (4) | (5) | (6) | | (7) | (8) | | |
| **EXECUTIVES** | | | | | | | | | | | |
| Peter Harmer | | | | | | | | | | | |
| **2016** | **1,425** | **905** | **16** | **35** | **54** | **-** | **2,435** | **313** | **1,016** | **3,764** | **59** |
| 2015 | 977 | 473 | (37) | 35 | 14 | - | 1,462 | 341 | 1,032 | 2,835 | 65 |
| Julie Batch | | | | | | | | | | | |
| **2016** | **326** | **153** | **16** | **17** | **18** | **-** | **530** | **110** | **171** | **811** | **54** |
| Chris Bertuch | | | | | | | | | | | |
| **2016** | **380** | **138** | **25** | **20** | **8** | **-** | **571** | **131** | **195** | **897** | **52** |
| Ben Bessell | | | | | | | | | | | |
| **2016** | **656** | **271** | **(5)** | **30** | **36** | **-** | **988** | **86** | **156** | **1,230** | **42** |
| 2015 | 116 | 65 | (10) | 7 | 3 | - | 181 | - | - | 181 | 36 |
| Duncan Brain | | | | | | | | | | | |
| **2016** | **899** | **532** | **245** | **35** | **16** | **-** | **1,727** | **815** | **719** | **3,261** | **63** |
| 2015 | 886 | 469 | 243 | 35 | 20 | - | 1,653 | 167 | 534 | 2,354 | 50 |
| David Harrington | | | | | | | | | | | |
| **2016** | **326** | **160** | **29** | **20** | **4** | **-** | **539** | **96** | **163** | **798** | **53** |
| Nicholas Hawkins | | | | | | | | | | | |
| **2016** | **996** | **593** | **(35)** | **30** | **(13)** | **-** | **1,571** | **341** | **977** | **2,889** | **66** |
| 2015 | 982 | 603 | 68 | 30 | (12) | - | 1,671 | 353 | 1,007 | 3,031 | 65 |
| Jacki Johnson[9] | | | | | | | | | | | |
| **2016** | **1,025** | **585** | **78** | **28** | **14** | **-** | **1,730** | **258** | **957** | **2,945** | **61** |
| 2015 | 1,096 | 418 | (50) | - | 7 | - | 1,471 | 287 | 940 | 2,698 | 61 |
| Anthony Justice | | | | | | | | | | | |
| **2016** | **355** | **156** | **(17)** | **17** | **11** | **-** | **522** | **64** | **76** | **662** | **45** |
| Mark Milliner | | | | | | | | | | | |
| **2016** | **176** | **-** | **19** | **5** | **1** | **-** | **201** | **-** | **-** | **201** | **-** |
| Craig Olsen[10] | | | | | | | | | | | |
| **2016** | **330** | **124** | **36** | **-** | **-** | **-** | **490** | **75** | **130** | **695** | **47** |
| Claire Rawlins | | | | | | | | | | | |
| **2016** | **321** | **152** | **30** | **20** | **2** | **-** | **525** | **-** | **21** | **546** | **32** |
| Clayton Whipp | | | | | | | | | | | |
| **2016** | **749** | **415** | **48** | **35** | **16** | **-** | **1,263** | **184** | **321** | **1,768** | **52** |
| 2015 | 720 | 341 | 29 | 35 | 35 | - | 1,160 | 138 | 208 | 1,506 | 46 |

| | SHORT TERM EMPLOYMENT BENEFITS | | | POST EMPLOY-MENT BENEFITS | OTHER LONG TERM EMPLOY-MENT BENEFITS | TERM-INATION BENEFITS | SUB-TOTAL | SHARE-BASED PAYMENT | | TOTAL | AT-RISK REMUN-ERATION PAID |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | Base salary | Cash STI | Leave accruals and other benefits | Superan-nuation | Long service leave accruals | | | Value of deferred STI | Value of rights granted | | as a % of Total Reward |
| | $000 | $000 | $000 | $000 | $000 | $000 | $000 | $000 | $000 | $000 | % |
| | (1) | (2) | (3) | (4) | (5) | (6) | | (7) | (8) | | |
| **EXECUTIVES WHO CEASED AS KEY MANAGEMENT PERSONNEL** | | | | | | | | | | | |
| Michael Wilkins | | | | | | | | | | | |
| **2016** | **801** | **1,197** | **144** | **7** | **(190)** | **1,060** | **3,019** | **1,383** | **3,898** | **8,300** | **78** |
| 2015 | 2,093 | 1,314 | 188 | 19 | 44 | - | 3,658 | 898 | 2,525 | 7,081 | 67 |
| Andy Cornish | | | | | | | | | | | |
| **2016** | **846** | **887** | **29** | **29** | **20** | **1,086** | **2,897** | **505** | **2,421** | **5,823** | **65** |
| 2015 | 1,017 | 602 | 73 | 35 | 20 | - | 1,747 | 307 | 1,048 | 3,102 | 63 |
| Alex Harrison | | | | | | | | | | | |
| **2016** | **139** | **-** | **(31)** | **6** | **25** | **782** | **921** | **126** | **769** | **1,816** | **49** |
| 2015 | 819 | 611 | 29 | 30 | 22 | - | 1,511 | 144 | 308 | 1,963 | 54 |
| Leona Murphy | | | | | | | | | | | |
| **2016** | **450** | **410** | **21** | **16** | **31** | **808** | **1,736** | **484** | **2,121** | **4,341** | **69** |
| 2015 | 880 | 505 | 20 | 30 | 18 | - | 1,453 | 298 | 907 | 2,658 | 64 |

(1) Base salary includes amounts paid in cash plus the portion of the Company's superannuation contribution that is paid as cash instead of being paid into superannuation plus salary sacrifice items such as cars and parking, as determined in accordance with AASB 119 Employee Benefits.

(2) Cash STI represents the amount to be settled in cash in relation to the financial year from 1 July 2015 to 30 June 2016.

(3) This column includes leave accruals, 30% tax rebate on car allowances for certain KMP who have salary sacrifice arrangements on cars and other short term employment benefits as agreed and provided under specific conditions. Other benefits provided under specific conditions for KMP are provided as follows: Duncan Brain: accommodation allowances, airfares for home visits and medical insurance.

(4) Superannuation represents the employer's contributions.

(5) Long service leave accruals as determined in accordance with AASB 119.

(6) Termination benefits include payment in lieu of notice, redundancy entitlements and outplacement services (where provided).

(7) The deferred STI is granted as DAR and is valued using the Black-Scholes valuation model. An allocated portion of unvested DAR for financial years prior to 30 June 2015 is included in the total remuneration disclosure above. The deferred STI for the year ended 30 June 2016 will be granted in the next financial year, so no value was included in the current financial year's total remuneration.

(8) This value represents the allocated portion of unvested EPR. To determine the EPR values the Monte Carlo simulation (for the TSR performance hurdle) and Black-Scholes valuation (for the ROE performance hurdle) models have been applied. The valuation takes into account the exercise price of the EPR, life of the EPR, price of IAG ordinary shares as at 30 June, expected volatility of the IAG share price, expected dividends, risk free interest rate, performance of shares in the peer group of companies, early exercise and non-transferability and turnover which is assumed to be zero for an individual's remuneration calculation.

(9) Remuneration for Jacki Johnson for the period 1 July 2015 to 1 January 2016 was determined in New Zealand dollars and reported in Australian dollars.

(10) Remuneration for Craig Olsen was determined in New Zealand dollars and reported in Australian dollars.

### II. Movement in equity plans within the financial year

Changes in each Executive's holding of DAR and EPR during the financial year are set out below. The DAR granted during the year reflect the deferred portion of the STI outcome for the year ended 30 June 2015. The EPR granted during the year ended 30 June 2016 were in relation to the LTI plan.

TABLE 9 - MOVEMENT IN POTENTIAL VALUE OF DAR AND EPR FOR THE YEAR ENDED 30 JUNE 2016(1)

| | | RIGHTS ON ISSUE 1 JULY (2) | RIGHTS GRANTED DURING THE YEAR (3) | | RIGHTS EXERCISED DURING THE YEAR (4) | | RIGHTS ON ISSUE 30 JUNE | RIGHTS VESTED DURING THE YEAR | RIGHTS VESTED AND EXERCISABLE 30 JUNE |
|---|---|---|---|---|---|---|---|---|---|
| | | Number | Number | Value ($000) | Number | Value ($000) | Number | Number | Number |
| **EXECUTIVES** | | | | | | | | | |
| Peter Harmer | DAR | 90,600 | 42,500 | 220 | (60,450) | 331 | 72,650 | 60,450 | - |
| | EPR | 799,200 | 370,200 | 1,343 | (271,117) | 1,485 | 898,283 | 271,117 | - |
| Julie Batch | DAR | 48,050 | - | - | (18,600) | 102 | 29,450 | 18,600 | - |
| | EPR | 162,800 | 54,400 | 197 | (40,271) | 221 | 176,929 | 40,271 | - |
| Chris Bertuch | DAR | 33,950 | - | - | - | - | 33,950 | - | - |
| | EPR | 138,545 | 64,500 | 234 | - | - | 203,045 | - | - |
| Ben Bessell | DAR | 22,550 | 16,500 | 85 | (16,200) | 89 | 22,850 | 16,200 | - |
| | EPR | 101,100 | 108,600 | 394 | (10,000) | 55 | 199,700 | 30,569 | 20,569 |
| Duncan Brain | DAR | 47,700 | 400,600 | 2,074 | (29,950) | 164 | 418,350 | 29,950 | - |
| | EPR | 474,200 | 207,000 | 751 | (51,821) | 284 | 629,379 | 51,821 | - |
| David Harrington | DAR | 29,450 | - | - | - | - | 29,450 | - | - |
| | EPR | 130,191 | 52,300 | 190 | - | - | 182,491 | - | - |
| Nicholas Hawkins | DAR | 93,150 | 54,000 | 280 | (61,800) | 338 | 85,350 | 61,800 | - |
| | EPR | 799,200 | 227,400 | 825 | (271,117) | 1,485 | 755,483 | 271,117 | - |
| Jacki Johnson | DAR | 73,300 | 37,500 | 194 | (49,100) | 269 | 61,700 | 49,100 | - |
| | EPR | 756,700 | 244,500 | 887 | (244,167) | 1,337 | 757,033 | 244,167 | - |
| Anthony Justice | DAR | 20,600 | - | - | - | - | 20,600 | - | - |
| | EPR | 57,500 | 65,300 | 237 | - | - | 122,800 | - | - |
| Mark Milliner(5) | DAR | - | - | - | - | - | - | - | - |
| | EPR | - | - | - | - | - | - | - | - |
| Craig Olsen | DAR | 34,000 | - | - | (13,650) | 75 | 20,350 | 13,650 | - |
| | EPR | 115,000 | 62,600 | 227 | (22,638) | 124 | 154,962 | 22,638 | - |
| Claire Rawlins | DAR | - | - | - | - | - | - | - | - |
| | EPR | - | 75,500 | 274 | - | - | 75,500 | - | - |
| Clayton Whipp | DAR | 34,650 | 53,200 | 274 | (22,700) | 124 | 65,150 | 22,700 | - |
| | EPR | 178,900 | 173,700 | 630 | (46,046) | 252 | 306,554 | 46,046 | - |
| **EXECUTIVES WHO CEASED AS KEY MANAGEMENT PERSONNEL** | | | | | | | | | |
| Michael Wilkins | DAR | 230,950 | 117,800 | 610 | (154,050) | 844 | 194,700 | 154,050 | - |
| | EPR | 2,002,500 | - | - | (679,448) | 3,720 | 1,323,052 | 679,448 | - |
| Andy Cornish | DAR | 70,750 | 54,000 | 280 | (49,900) | 273 | 74,850 | 49,900 | - |
| | EPR | 831,400 | 236,500 | 858 | (282,128) | 1,545 | 785,772 | 282,128 | - |
| Alex Harrison | DAR | 37,600 | - | - | - | - | 37,600 | - | - |
| | EPR | 290,300 | - | - | - | - | 290,300 | 32,050 | 32,050 |
| Leona Murphy | DAR | 75,250 | 45,300 | 235 | (50,850) | 278 | 69,700 | 50,850 | - |
| | EPR | 719,500 | 204,700 | 743 | (244,090) | 1,337 | 680,110 | 244,090 | - |

(1) There were no rights that lapsed or were forfeited but not yet lapsed during the year.

(2) Opening number of rights on issue represents the balance as at the date of appointment as KMP or 1 July 2015.

(3) The value of the DAR granted during the year is the fair value at grant date calculated using the Black-Scholes valuation model. The value of the annual DAR granted on 2 November 2015 and 31 March 2016 was $5.18 and $5.25 respectively. This amount is allocated to remuneration over years ending 30 June 2016 to 30 June 2018. Additional DAR grants of 358,500 to Duncan Brain and 22,600 to Clay Whipp were granted on 2 November 2015 have an expiry date of 2 November 2022 and are exercisable on 20 December 2017 and 1 September 2018 respectively. The value of the 358,500 DAR granted was $4.97 and this amount is allocated to remuneration over years ending 30 June 2016 to 30 June 2018. The value of the 22,600 DAR granted was $4.76. This amount is allocated to remuneration over the years ending 30 June 2016 to 30 June 2019. The value of the ROE portion of the EPR granted on 2 November 2015 and 31 March 2016 is the fair value at grant date, calculated using the Black-Scholes valuation model, which was $4.84 and $4.80 respectively. The value of the TSR portion of the EPR granted on 2 November 2015 and 31 March 2016 is the fair value at grant date, calculated using the Monte Carlo simulation, which was $2.42 and $2.35 respectively. The ROE portion of the EPR grants is first exercisable after the performance period concludes on 30 June 2018. The TSR portion of the EPR is first exercisable on 30 September 2019. The amount is allocated to remuneration over the years ending 30 June 2016 to 30 June 2020.

(4) Rights vested on or before 1 September 2015 and exercised during the financial year. The value of the rights exercised is based on the weighted average share price which was $5.48 for the year ended 30 June 2016.

(5) Mark Milliner will receive 150,000 DAR in November 2016 as compensation for incentives foregone on leaving his previous employer.

**III. LTI awards outstanding during the year ended 30 June 2016**
Details of outstanding LTI awards made to Executives in the year ended 30 June 2016 are shown in the table below:

TABLE 10 - LTI AWARDS OUTSTANDING DURING THE YEAR ENDED 30 JUNE 2016

| AWARD | GRANT DATE | BASE DATE | FIRST TEST DATE | LAST TEST DATE | PERFORMANCE HURDLE ACHIEVEMENT | LAST EXERCISE DATE |
|---|---|---|---|---|---|---|
| 2015/2016 Series 6 - TSR[(a)] | 31/03/2016 | 30/09/2015 | 30/09/2019 | | N/A | 31/03/2023 |
| 2015/2016 Series 6 - ROE[(a)] | 31/03/2016 | 01/07/2015 | 30/06/2018 | | N/A | 31/03/2023 |
| 2015/2016 Series 6 - TSR[(a)] | 02/11/2015 | 30/09/2015 | 30/09/2019 | | N/A | 02/11/2022 |
| 2015/2016 Series 6 - ROE[(a)] | 02/11/2015 | 01/07/2015 | 30/06/2018 | | N/A | 02/11/2022 |
| 2014/2015 Series 6 - TSR[(a)] | 03/11/2014 | 30/09/2014 | 30/09/2018 | | N/A | 03/11/2021 |
| 2014/2015 Series 6 - ROE[(a)] | 03/11/2014 | 01/07/2014 | 30/06/2017 | | N/A | 03/11/2021 |
| 2013/2014 Series 6 - TSR[(a)] | 01/11/2013 | 30/09/2013 | 30/09/2017 | | N/A | 01/11/2020 |
| 2013/2014 Series 6 - ROE[(a)(b)] | 01/11/2013 | 01/07/2013 | 30/06/2016 | | N/A | 01/11/2020 |
| 2012/2013 Series 5 - TSR | 26/10/2012 | 30/09/2012 | 30/09/2015 | 30/09/2017 | 54% | 26/10/2019 |
| 2012/2013 Series 5 - ROE | 26/10/2012 | 01/07/2012 | 30/06/2015 | | 100% | 26/10/2019 |

(a) Terms and conditions for EPR Plan 2013/2014, 2014/2015 and 2015/2016 are the same, therefore they are all referred to as Series 6.
(b) The cash ROE portion of EPR Plan 2013/2014 has been tested and is expected to vest in full. Vesting details will be included in the Remuneration Report for the year ending 30 June 2017.

## H. NON-EXECUTIVE DIRECTOR REMUNERATION

**I. Remuneration policy**
The principles that underpin IAG's approach to remuneration for Non-Executive Directors are that remuneration should:
- be sufficiently competitive to attract and retain a high calibre of Non-Executive Director; and
- create alignment between the interests of Non-Executive Directors and shareholders through the mandatory shareholding requirement.

**II. Remuneration structure**
Non-Executive Director remuneration has two components:
- Board fees (paid as cash and superannuation); and
- subsidiary board and Committee fees.

a. CHANGES TO NON-EXECUTIVE REMUNERATION DURING THE YEAR ENDED 30 JUNE 2016
In August 2015, the Board approved maintaining Board fees at the current level, aligning to the approach taken for Executive fixed pay. The Board approved a Committee fee increase of 22.25% for all Committees except the Nominations Committee, to align fees with the market. The aggregate limit of Board fees approved by shareholders at the Annual General Meeting in October 2013 remains unchanged at $3,500,000 per annum.

The figures shown below are inclusive of superannuation. Directors can elect the portion of fees contributed into their nominated superannuation fund, provided minimum legislated contribution levels are met.

TABLE 11 - BOARD AND COMMITTEE FEES

| | | ROLE | |
|---|---|---|---|
| BOARD/COMMITTEE | YEAR | CHAIRMAN | DIRECTOR |
| Board | **2016** | **$565,800** | **$188,600** |
| | 2015 | $565,800 | $188,600 |
| Audit Committee | **2016** | **$50,000** | **$25,000** |
| | 2015 | $40,900 | $20,450 |
| Risk Committee | **2016** | **$50,000** | **$25,000** |
| | 2015 | $40,900 | $20,450 |
| People and Remuneration Committee | **2016** | **$50,000** | **$25,000** |
| | 2015 | $40,900 | $20,450 |
| Nominations Committee* | **2016** | **N/A** | **$10,000** |
| | 2015 | N/A | $10,000 |

* The Chair of the Nominations Committee is also the Chairman of the Company, therefore no Chair fee is applicable.

b. SUBSIDIARY BOARD AND COMMITTEE FEES
A summary of Non-Executive Directors' service on subsidiary boards and the fees paid is set out below:

TABLE 12 - FEES FOR NON-EXECUTIVE DIRECTORS' SERVICE ON SUBSIDIARY BOARDS

| DIRECTOR | SUBSIDIARY | CAPACITY | ANNUAL FEE |
|---|---|---|---|
| Elizabeth Bryan | Insurance Manufacturers of Australia Pty Limited | Chairman | $247,000 |
| Hugh Fletcher* | IAG New Zealand Limited | Chairman | $137,936 |

* This amount was paid to Hugh Fletcher in New Zealand dollars and reported in Australian dollars.

#### III. Board performance

The Board conducts a review of its performance, composition, size and succession planning at least every three years with assistance from external experts (Formal Review). A Formal Review of the Board and each Non-Executive Director (including the Chairman), with assistance and input from an independent board performance expert, was conducted in 2016. The Formal Review process involves the completion of questionnaires by Non-Executive Directors and the Executive team; interviews with the independent expert; the collation of results; and discussion with individual Non-Executive Directors and the Board as a whole led by the Chairman. The PARC is responsible for coordinating the Board's review of the Chairman's performance.

Measures of a Non-Executive Director's performance include:

- contribution to Board teamwork;
- contribution to debates on significant issues and proposals;
- advice and assistance given to management;
- input regarding regulatory, industry and social developments surrounding the business; and
- in the case of the Chairman's performance, the fulfilment of the additional role as Chairman.

#### IV. Total remuneration details

Details of total remuneration for Non-Executive Directors on the Board for the year ended 30 June 2016 are set out below:

TABLE 13 - STATUTORY REMUNERATION DETAILS (NON-EXECUTIVE DIRECTORS)

| | SHORT TERM EMPLOYMENT BENEFITS | | POST-EMPLOYMENT BENEFITS | | OTHER LONG TERM EMPLOYMENT BENEFITS | TERMINATION BENEFITS | SHARE BASED PAYMENT | TOTAL |
|---|---|---|---|---|---|---|---|---|
| | IAG Board fees received as cash | Other Boards and Committee fees | Superannuation | Retirement benefits | | | | |
| | $000 | $000 | $000 | $000 | $000 | $000 | $000 | $000 |
| NON-EXECUTIVE DIRECTORS | | | | | | | | |
| Elizabeth Bryan | | | | | | | | |
| **2016** | **276** | **111** | **19** | **-** | **-** | **-** | **-** | **406** |
| 2015 | 99 | 6 | 10 | - | - | - | - | 115 |
| Alison Deans | | | | | | | | |
| **2016** | **172** | **28** | **19** | **-** | **-** | **-** | **-** | **219** |
| 2015 | 173 | 37 | 19 | - | - | - | - | 229 |
| Hugh Fletcher | | | | | | | | |
| **2016** | **172** | **184** | **21** | **-** | **-** | **-** | **-** | **377** |
| 2015 | 172 | 177 | 20 | - | - | - | - | 369 |
| Raymond Lim | | | | | | | | |
| **2016** | **172** | **23** | **19** | **-** | **-** | **-** | **-** | **214** |
| 2015 | 172 | 19 | 18 | - | - | - | - | 209 |
| Jonathan Nicholson[a] | | | | | | | | |
| **2016** | **145** | **36** | **14** | **-** | **-** | **-** | **-** | **195** |
| Tom Pockett | | | | | | | | |
| **2016** | **177** | **78** | **19** | **-** | **-** | **-** | **-** | **274** |
| 2015 | 86 | - | 8 | - | - | - | - | 94 |
| Philip Twyman | | | | | | | | |
| **2016** | **177** | **82** | **19** | **-** | **-** | **-** | **-** | **278** |
| 2015 | 177 | 80 | 19 | - | - | - | - | 276 |
| NON-EXECUTIVE DIRECTORS WHO CEASED AS KEY MANAGEMENT PERSONNEL | | | | | | | | |
| Brian Schwartz | | | | | | | | |
| **2016** | **424** | **169** | **14** | **-** | **-** | **-** | **-** | **607** |
| 2015 | 568 | 226 | 19 | - | - | - | - | 813 |
| Yasmin Allen | | | | | | | | |
| **2016** | **44** | **16** | **5** | **-** | **-** | **-** | **-** | **65** |
| 2015 | 178 | 84 | 19 | - | - | - | - | 281 |

(a) Director appointed part way through current financial year.

## I. RELATED PARTY INTERESTS

In accordance with the Corporations Act Regulation 2M.3.03, the Remuneration Report includes disclosure of related parties.

### I. Movements in total number of ordinary shares held

The relevant interests of each key management personnel and their related parties in IAG ordinary shares are disclosed in the table below:

TABLE 14 - MOVEMENT IN TOTAL NUMBER OF ORDINARY SHARES HELD

| | SHARES HELD AT 1 JULY | SHARES RECEIVED ON EXERCISE OF DAR | SHARES RECEIVED ON EXERCISE OF EPR | NET MOVEMENT OF SHARES DUE TO OTHER CHANGES[(a)] | TOTAL SHARES HELD AT 30 JUNE | SHARES HELD NOMINALLY AT 30 JUNE[(b)] |
|---|---|---|---|---|---|---|
| | Number | Number | Number | Number | Number | Number |
| **2016** | | | | | | |
| NON-EXECUTIVE DIRECTORS AND EXECUTIVES | | | | | | |
| Elizabeth Bryan | **31,409** | **-** | **-** | **1,316** | **32,725** | **32,725** |
| Alison Deans | **37,742** | **-** | **-** | **-** | **37,742** | **37,742** |
| Hugh Fletcher | **80,707** | **-** | **-** | **1,325** | **82,032** | **45,471** |
| Raymond Lim | **30,000** | **-** | **-** | **5,000** | **35,000** | **35,000** |
| Jonathan Nicholson[(c)] | **1,468** | **-** | **-** | **10,000** | **11,468** | **1,041** |
| Tom Pockett | **32,096** | **-** | **-** | **155** | **32,251** | **-** |
| Philip Twyman | **31,272** | **-** | **-** | **(15,750)** | **15,522** | **12,780** |
| Peter Harmer | **624,400** | **60,450** | **271,117** | **(300,000)** | **655,967** | **172,800** |
| Julie Batch[(c)] | **124,036** | **18,600** | **40,271** | **-** | **182,907** | **277** |
| Chris Bertuch[(c)] | **53,840** | **-** | **-** | **40** | **53,880** | **380** |
| Ben Bessell | **464** | **16,200** | **10,000** | **(26,200)** | **464** | **277** |
| Duncan Brain | **152,987** | **29,950** | **51,821** | **-** | **234,758** | **-** |
| David Harrington[(c)] | **1,227** | **-** | **-** | **160** | **1,387** | **789** |
| Nicholas Hawkins | **200,000** | **61,800** | **271,117** | **(312,917)** | **220,000** | **-** |
| Jacki Johnson | **1,299,493** | **49,100** | **244,167** | **(1,366,827)** | **225,933** | **225,933** |
| Anthony Justice[(c)] | **-** | **-** | **-** | **-** | **-** | **-** |
| Mark Milliner[(c)] | **-** | **-** | **-** | **-** | **-** | **-** |
| Craig Olsen[(c)] | **130,765** | **13,650** | **22,638** | **(43,650)** | **123,403** | **14,800** |
| Claire Rawlins[(c)] | **-** | **-** | **-** | **-** | **-** | **-** |
| Clayton Whipp | **32,381** | **22,700** | **46,046** | **187** | **101,314** | **1,378** |
| NON-EXECUTIVE DIRECTORS AND EXECUTIVES WHO CEASED AS KEY MANAGEMENT PERSONNEL[(d)] | | | | | | |
| Brian Schwartz | **111,171** | **-** | **-** | **2,348** | **113,519** | **110,963** |
| Yasmin Allen | **41,753** | **-** | **-** | **-** | **41,753** | **40,087** |
| Michael Wilkins | **2,048,030** | **154,050** | **679,448** | **-** | **2,881,528** | **1,207,840** |
| Andy Cornish | **203,081** | **49,900** | **282,128** | **(185,000)** | **350,109** | **-** |
| Alex Harrison | **-** | **-** | **-** | **-** | **-** | **-** |
| Leona Murphy | **340,660** | **50,850** | **244,090** | **99** | **635,699** | **114,644** |

(a) Net movement of shares relates to acquisition and disposal transactions by the KMP and their related parties during the year.
(b) Shares nominally held are included in the column headed total shares held at 30 June and include those held by the KMP's related parties, inclusive of domestic partner, dependants and entities controlled, jointly controlled or significantly influenced by the KMP.
(c) Opening number of shares held represents the balance as at the date of appointment.
(d) Information on shares held is disclosed up to the date of cessation.

### II. Movements in total number of convertible preference shares

Philip Twyman acquired 994 (2015-1,100) convertible preference shares during the year, indirectly holding a total of 5,109 shares as at 30 June 2016. No other key management personnel had any interest directly or nominally in convertible preference shares at any time during the financial year (2015-nil).

### III. Movements in total number of reset exchangeable securities held

No key management personnel had any interest directly or nominally in reset exchangeable securities of IAG Finance (New Zealand) Limited at any time during the financial year (2015-nil).

**J. KEY TERMS AND DEFINITIONS**

The key terms and definitions used throughout this report are explained below:

| TERM | DEFINITION |
|---|---|
| Actual remuneration | The dollar value of remuneration actually received by the Executives in the financial year. This is the sum of fixed pay plus the cash portion of the STI plus the value of DAR vested during the year plus the value of EPR vested during the year. |
| At-risk remuneration | Remuneration that is dependent on a combination of the financial performance of the Group, the Executives' performance against individual measures (financial and non-financial) and continuing employment. At-risk remuneration typically includes STI (cash and deferred remuneration) and LTI. |
| Balanced scorecard | The balanced scorecard sets out the objectives that have to be achieved to meet key strategic priorities of the organisation. All balanced scorecards use goals set against financial and non financial objectives. Achievement against these objectives is measured and this informs the Board's determination of STI outcomes. |
| Base salary | The cash component of fixed pay. |
| Cash return on equity (ROE) | Calculated as cash earnings divided by average total shareholders' equity during the financial year. Cash earnings is defined as net profit after tax attributable to IAG shareholders plus amortisation and impairment of acquired identifiable intangible assets and adjusted for unusual items after tax (non-recurring in nature). Cash ROE is used to calculate one half of the outcome in the LTI plan. |
| Cash STI | The two thirds portion of an Executive's STI outcome that is paid in the form of cash, following the end of year assessment and approval by the Board. |
| Deferred STI/Deferred Award Rights (DAR) | The one third portion of an Executive's STI that is deferred over a period of two years and awarded in the form of DAR. |
| Divisional Executives | The Executives with responsibility for managing a division, being the Chief Executive, Australian Consumer Division; Chief Executive, Australian Business Division; Chief Executive, New Zealand; and Chief Executive, Asia. |
| Executive team | The Divisional and Group Executives who form part of the Group Leadership Team. |
| Executives | The Group CEO and the Executive team. |
| Fixed Pay | Base salary plus superannuation. Individuals can determine the mix of base salary and superannuation they receive in line with legislative requirements. |
| Group CEO | IAG's Managing Director and Chief Executive Officer. |
| Group Executives | The Chief Financial Officer; Chief Operating Officer; Chief Risk Officer; Chief Customer Officer; Group Executive, Digital & Technology; Group Executive, Office of the CEO; Group General Counsel & Company Secretary; and Group Executive, People, Performance & Reputation. |
| IAG Spirit | The IAG Spirit, Closer, Braver, Faster is a set of statements that capture a shared view across IAG of how we work together, what we stand for and what makes us unique. |
| Key management personnel (KMP) | The Group CEO, the Executive team and the Board. |
| Long term incentive (LTI)/Executive Performance Rights (EPR) | A grant of rights in the form of EPR that is exercisable for IAG ordinary shares or cash between three and four years after the grant date if performance hurdles are achieved. |
| People and Remuneration Committee (PARC) | The Board committee which oversees IAG's remuneration practices. |
| Short term incentive (STI) | The part of annual at-risk remuneration that is designed to motivate and reward for annual performance. STI results are determined by performance against a balanced scorecard, based on goals which reflect financial and non-financial measures. For the Group CEO and the Executive team, one third of STI is deferred for a period of two years and two thirds is paid in cash in September. |
| Total shareholder return (TSR) | Used as one measure of Group performance over a period of time. TSR combines share price appreciation and dividends paid to show total return to shareholders, relative to that of other companies in the peer group. IAG uses relative TSR performance to calculate one half of the LTI outcome. |
| WACC | Weighted average cost of capital. |

## RELEVANT INTEREST OF EACH DIRECTOR AND THEIR RELATED PARTIES IN LISTED SECURITIES OF THE IAG GROUP IN ACCORDANCE WITH THE CORPORATIONS ACT 2001

### HOLDINGS OF SHARES AND RESET EXCHANGEABLE SECURITIES FOR SECTION 205G OF THE CORPORATIONS ACT 2001

| | Ordinary Shares | | Convertible Preference Shares | | Reset Exchangeable Securities | |
|---|---|---|---|---|---|---|
| | Held directly[(a)] | Held indirectly[(b)] | Held directly | Held indirectly | Held directly | Held indirectly |
| Elizabeth Bryan | - | **32,725** | - | - | - | - |
| Alison Deans | - | **37,742** | - | - | - | - |
| Hugh Fletcher | **36,561** | **45,471** | - | - | - | - |
| Raymond Lim | - | **35,000** | - | - | - | - |
| Jonathan Nicholson | **10,427** | **1,041** | - | - | - | - |
| Tom Pockett | **32,251** | - | - | - | - | - |
| Philip Twyman | **2,742** | **12,780** | - | **5,109** | - | - |
| Peter Harmer | **483,167** | **172,800** | - | - | - | - |

(a) This represents the relevant interest of each Director in ordinary shares issued by the Company, as notified by the Directors to the ASX in accordance with section 205G of the Corporations Act 2001 until the date the financial report is signed. Trading in IAG shares is covered by the restrictions which limit the ability of an IAG Director to trade in the securities of the Group where they are in a position to be aware, or are aware, of price sensitive information.

(b) These IAG shares are held by the Director's related parties, inclusive of entities controlled, jointly controlled or significantly influenced by the Directors, as notified by the Directors to the ASX in accordance with section 205G of the Corporations Act 2001.

## ROUNDING OF AMOUNTS

Unless otherwise stated, amounts in the financial report and Directors' Report have been rounded to the nearest million dollars. The Company is of a kind referred to in the ASIC Corporations Instrument 2016/191 dated 24 March 2016 issued by the Australian Securities & Investments Commission. All rounding has been conducted in accordance with that instrument.

This report meets the remuneration reporting requirements of the Corporations Act 2001 and Accounting Standard AASB 124 Related Party Disclosures. The term remuneration used in this report has the same meaning as compensation as prescribed in AASB 124.

Signed at Sydney this 19th day of August 2016 in accordance with a resolution of the Directors.

**Peter Harmer**
Director

# LEAD AUDITOR'S INDEPENDENCE DECLARATION

**UNDER SECTION 307C OF THE CORPORATIONS ACT 2001**

**TO THE DIRECTORS OF INSURANCE AUSTRALIA GROUP LIMITED**

I declare that, to the best of my knowledge and belief, in relation to the audit for the financial year ended 30 June 2016 there have been:

- no contraventions of the auditor independence requirements as set out in the Corporations Act 2001 in relation to the audit; and
- no contraventions of any applicable code of professional conduct in relation to the audit.

KPMG

**KPMG**

**Dr Andries B Terblanché**
Partner

Sydney
19 August 2016

# CONSOLIDATED FINANCIAL STATEMENTS

# CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

**FOR THE YEAR ENDED 30 JUNE 2016**

| | NOTE | 2016 $m | 2015 $m |
|---|---|---|---|
| Gross earned premium | 2.1 | 11,411 | 11,525 |
| Outwards reinsurance premium expense | | (3,883) | (1,196) |
| Net earned premium (i) | | 7,528 | 10,329 |
| Claims expense | | (8,500) | (9,363) |
| Reinsurance and other recoveries revenue | 2.1 | 3,798 | 2,422 |
| Net claims expense (ii) | 2.2 | (4,702) | (6,941) |
| Commission expense | | (1,039) | (1,043) |
| Underwriting expense | | (1,822) | (1,856) |
| Reinsurance commission revenue | 2.1 | 745 | 52 |
| Net underwriting expense (iii) | | (2,116) | (2,847) |
| Underwriting profit/(loss) (i) + (ii) + (iii) | | 710 | 541 |
| Investment income on assets backing insurance liabilities | 2.3 | 484 | 585 |
| Investment expenses on assets backing insurance liabilities | | (21) | (23) |
| Insurance profit/(loss) before capitalised software accelerated amortisation and impairment | | 1,173 | 1,103 |
| Capitalised software accelerated amortisation and impairment expense | 5.1 | (198) | - |
| Insurance profit/(loss) | | 975 | 1,103 |
| Investment income on shareholders' funds | 2.3 | 113 | 231 |
| Fee and other income | | 204 | 187 |
| Share of net profit/(loss) of associates | | 17 | 6 |
| Finance costs | | (99) | (107) |
| Fee based, corporate and other expenses | | (285) | (465) |
| Net income/(loss) attributable to non-controlling interests in unitholders' funds | | (5) | (6) |
| Profit/(loss) before income tax | | 920 | 949 |
| Income tax (expense)/credit | 5.2 | (218) | (119) |
| Profit/(loss) for the year | | 702 | 830 |
| **OTHER COMPREHENSIVE INCOME AND (EXPENSE)** | | | |
| **Items that may be reclassified subsequently to profit or loss:** | | | |
| Net movement in foreign currency translation reserve, net of tax | | 65 | (78) |
| **Items that will not be reclassified to profit or loss:** | | | |
| Remeasurements of defined benefit plans, net of tax | | (32) | 15 |
| Other comprehensive income and (expense), net of tax | | 33 | (63) |
| Total comprehensive income and (expense) for the year, net of tax | | 735 | 767 |
| **PROFIT/(LOSS) FOR THE YEAR ATTRIBUTABLE TO** | | | |
| Shareholders of the Parent | | 625 | 728 |
| Non-controlling interests | | 77 | 102 |
| Profit/(loss) for the year | | 702 | 830 |
| **TOTAL COMPREHENSIVE INCOME AND (EXPENSE) FOR THE YEAR ATTRIBUTABLE TO** | | | |
| Shareholders of the Parent | | 658 | 665 |
| Non-controlling interests | | 77 | 102 |
| Total comprehensive income and (expense) for the year, net of tax | | 735 | 767 |

| | NOTE | 2016 cents | 2015 cents |
|---|---|---|---|
| **EARNINGS PER SHARE** | | | |
| Basic earnings per ordinary share | 4.3 | 25.79 | 31.22 |
| Diluted earnings per ordinary share | 4.3 | 25.34 | 30.45 |

The above consolidated statement of comprehensive income should be read in conjunction with the notes to the financial statements.

# CONSOLIDATED BALANCE SHEET

## AS AT 30 JUNE 2016

| | NOTE | 2016 $m | 2015 $m |
|---|---|---|---|
| **ASSETS** | | | |
| Cash held for operational purposes | 8.1 | **263** | 306 |
| Investments | 2.3 | **12,946** | 15,535 |
| Trade and other receivables | 2.6 | **4,321** | 3,904 |
| Current tax assets | | **54** | - |
| Reinsurance and other recoveries on outstanding claims | 2.2 | **4,689** | 3,713 |
| Deferred insurance expenses | 2.5 | **2,778** | 2,838 |
| Deferred levies and charges | | **131** | 116 |
| Deferred tax assets | 5.2 | **603** | 499 |
| Property and equipment | | **204** | 235 |
| Other assets | | **145** | 134 |
| Investment in joint venture and associates | 6.4 | **486** | 561 |
| Goodwill and intangible assets | 5.1 | **3,410** | 3,561 |
| Total assets | | **30,030** | 31,402 |
| **LIABILITIES** | | | |
| Trade and other payables | 2.7 | **2,346** | 2,761 |
| Current tax liabilities | | **5** | 109 |
| Unearned premium liability | 2.4 | **6,220** | 6,156 |
| Outstanding claims liability | 2.2 | **11,741** | 12,687 |
| Non-controlling interests in unitholders' funds | | **247** | 198 |
| Provisions | 5.3 | **370** | 383 |
| Other liabilities | | **354** | 328 |
| Interest bearing liabilities | 4.1 | **1,962** | 1,762 |
| Total liabilities | | **23,245** | 24,384 |
| Net assets | | **6,785** | 7,018 |
| **EQUITY** | | | |
| Share capital | 4.2 | **7,275** | 7,275 |
| Treasury shares held in trust | | **(43)** | (83) |
| Reserves | | **32** | (38) |
| Retained earnings | | **(701)** | (337) |
| Parent interest | | **6,563** | 6,817 |
| Non-controlling interests | | **222** | 201 |
| Total equity | | **6,785** | 7,018 |

The above consolidated balance sheet should be read in conjunction with the notes to the financial statements.

# CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

**FOR THE YEAR ENDED 30 JUNE 2016**

| | SHARE CAPITAL $m | TREASURY SHARES HELD IN TRUST $m | FOREIGN CURRENCY TRANSLATION RESERVE $m | SHARE BASED REMUN-ERATION RESERVE $m | RETAINED EARNINGS $m | NON-CONTROLLING INTERESTS $m | TOTAL EQUITY $m |
|---|---|---|---|---|---|---|---|
| **2016** | | | | | | | |
| Balance at the beginning of the financial year | **7,275** | **(83)** | **(68)** | **30** | **(337)** | **201** | **7,018** |
| Profit/(loss) for the year | **-** | **-** | **-** | **-** | **625** | **77** | **702** |
| Other comprehensive income and (expense) | **-** | **-** | **65** | **-** | **(32)** | **-** | **33** |
| Total comprehensive income/(expense) for the year | **-** | **-** | **65** | **-** | **593** | **77** | **735** |
| **Transactions with owners in their capacity as owners** | | | | | | | |
| Share based remuneration | **-** | **40** | **-** | **5** | **(12)** | **-** | **33** |
| Dividends determined and paid | **-** | **-** | **-** | **-** | **(948)** | **(56)** | **(1,004)** |
| Dividends received on treasury shares held in trust | **-** | **-** | **-** | **-** | **3** | **-** | **3** |
| Balance at the end of the financial year | **7,275** | **(43)** | **(3)** | **35** | **(701)** | **222** | **6,785** |
| 2015 | | | | | | | |
| Balance at the beginning of the financial year | 6,775 | (94) | 10 | 28 | (151) | 226 | 6,794 |
| Profit/(loss) for the year | - | - | - | - | 728 | 102 | 830 |
| Other comprehensive income and (expense) | - | - | (78) | - | 15 | - | (63) |
| Total comprehensive income/(expense) for the year | - | - | (78) | - | 743 | 102 | 767 |
| **Transactions with owners in their capacity as owners** | | | | | | | |
| Shares issued under institutional placement, net of transaction costs | 500 | - | - | - | - | - | 500 |
| Share based remuneration | - | 11 | - | 2 | (20) | - | (7) |
| Non-controlling interests in acquisitions during the year | - | - | - | - | - | 2 | 2 |
| Dividends determined and paid | - | - | - | - | (913) | (129) | (1,042) |
| Dividends received on treasury shares held in trust | - | - | - | - | 4 | - | 4 |
| Balance at the end of the financial year | 7,275 | (83) | (68) | 30 | (337) | 201 | 7,018 |

The above consolidated statement of changes in equity should be read in conjunction with the notes to the financial statements.

# CONSOLIDATED CASH FLOW STATEMENT

## FOR THE YEAR ENDED 30 JUNE 2016

| | NOTE | 2016 $m | 2015 $m |
|---|---|---|---|
| **CASH FLOWS FROM OPERATING ACTIVITIES** | | | |
| Premium received | | **11,310** | 11,503 |
| Reinsurance and other recoveries received | | **2,170** | 1,938 |
| Claims costs paid | | **(9,447)** | (8,736) |
| Outwards reinsurance premium expense paid | | **(4,029)** | (1,427) |
| Dividends, interest and trust distributions received | | **525** | 594 |
| Finance costs paid | | **(95)** | (102) |
| Income taxes paid | | **(388)** | (351) |
| Other operating receipts | | **1,582** | 884 |
| Other operating payments | | **(3,574)** | (3,605) |
| Net cash flows from operating activities | 8.1 | **(1,946)** | 698 |
| **CASH FLOWS FROM INVESTING ACTIVITIES** | | | |
| Net cash flows on acquisition of subsidiaries and associates | | **5** | (162) |
| Net cash flows from sale/(purchase) of investments and plant and equipment | | **2,362** | (1,530) |
| Net cash flows from investing activities | | **2,367** | (1,692) |
| **CASH FLOWS FROM FINANCING ACTIVITIES** | | | |
| Proceeds from issue of shares, net of transaction costs | | **-** | 500 |
| Outlays for purchase of treasury shares | | **-** | (35) |
| Proceeds from borrowings | | **326** | - |
| Repayment of borrowings | | **(131)** | - |
| Net cash flow from issue and redemption of trust units | | **45** | 1 |
| Dividends paid to IAG shareholders | | **(948)** | (913) |
| Dividends paid to non-controlling interests | | **(56)** | (129) |
| Dividends received on treasury shares | | **3** | 4 |
| Net cash flows from financing activities | | **(761)** | (572) |
| Net movement in cash held | | **(340)** | (1,566) |
| Effects of exchange rate changes on balances of cash held in foreign currencies | | **11** | (11) |
| Cash and cash equivalents at the beginning of the financial year | | **1,433** | 3,010 |
| Cash and cash equivalents at the end of the financial year | 8.1 | **1,104** | 1,433 |

The above consolidated cash flow statement should be read in conjunction with the notes to the financial statements.

# NOTES TO THE FINANCIAL STATEMENTS

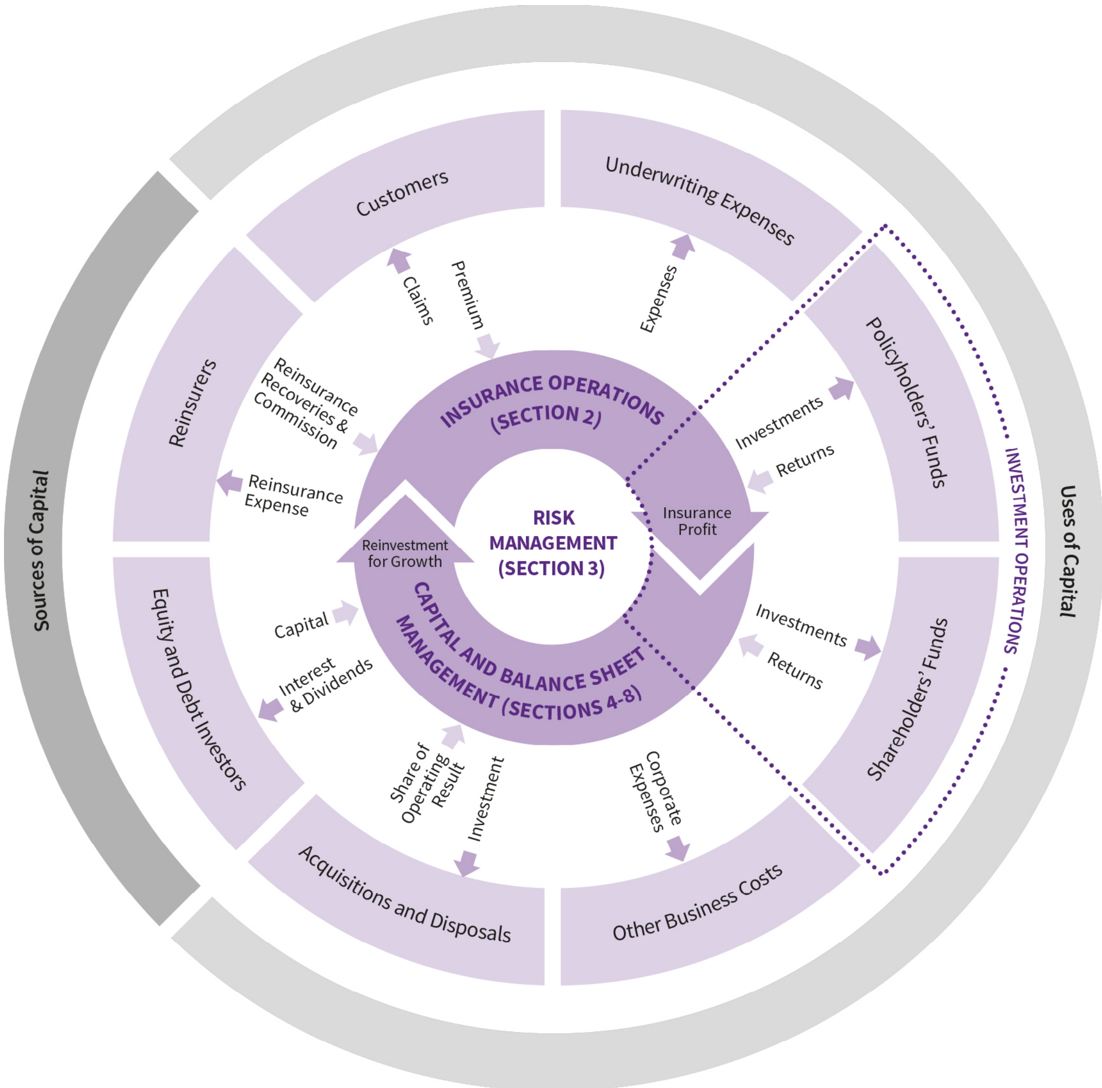
## 1. OVERVIEW

### NOTE 1.1 INTRODUCTION

The financial report is structured to provide prominence to the disclosures that are considered most relevant to the users' understanding of the operations, results and financial position of the Group.

The financial report has been organised into the following sections:

1. Overview - contains information that affects the financial report as a whole, as well as segment reporting disclosures.
2. Insurance disclosures - financial statement disclosures considered most relevant to the core insurance activities.
3. Risk - discusses the Group's exposure to various risks, explains how these affect the Group's financial position and performance and how the Group seeks to manage and mitigate these risks.
4. Capital structure - provides information about the capital management practices of the Group and related shareholder returns.
5. Other balance sheet disclosures - discusses other balance sheet items such as goodwill and intangible assets, as well as disclosures in relation to the Group's tax balances.
6. Group structure - provides a summary of the Group's controlled entities and includes acquisition and divestment disclosure.
7. Off-balance sheet disclosures - disclosure of items not recognised in the financial statements at the balance date but which could potentially have a significant impact on the Group's financial position and performance going forward.
8. Additional disclosures - other disclosures required to comply with Australian Accounting Standards.



# NOTE 1.2 ABOUT THIS REPORT

## A. CORPORATE INFORMATION

Insurance Australia Group Limited (IAG, Parent or Company), the ultimate parent entity in the Consolidated entity, is a for-profit company incorporated and domiciled in Australia and limited by shares publicly traded on the Australian Securities Exchange (ASX). Its registered office and principal place of business is Level 26, 388 George Street, Sydney, NSW 2000, Australia. This financial report covers the consolidated financial statements for the Company and its subsidiaries (Group or Consolidated entity) for the year ended 30 June 2016.

A description of the nature of the Group's operations and its principal activities is included in the Directors' Report.

## B. STATEMENT OF COMPLIANCE

This general purpose financial report was authorised by the Board of Directors for issue on 19 August 2016 and complies with International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board, the Corporations Act 2001, Australian Accounting Standards (AASBs) adopted by the Australian Accounting Standards Board (AASB), other authoritative pronouncements of the AASB and the ASX Listing Rules.

The current IFRS standard for insurance contracts does not include a comprehensive set of recognition and measurement criteria. The IASB continues to work on a project to issue a standard that does include such criteria. Until the issuance of that standard, the financial reports of insurers in different countries that comply with IFRS may not be comparable in terms of the recognition and measurement of insurance contracts.

## C. BASIS OF PREPARATION

The financial statements have been prepared on the basis of historical cost principles, as modified by certain exceptions noted in the financial report, with the principal exceptions being the measurement of all investments and derivatives at fair value and the measurement of the outstanding claims liability and related reinsurance and other recoveries at present value. All values are rounded to the nearest million dollars, unless otherwise stated, in accordance with ASIC Corporations Instrument 2016/191.

The balance sheet is prepared with the assets and liabilities presented broadly in order of liquidity. The assets and liabilities comprise both current amounts (expected to be recovered or settled within 12 months after the reporting date) and non-current amounts (expected to be recovered or settled more than 12 months after the reporting date).

### I. Basis of consolidation

The consolidated financial statement incorporates the assets and liabilities of all entities controlled by the Company as at 30 June 2016. A list of significant controlled entities is set out in note 6.2 details of subsidiaries. IAG controls an investee if it has (i) power over the investee; (ii) exposure, or rights, to variable returns from its involvement with the investee; and (iii) the ability to use its power over the investee to affect the amount of those returns. Where an entity either began or ceased to be controlled during a financial year, the results are included from the date control commenced or up to the date control ceased. The financial information of all subsidiaries is prepared for consolidation for the same reporting year as the Parent. In preparing the consolidated financial statements, all inter-company balances and transactions, including income, expenses, and profits and losses resulting from intra-Group transactions, have been eliminated.

Where a subsidiary is less than wholly owned, the equity interests held by external parties are presented separately as non-controlling interests on the consolidated balance sheet, except when presented as a liability where the subsidiary is a trust or similar entity. A change in ownership of a controlled entity that results in no gain or loss of control is accounted for as an equity transaction.

### II. Presentation and foreign currency

The financial report is presented in Australian dollars, which is the functional currency of the Company. Foreign currency transactions are translated into Australian dollars using the exchange rates prevailing at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at reporting date are translated to Australian dollars using reporting date exchange rates. Resulting exchange differences are recognised in profit or loss.

The assets and liabilities of foreign operations are translated to Australian dollars using reporting date exchange rates while equity items are translated using historical rates. The consolidated statement of comprehensive income and consolidated cash flow statement are translated using annual average rates for the reporting year. Exchange rate differences arising on translation are recorded directly in equity in the foreign currency translation reserve (FCTR). On the disposal of a foreign operation, the cumulative amount of exchange differences deferred in the FCTR relating to that foreign operation is recognised in profit or loss.

### III. Changes to comparatives

As a result of the reorganisation of the financial report, certain comparative items have been reclassified from the Consolidated entity's prior year financial report to conform to the current period's presentation.

### D. SIGNIFICANT ACCOUNTING POLICIES ADOPTED

The accounting policies adopted in the preparation of this financial report have been applied consistently by all entities in the Group and are the same as those applied for the previous reporting year, unless otherwise stated. The financial statements of entities operating outside Australia that maintain accounting records in accordance with overseas accounting principles are adjusted where necessary to comply with the significant accounting policies of the Consolidated entity. The significant accounting policies adopted in the preparation of this financial report are set out within the relevant note.

#### I. Changes in accounting policies

There were new Australian Accounting Standards and Interpretations applicable for the current reporting year, with no material financial impact to the Group on adoption. Refer to note 8.5 impact of new Australian Accounting Standards issued for further details.

#### II. Critical accounting estimates and judgements

In the process of applying the significant accounting policies, certain critical accounting estimates and assumptions are applied and judgements are made by management, the results of which affect the amounts recognised in the financial statements. The estimates and related assumptions are based on experience and other factors that are considered to be reasonable, and are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which they are revised, and future periods if relevant. Details of the material estimates and judgements are set out with the relevant note, as outlined below.

| AREAS OF CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS | REFERENCE |
|---|---|
| Claims and reinsurance and other recoveries on outstanding claims | Note 2.2 |
| Liability adequacy test | Note 2.4 |
| Intangible assets and goodwill impairment testing, initial measurement and useful life | Note 5.1 |
| Income tax and related assets and liabilities | Note 5.2 |
| Acquisitions and disposals of businesses | Note 6.1 |

## NOTE 1.3 SEGMENT REPORTING

The Consolidated entity has identified its operating segments based on the internal reports that are reviewed and used by the Chief Executive Officer (being the chief operating decision maker) in assessing performance and in determining the allocation of resources. The operating segments are the source of major risks and have the most effect on the rates of return.

### A. CHANGES DURING THE YEAR

Titles of the Australian divisions have been amended to reflect the organisational structure effective from 9 December 2015. In effect, IAG continues to report its financial results using its pre-existing profit segments, as the financial performance and resource allocation decisions continue to be made on this basis.

### B. REPORTABLE SEGMENTS

The Consolidated entity has general insurance operations in Australia, New Zealand and Asia, with the reportable segments comprising the following business divisions:

#### I. Consumer division (Australia)

This segment provides general insurance products to individuals and families throughout Australia, primarily under the NRMA Insurance, SGIO, SGIC and CGU brands, under the RACV brand in Victoria (via a distribution and underwriting relationship with RACV) and the Coles Insurance brand nationally (via a distribution agreement with Coles).

#### II. Business division (Australia)

This segment provides commercial insurance to businesses of all sizes throughout Australia, predominantly under the CGU, WFI, and Swann Insurance brands through intermediaries including brokers, authorised representatives and distribution partners.

#### III. New Zealand

This segment provides general insurance business underwritten in New Zealand. Insurance products are sold directly to customers predominantly under the State and AMI brands, and through intermediaries (insurance brokers and authorised representatives) primarily using the NZI and Lumley Insurance brands. Personal and commercial products are also distributed by corporate partners, such as large financial institutions, using third party brands.

#### IV. Asia

This segment provides direct and intermediated insurance business underwritten through subsidiaries in Thailand, Vietnam and Indonesia and the share of the operating result from the investment in associates in Malaysia and India. The businesses offer personal and commercial insurance products through local brands.

#### V. Corporate and other

This segment comprises other activities, including corporate services, capital management activity, placement of the Group's reinsurance program, inward reinsurance from associates and all investment activities.

## C. FINANCIAL INFORMATION

| | AUSTRALIA CONSUMER DIVISION $m | AUSTRALIA BUSINESS DIVISION $m | NEW ZEALAND $m | ASIA $m | CORPORATE AND OTHER $m | TOTAL $m |
|---|---|---|---|---|---|---|
| **2016** | | | | | | |
| **I. Financial performance** | | | | | | |
| Total external revenue[(a)] | **7,956** | **4,563** | **2,791** | **513** | **949** | **16,772** |
| Underwriting profit/(loss) | **544** | **41** | **128** | **2** | **(5)** | **710** |
| Net investment income on technical reserves | **261** | **189** | **7** | **5** | **1** | **463** |
| Insurance profit/(loss) before capitalised software accelerated amortisation and impairment | **805** | **230** | **135** | **7** | **(4)** | **1,173** |
| Capitalised software accelerated amortisation and impairment expense | **-** | **-** | **-** | **-** | **(198)** | **(198)** |
| Net investment income on shareholders' funds | **-** | **-** | **-** | **-** | **97** | **97** |
| Share of net profit/(loss) of associates | **-** | **1** | **-** | **19** | **(3)** | **17** |
| Finance costs | **-** | **-** | **-** | **-** | **(99)** | **(99)** |
| Other net operating result | **-** | **4** | **1** | **-** | **(75)** | **(70)** |
| Total segment result | **805** | **235** | **136** | **26** | **(282)** | **920** |
| Income tax expense | | | | | | **(218)** |
| Profit/(loss) for the year | | | | | | **702** |
| **II. Other segment information** | | | | | | |
| Capital expenditure[(b)] | **-** | **-** | **-** | **-** | **189** | **189** |
| Depreciation, amortisation and impairment expense | **57** | **87** | **49** | **3** | **198** | **394** |
| 2015 | | | | | | |
| **I. Financial performance** | | | | | | |
| Total external revenue[(a)] | 6,904 | 4,023 | 3,349 | 483 | 249 | 15,008 |
| Underwriting profit/(loss) | 505 | (110) | 154 | (8) | - | 541 |
| Net investment income on technical reserves | 283 | 203 | 62 | 13 | 1 | 562 |
| Insurance profit/(loss) | 788 | 93 | 216 | 5 | 1 | 1,103 |
| Net investment income on shareholders' funds | - | - | - | - | 223 | 223 |
| Share of net profit/(loss) of associates | - | - | - | 16 | (10) | 6 |
| Finance costs | - | - | - | - | (107) | (107) |
| Other net operating result | - | 16 | 4 | - | (296) | (276) |
| Total segment result | 788 | 109 | 220 | 21 | (189) | 949 |
| Income tax expense | | | | | | (119) |
| Profit/(loss) for the year | | | | | | 830 |
| **II. Other segment information** | | | | | | |
| Capital expenditure[(b)] | - | - | - | - | 315 | 315 |
| Depreciation and amortisation expense | 53 | 90 | 52 | 11 | - | 206 |

(a) Total external revenue comprises premium revenue, reinsurance and other recoveries, reinsurance commission revenue, investment income on assets backing insurance liabilities, investment income on shareholders' funds, fee and other income and share of net profit/(loss) of associates.

(b) Capital expenditure includes acquisitions of property and equipment, intangibles and other non-current segment assets.

# 2. INSURANCE DISCLOSURES

**SECTION INTRODUCTION**

This section provides an overview of the Group's general insurance operations, which are the main driver of the Group's overall performance and financial position.

The Group collects premium and recognises revenue for the insurance policies it underwrites. From this, the Group pays amounts to customers on settlement of insurance claims, with the claims expense representing the largest cost to the Group, as well as operating costs, which include the costs associated with obtaining and recording insurance contracts.

To mitigate the Group's overall risk and optimise its return profile, the Group passes some of its underwriting exposure to third parties (primarily reinsurance companies). The premiums paid to reinsurers are an expense to the Group, whereas recoveries under the reinsurance contracts are recognised as revenue. These recoveries can either be in relation to operating costs (reinsurance commission) or underwriting risk (reinsurance recoveries).

Investment activities are an integral part of the insurance business. The funds received from the collection of premium are invested as a key source of return for the Group under a sound investment philosophy. The Group starts investing insurance premiums as soon as they are collected and continues to generate returns until claims or other expenses are paid out.

The underwriting result measures the profit (or loss) generated from underwriting activities in a given period. The Insurance result, which is a key performance metric, adds the net investment return to the underwriting result to derive the overall pre-tax profit (or loss) from insurance operations.

## NOTE 2.1 GENERAL INSURANCE REVENUE

| | **2016** | 2015 |
|---|---|---|
| | **\$m** | \$m |
| **A. COMPOSITION** | | |
| Gross written premium | **11,367** | 11,440 |
| Movement in unearned premium liability | **44** | 85 |
| Premium revenue | **11,411** | 11,525 |
| Reinsurance and other recoveries revenue | **3,798** | 2,422 |
| Reinsurance commission revenue | **745** | 52 |
| Total general insurance revenue | **15,954** | 13,999 |

### B. RECOGNITION AND MEASUREMENT

**I. Premium revenue**

Premiums written are earned through the profit or loss in line with the incidence of the pattern of risk. The majority of premium is earned according to the passage of time (e.g. for a one year policy, 1/365th of premium written will be earned each day).

**II. Reinsurance and other recoveries**

The recognition and measurement criteria for reinsurance and other recoveries revenue is referred to in note 2.2 claims and reinsurance and other recoveries on outstanding claims.

**III. Reinsurance commission revenue**

Reinsurance commission revenue includes reimbursements by reinsurers to cover a share of IAG’s operating costs and, where applicable, fee income which reinsurers pay for accessing IAG's franchise. These income items are recognised broadly in line with the reference premium over the term of the reinsurance agreements. Where applicable, the reinsurance commission revenue also includes income which is based on the expected profitability of the covered business ceded to the reinsurer. This income is recognised over the term of the reinsurance contract on a systematic basis.

## NOTE 2.2 CLAIMS AND REINSURANCE AND OTHER RECOVERIES ON OUTSTANDING CLAIMS

### A. NET CLAIMS EXPENSE

| | Current year | Prior years | 2016 Total | Current year | Prior years | 2015 Total |
|---|---|---|---|---|---|---|
| | $m | $m | $m | $m | $m | $m |
| Gross claims - undiscounted | **8,934** | **(786)** | **8,148** | 8,956 | 199 | 9,155 |
| Discount | **(165)** | **517** | **352** | (205) | 413 | 208 |
| Gross claims - discounted | **8,769** | **(269)** | **8,500** | 8,751 | 612 | 9,363 |
| Reinsurance and other recoveries - undiscounted | **(3,128)** | **(949)** | **(4,077)** | (1,651) | (734) | (2,385) |
| Discount | **302** | **(23)** | **279** | 61 | (98) | (37) |
| Reinsurance and other recoveries - discounted | **(2,826)** | **(972)** | **(3,798)** | (1,590) | (832) | (2,422) |
| Net claims expense | **5,943** | **(1,241)** | **4,702** | 7,161 | (220) | 6,941 |

### B. NET OUTSTANDING CLAIMS LIABILITY

#### I. Composition of net outstanding claims liability

| | 2016 | 2015 |
|---|---|---|
| | $m | $m |
| Gross central estimate - discounted | **9,548** | 10,503 |
| Reinsurance and other recoveries - discounted | **(4,009)** | (3,494) |
| Net central estimate - discounted | **5,539** | 7,009 |
| Claim handling costs - discounted | **384** | 406 |
| Risk margin | **1,129** | 1,559 |
| Net outstanding claims liability - discounted | **7,052** | 8,974 |

The outstanding claim liability includes $6,940 million (2015-$6,977 million) which is expected to be settled more than 12 months from the reporting date.

The carrying value of reinsurance and other recoveries includes $2,694 million (2015-$1,839 million) which is expected to be settled more than 12 months from the reporting date.

During the second half of the financial year the Group completed a reinsurance arrangement in respect of liability and workers' compensation risks with exposure to asbestos. This transaction has reduced the overall risk attaching to the Group's net outstanding claims liability and has resulted in a substantial reduction in the quantum of the risk margin the Group is required to hold. It has also led to a reduction in the discounted average term to settlement of claims, and the resultant interest rate sensitivities, both for the Group but particularly the Australia Business Division (to 2.5 years from 4.4 years).

#### II. Reconciliation of movements in net discounted outstanding claims liability

| | 2016 | 2015 |
|---|---|---|
| | $m | $m |
| Net outstanding claims liability at the beginning of the financial year | **8,974** | 8,758 |
| Movement in the prior year central estimate | **(580)** | (127) |
| Current year claims incurred, net of reinsurance and other recoveries | **5,474** | 6,896 |
| Claims paid, net of reinsurance and other recoveries received | **(6,703)** | (6,744) |
| Movement in discounting | **224** | 273 |
| Movement in risk margin | **(431)** | (37) |
| Addition through business acquisition | **-** | 4 |
| Net foreign currency movements | **94** | (49) |
| Net outstanding claims liability at the end of the financial year | **7,052** | 8,974 |
| Reinsurance and other recoveries on outstanding claims liability | **4,689** | 3,713 |
| Gross outstanding claims liability at the end of the financial year | **11,741** | 12,687 |

**III. Maturity analysis**
Refer to note 3.1 risk and capital management for details of the maturity profile of the estimated net discounted outstanding claims liability based on the remaining term to payment at the reporting date.

**IV. Development table**
Claims will often take a number of years to be settled from the date the original loss occurred. The following table shows the development of the net undiscounted ultimate claims for all claims for the ten most recent accident years and a reconciliation to the net discounted outstanding claims liability. This table provides the user with an overview of how the Group's estimates of total claim amounts payable in relation to a given year have evolved over time. If the estimate of ultimate claims in relation to a given accident year declines over time, this suggests claims have developed more favourably than was anticipated at the time the original reserving assumptions were set.

Where an entity or business that includes an outstanding claim liability has been acquired the claims for the acquired businesses are included in the claims development table from and including the year of acquisition. The outstanding claims liability includes international operations. For ease of comparison within the claims development table, all payments not denominated in Australian dollars have been converted to Australian dollars using the applicable exchange rates at the reporting dates. Therefore, the claims development table disclosed each reporting year cannot be reconciled directly to the equivalent tables presented in previous years' financial statements.

| | | | | | | | | | | | Accident year |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | 2006 and prior | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | **2016** | Total |
| | $m | $m | $m | $m | $m | $m | $m | $m | $m | $m | **$m** | $m |
| NET ULTIMATE CLAIM PAYMENTS | | | | | | | | | | | | |
| Development | | | | | | | | | | | | |
| At end of accident year | | **4,790** | **4,713** | **4,727** | **4,677** | **5,028** | **5,227** | **5,187** | **5,637** | **6,320** | **4,986** | |
| One year later | | **4,760** | **4,673** | **4,765** | **4,651** | **5,144** | **5,302** | **5,111** | **5,641** | **6,247** | | |
| Two years later | | **4,718** | **4,668** | **4,701** | **4,549** | **5,187** | **5,243** | **5,030** | **5,555** | | | |
| Three years later | | **4,730** | **4,646** | **4,693** | **4,498** | **5,219** | **5,153** | **4,951** | | | | |
| Four years later | | **4,660** | **4,626** | **4,608** | **4,446** | **5,430** | **5,102** | | | | | |
| Five years later | | **4,585** | **4,556** | **4,555** | **4,393** | **5,505** | | | | | | |
| Six years later | | **4,559** | **4,545** | **4,510** | **4,358** | | | | | | | |
| Seven years later | | **4,549** | **4,530** | **4,471** | | | | | | | | |
| Eight years later | | **4,540** | **4,511** | | | | | | | | | |
| Nine years later | | **4,537** | | | | | | | | | | |
| Current estimate of net ultimate claim payments | | **4,537** | **4,511** | **4,471** | **4,358** | **5,505** | **5,102** | **4,951** | **5,555** | **6,247** | **4,986** | |
| Cumulative payments made to date | | **4,503** | **4,441** | **4,391** | **4,232** | **4,896** | **4,761** | **4,405** | **4,736** | **5,191** | **3,072** | |
| Net undiscounted outstanding claim liability | **202** | **34** | **70** | **80** | **126** | **609** | **341** | **546** | **819** | **1,056** | **1,914** | **5,797** |
| Discount to present value | **(14)** | **(2)** | **(5)** | **(5)** | **(8)** | **(19)** | **(19)** | **(28)** | **(41)** | **(56)** | **(61)** | **(258)** |
| Net discounted outstanding claim liability | **188** | **32** | **65** | **75** | **118** | **590** | **322** | **518** | **778** | **1,000** | **1,853** | **5,539** |
| Reconciliation | | | | | | | | | | | | |
| Claims handling costs | | | | | | | | | | | | **384** |
| Risk margin | | | | | | | | | | | | **1,129** |
| Net outstanding claim liability | | | | | | | | | | | | **7,052** |

## C. RECOGNITION AND MEASUREMENT

**I. Outstanding claims liability and claims expense**
Claims expense represents claim payments and the movement in the closing outstanding claims liability from one financial period to the next. Current year claims relate to loss events that occurred during the current financial year. Prior year claims represent the movement on the estimates held for claims that occurred in all previous financial periods.

The outstanding claims liability is determined based on three building blocks:
- a central estimate of the future cash flows;
- discounting for the effect of the time value of money; and
- a risk margin for uncertainty.

a. CENTRAL ESTIMATE OF THE FUTURE CASH FLOWS
The outstanding claims liability is measured as the central estimate of the expected future payments relating to claims incurred at the reporting date including direct and indirect claim handling costs. The liability is measured based on the advice and/or valuations performed by, or under the direction of, the Appointed Actuary, and is intended to contain no deliberate or conscious bias toward over or under estimation. Given the uncertainty in establishing the liability, it is likely that the final outcome will differ from the original liability established. Changes in claim estimates are recognised in profit or loss in the reporting year in which the estimates are changed.

b. DISCOUNTING
Projected future claims payments, both gross and net of reinsurance and other recoveries and associated claim handling costs, are discounted to a present value using risk free discount rates (derived from market yields on government securities) to reflect the time value of money.

c. RISK MARGIN
Given the uncertainty inherent in estimating future claim payments, it is considered appropriate to add a risk margin to the central estimate of expected future claim payments. The risk margin represents the amount by which the liability recognised in the financial statements is greater than the actuarial central estimate. IAG currently applies a 90% probability of adequacy to the outstanding claims liability. In effect this means there is approximately a 1-in-10 chance all future claims payments will exceed the overall reserve held.

Uncertainties surrounding the liability estimation process include those relating to the available data, actuarial models and assumptions, the statistical uncertainty associated with a general insurance claims run-off process, and risks external to IAG, for example the impact of future legislative reform. Uncertainty from these sources is examined for each class of business and expressed as a volatility measure relative to the net central estimate. The volatility measure for each class is derived after consideration of statistical modelling and benchmarking to industry analyses. Certain product classes may be subject to the emergence of new types of latent claims, and such uncertainties are considered when setting the volatility and hence the risk margin appropriate for those classes.

Long-tail classes of business generally have the highest volatilities for outstanding claims as the longer average time for claims to be reported and settled allows more time for sources of uncertainty to emerge. Short-tail classes generally have lower levels of volatility for outstanding claims.

The Group benefits from holding a portfolio diversified into many classes of business across different regions. The risk margin required to provide a given probability of adequacy for two or more classes of business or for two or more geographic locations combined is likely to be less than the sum of risk margins for the individual classes. This reflects the benefit of diversification. The level of diversification assumed between classes takes into account industry analysis, historical experience and the judgement of experienced and qualified actuaries.

The current risk margin and resultant overall probability of adequacy for the outstanding claims, which has been determined after assessing the inherent uncertainty in the central estimate, diversification and risks in the prevailing environment, is set out below:

| | **2016** | 2015 |
|---|---|---|
| | % | % |
| The percentage risk margin applied to the net outstanding claims liability | **19** | 21 |
| The probability of adequacy of the risk margin | **90** | 90 |

**II. Reinsurance and other recoveries on outstanding claims**
Reinsurance and other recoveries on outstanding claims are recognised as income with the corresponding asset being recognised on the balance sheet. Reinsurance and other recoveries on outstanding claims are measured as the present value (discounted using appropriate risk free discount rates) of the expected future receipts due as a result of the reinsurance protection that IAG has in place. The reporting date balance also includes the net GST receivable on outstanding claims.

## D. SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS

**I. Outstanding claims liability**
The estimation of the outstanding claims liability involves a number of key assumptions and is the most critical accounting estimate. The process involves using the Consolidated entity's specific data, relevant industry data and more general economic data. Each class of business is usually examined separately, and the process involves consideration of a large number of factors, including the risks to which the business is exposed at a point in time, claim frequencies and average claim sizes, historical trends in the incidence and development of claims reported and finalised, as well as legal, social and economic factors that may affect each class of business.

The estimation process of the gross cash flows for the 2011 financial year natural catastrophe events in New Zealand is subject to a higher degree of uncertainty owing to the unique nature of the events, but is determined in a manner consistent with that set out in the recognition and measurement section of this note. The uncertainties related to these events include allocation of costs between the various earthquake events (September 2010, February 2011 and June 2011) for policies affected by multiple events, claims under the Earthquake Commission (EQC) cap (NZ$100,000) which may subsequently exceed the cap, potential latent claims, outcomes of court cases and litigation, the impact of demand surge inflation, the interaction with the EQC and uncertainty relating to IAG's share of claim costs.

The following ranges of key actuarial assumptions were used in the measurement of outstanding claims and recoveries, where appropriate, within the operating segments at the reporting date.

| ASSUMPTION | AUSTRALIA CONSUMER DIVISION | AUSTRALIA BUSINESS DIVISION | NEW ZEALAND | ASIA |
|---|---|---|---|---|
| **2016** | | | | |
| Discounted average term to settlement | **2.9 years** | **2.5 years** | **0.9 years** | **0.3 years** |
| Inflation rate | **2.2%-4.0%** | **0.0%-4.5%** | **1.7%** | **0.0%-4.0%** |
| Superimposed inflation rate | **0.0%-5.0%** | **0.0%-5.0%** | **0.0%** | **0.0%** |
| Discount rate | **1.5%-4.5%** | **1.6%-3.2%** | **1.8%-2.3%** | **0.0%** |
| Claims handling costs ratio | **4.1%** | **4.6%** | **4.2%** | **1.9%** |
| 2015 | | | | |
| Discounted average term to settlement | 3.1 years | 4.4 years | 1.0 years | 0.4 years |
| Inflation rate | 2.3%-4.0% | 0.0%-4.5% | 2.0%-2.5% | 0.0%-4.0% |
| Superimposed inflation rate | 0.0%-5.0% | 0.0%-5.0% | 0.0% | 0.0% |
| Discount rate | 1.9%-4.8% | 1.9%-4.7% | 2.2%-3.3% | 0.0% |
| Claims handling costs ratio | 3.9% | 5.2% | 5.3% | 1.4% |

a. DISCOUNTED AVERAGE TERM TO SETTLEMENT
The discounted average term to settlement provides a summary indication of the expected future cash flow pattern for claims (inflated and discounted). It is calculated by class of business and is generally based on historic settlement patterns. A decrease in the discounted average term to settlement would reflect claims being paid sooner than anticipated and so would increase the claims expense. Note that this sensitivity test only extends or shortens the term of the payments assumed in the valuation, without changing the total nominal amount of the payments.

b. INFLATION RATE AND SUPERIMPOSED INFLATION
Payments of claims outstanding at the reporting date are to be made in the future and so need to take account of expected increases in the underlying cost of final claims settlements due to inflationary pressures. Economic inflation assumptions are set by reference to current economic indicators. Superimposed inflation tends to occur due to wider societal trends such as the cost of court settlements increasing at a faster rate than the economic inflation rate.

c. DISCOUNT RATE
An increase or decrease in the assumed discount rate will have a corresponding decrease or increase (respectively) on the claims expense recognised in the profit or loss.

d. CLAIMS HANDLING COSTS RATIO
This reflects the cost to administer future claims. The ratio is generally calculated with reference to the historical experience of claims handling costs as a percentage of past payments, together with budgeted future costs.

**II. Reinsurance and other recoveries on outstanding claims**
The measurement of reinsurance and other recoveries on outstanding claims is an inherently uncertain process involving estimates. The amounts are generally calculated using actuarial assumptions and methods similar to those used for the outstanding claims liability, with appropriate consideration of the credit risk of the counterparty. Accordingly, the valuation of outstanding reinsurance recoveries is subject to largely similar risks and uncertainties as the valuation of the outstanding claims liability. Significant individual losses, for example those relating to catastrophe events, are analysed on a case-by-case basis.

**E. SENSITIVITY ANALYSIS**
The impact on the net outstanding claims liabilities (net of reinsurance recoveries) before income tax to changes in key actuarial assumptions is summarised below. Each change has been calculated in isolation of the other changes, and without regard to other balance sheet changes that may occur simultaneously.

The movements are stated in absolute terms where the base assumption is a percentage. For example, if the base inflation rate assumption was 3.5%, a 1% increase would mean assuming a 4.5% inflation rate.

The general reduction in the quantum of sensitivity impacts, year-on-year, reflects the impact of the BH quota share. For Business Division, the impacts also reflect its lower net outstanding claims exposure to long-tail classes following the completion of the loss portfolio transfer in respect of its asbestos exposure.

| ASSUMPTION | MOVEMENT IN ASSUMPTION | AUSTRALIA CONSUMER DIVISION | AUSTRALIA BUSINESS DIVISION | NEW ZEALAND | ASIA |
|---|---|---|---|---|---|
| | | $m | $m | $m | $m |
| **2016** | | | | | |
| Discounted average term to settlement | **+10%** | **(21)** | **(11)** | **(1)** | **-** |
| | **-10%** | **21** | **11** | **1** | **-** |
| Inflation rate | **+1%** | **101** | **56** | **4** | **-** |
| | **-1%** | **(96)** | **(53)** | **(4)** | **-** |
| Discount rate | **+1%** | **(99)** | **(54)** | **(3)** | **-** |
| | **-1%** | **107** | **58** | **3** | **-** |
| Claims handling costs ratio | **+1%** | **56** | **42** | **6** | **2** |
| | **-1%** | **(56)** | **(42)** | **(6)** | **(2)** |
| 2015 | | | | | |
| Discounted average term to settlement | +10% | (38) | (75) | (1) | - |
| | -10% | 38 | 73 | 1 | - |
| Inflation rate | +1% | 125 | 152 | 6 | 1 |
| | -1% | (117) | (134) | (6) | (1) |
| Discount rate | +1% | (117) | (133) | (5) | - |
| | -1% | 127 | 153 | 5 | - |
| Claims handling costs ratio | +1% | 57 | 42 | 6 | 3 |
| | -1% | (57) | (42) | (6) | (3) |

## NOTE 2.3 INVESTMENTS

| | **2016** | 2015 |
|---|---|---|
| | **$m** | $m |
| **A. INVESTMENT INCOME** | | |
| Dividend revenue | **34** | 39 |
| Interest revenue | **448** | 517 |
| Trust revenue | **26** | 19 |
| Realised net gains and (losses) | **(74)** | 227 |
| Unrealised net gains and (losses) | **163** | 14 |
| Total investment income | **597** | 816 |
| **Represented by** | | |
| Investment income on assets backing insurance liabilities | **484** | 585 |
| Investment income on shareholders' funds | **113** | 231 |
| | **597** | 816 |
| **B. INVESTMENT COMPOSITION** | | |
| **I. Interest bearing investments** | | |
| Cash and short term money held in investment | **841** | 1,127 |
| Government and semi-government bonds | **1,671** | 2,915 |
| Corporate bonds and notes | **6,826** | 8,158 |
| Subordinated securities | **1,636** | 1,769 |
| Other | **160** | 156 |
| | **11,134** | 14,125 |
| **II. Equity investments (includes exposure to convertible securities)** | | |
| Listed | **1,045** | 656 |
| Unlisted | **446** | 486 |
| | **1,491** | 1,142 |
| **III. Other investments** | | |
| Other trusts | **291** | 268 |
| Foreign exchange risk derivatives | **30** | - |
| | **321** | 268 |
| Total investments | **12,946** | 15,535 |

**C. RECOGNITION AND MEASUREMENT**

Investment revenue is brought to account on an accruals basis. Revenue on investments in equity securities and property trusts is deemed to accrue on the date the dividends/distributions are declared, which for listed equity securities is deemed to be the ex-dividend date.

Investments comprise assets held to back insurance liabilities (policyholder funds that represent assets available for future settlement of outstanding claims) and assets that represent shareholders' funds. The investment funds themselves are predominantly generated from the collection of insurance premiums. The allocation of investments between policyholder funds and shareholders' funds is regularly monitored and the portfolio rebalanced accordingly. To determine the allocation, the Group's investment funds under management are compared to the technical provisions of the Group, which includes insurance liabilities. The policyholder funds are allocated to back the technical provisions, with the excess representing shareholders' funds.

All investments are designated at fair value through profit or loss. Investments are recorded and subsequently remeasured to fair value at each reporting date. Changes in the fair value are recognised as realised or unrealised investment gains or losses in profit or loss. The Group recognises transfers into and transfers out of fair value hierarchy levels (described below) as at the end of the reporting year. Purchases and sales of investments are recognised on a trade date basis, being the date on which a commitment is made to purchase or sell the asset. Transaction costs for purchases of investments are expensed as incurred. Investments are derecognised when the rights to receive future cash flows from the assets have expired, or have been transferred, and substantially all the risks and rewards of ownership have transferred.

The inputs used to determine the fair value for securities recognised under each level of the fair value hierarchy is set out below.

**I. Level 1 quoted prices**

The fair value is determined by reference to quoted prices (mid-market) in active markets for identical assets and liabilities. For IAG, this category includes government securities and listed equities.

**II. Level 2 other observable inputs**

The fair value is determined by reference to quoted prices in active markets for similar assets or liabilities or by reference to other significant inputs that are not quoted prices but are based on observable market data, for example interest rate yield curves observable at commonly quoted intervals. For IAG, this category primarily includes corporate and other fixed interest securities where the market is considered to be lacking sufficient depth to be considered active.

**III. Level 3 unobservable inputs**

The fair value is determined using valuation techniques in which a number of the significant inputs are not based on observable market data. Level 3 investments are primarily unlisted private equity funds where the fair value of investments is determined on the basis of published redemption values of those funds. This category also includes IAG's unlisted equity interest in Bohai Property Insurance Company Limited (Bohai). The fair value of Bohai is determined using a discounted cash flow model. The investment in Bohai was transferred into Level 3 category during the financial year with no valuation gain or loss recognised on reclassification.

The table below separates the total investment balance by hierarchy category:

| | LEVEL 1<br>$m | LEVEL 2<br>$m | LEVEL 3<br>$m | TOTAL<br>$m |
|---|---|---|---|---|
| **2016** | | | | |
| Interest bearing investments | **2,047** | **9,086** | **1** | **11,134** |
| Equity investments | **1,021** | **313** | **157** | **1,491** |
| Other investments | **14** | **306** | **1** | **321** |
| | **3,082** | **9,705** | **159** | **12,946** |
| 2015 | | | | |
| Interest bearing investments | 4,056 | 10,068 | 1 | 14,125 |
| Equity investments | 636 | 363 | 143 | 1,142 |
| Other investments | - | 268 | - | 268 |
| | 4,692 | 10,699 | 144 | 15,535 |

## NOTE 2.4 UNEARNED PREMIUM LIABILITY

| | 2016 $m | 2015 $m |
|---|---|---|
| **A. RECONCILIATION OF MOVEMENTS** | | |
| Unearned premium liability at the beginning of the financial year | **6,156** | 6,256 |
| Deferral of premiums written during the financial year | **5,866** | 5,935 |
| Earning of premiums written in previous financial years | **(5,910)** | (6,020) |
| Additions through business acquisition | **20** | 7 |
| Net foreign exchange movements | **88** | (22) |
| Unearned premium liability at the end of the financial year | **6,220** | 6,156 |

The carrying value of unearned premium liability includes $236 million (2015-$246 million) which is expected to be earned more than 12 months from reporting date.

**B. RECOGNITION AND MEASUREMENT**

Unearned premium is the portion of premium income that has yet to be recognised in the profit or loss (i.e. unexpired portion for risks underwritten) and is calculated based on the term of the risk and in accordance with the expected pattern of the incidence of risk underwritten, using an appropriate pro-rata method.

**C. ADEQUACY OF UNEARNED PREMIUM LIABILITY**

**I. Liability adequacy test (LAT)**

The LAT assesses the adequacy of the carrying amount of the net unearned premium liability to settle future claims. To determine if any deficiency exists, estimates of future claim costs (premium liabilities net of reinsurance) are compared to the unearned premium liability (net of reinsurance and related deferred acquisition costs). If the future claim costs exceed the net premium liabilities then a deficiency exists. Any deficiency is recognised immediately in profit or loss, with the corresponding impact on the balance sheet recognised first through the write down of deferred acquisition costs for the relevant portfolio of contracts and then through the establishment of a provision (unexpired risk liability).

The LAT is required to be conducted at the level of a portfolio of contracts that are subject to broadly similar risks and that are managed together as a single portfolio. The Group defines 'broadly similar risks' at a level where policies are affected by one or more common risk factors, including natural peril events, general weather conditions, economic conditions, inflationary movements, legal and regulatory changes as well as legislative reforms, reinsurance cost changes and variation in other input costs. The Group defines 'managed together' at a segment level as the respective Divisional CEOs collectively manage the entire portfolio within their control. The LAT is currently performed at the segment level for Australia (Australian Consumer Division and Australian Business Division) and New Zealand, and at a subsidiary level within Asia.

The LAT at reporting date resulted in a surplus for the Group (2015-surplus for the Group), with the table below providing details of the net premium liabilities (net of reinsurance and adjusted for appropriate risk margin) used in the LAT:

| | 2016 $m | 2015 $m |
|---|---|---|
| Net central estimate of present value of expected future cash flows from future claims | **3,564** | 3,481 |
| Risk margin of the present value of expected future cash flows | **82** | 81 |
| | **3,646** | 3,562 |
| Risk margin percentage | **2.3%** | 2.3% |
| Probability of adequacy | **60.0%** | 60.0% |

**II. Significant accounting estimates and judgements**

The LAT is conducted using the central estimate of the premium liabilities, applying a methodology consistent for reporting to APRA, which requires an estimation of the present value of future net cash flows (relating to future claims arising from the rights and obligations under current general insurance contracts) and adjusted for an appropriate risk margin for uncertainty in the central estimate for each portfolio of contracts. The test is based on prospective information and so is heavily dependent on assumptions and judgements.

The risk margin used in the LAT for individual portfolios is calculated by using a probability of adequacy (POA) methodology including diversification benefit, which is consistent with that used for the determination of the risk margin for the outstanding claims liability, based on assessments of the levels of risk in each portfolio. The 60% POA represented by the LAT differs from the 90% POA represented by the outstanding claims liability as the former is in effect an impairment test used only to test the sufficiency of net unearned premium liabilities, whereas the latter is a measurement accounting policy used in determining the carrying value of the outstanding claims liability. The process used to determine the risk margin, including the way in which diversification of risks has been allowed for, is explained in note 2.2 claims and reinsurance and other recoveries on outstanding claims.

## NOTE 2.5 DEFERRED INSURANCE EXPENSES

| | DEFERRED ACQUISITION COSTS[(a)] | | DEFERRED OUTWARDS REINSURANCE EXPENSE[(b)] | | TOTAL DEFERRED INSURANCE EXPENSES | |
|---|---|---|---|---|---|---|
| | **2016** | 2015 | **2016** | 2015 | **2016** | 2015 |
| | **$m** | $m | **$m** | $m | **$m** | $m |
| **A. RECONCILIATION OF MOVEMENTS** | | | | | | |
| At the beginning of the financial year | **1,015** | 1,028 | **1,823** | 706 | **2,838** | 1,734 |
| Costs deferred | **1,769** | 1,744 | **3,744** | 2,326 | **5,513** | 4,070 |
| Amortisation charged to profit | **(1,749)** | (1,750) | **(3,883)** | (1,196) | **(5,632)** | (2,946) |
| Addition through business acquisition | **-** | - | **-** | 3 | **-** | 3 |
| Net foreign exchange movements | **16** | (7) | **43** | (16) | **59** | (23) |
| Deferred costs at the end of the financial year | **1,051** | 1,015 | **1,727** | 1,823 | **2,778** | 2,838 |

(a) The carrying value of deferred acquisition costs includes $90 million (2015-$90 million) which is expected to be amortised more than 12 months from reporting date.

(b) The carrying value of deferred outwards reinsurance expense includes $28 million (2015-$20 million) which is expected to be amortised more than 12 months from reporting date.

### B. RECOGNITION AND MEASUREMENT

#### I. Acquisition costs

Acquisition costs are incurred in obtaining and recording general insurance contracts, which include advertising expenses, commission or brokerage paid to agents or brokers, premium collection costs, risk assessment costs and other administrative costs. These costs are initially capitalised and then expensed in line with the earning pattern of the related premium. Deferred acquisition costs at the reporting date represent the acquisition costs relating to unearned premium.

#### II. Outwards reinsurance expense

Premium ceded to reinsurers is recognised as an expense in accordance with the pattern of reinsurance service received. The outwards reinsurance premium relating to unearned premium is treated as a prepayment at the reporting date.

## NOTE 2.6 TRADE AND OTHER RECEIVABLES

| | **2016** | 2015 |
|---|---|---|
| | **$m** | $m |
| **A. COMPOSITION** | | |
| **I. Premium receivable** | | |
| Gross premium receivable | **3,370** | 3,290 |
| Provision for impairment | **(36)** | (39) |
| Net premium receivable | **3,334** | 3,251 |
| **II. Trade and other receivables[(a)]** | | |
| Reinsurance recoveries on paid claims | **658** | 300 |
| Loan to associates[(b)] | **99** | 102 |
| Investment related receivables | **98** | 96 |
| Trade and other debtors | **132** | 155 |
| Trade and other receivables | **987** | 653 |
| | **4,321** | 3,904 |

(a) Other than the loan to associates, receivables are non-interest bearing and are normally settled between 30 days and 12 months. The balance has not been discounted as the effect of the time value of money is not material. The net carrying amount of receivables is a reasonable approximation of the fair value of the assets due to the short term nature of the assets.

(b) This loan is denominated in Malaysian ringgit and has a fixed term of 15 years. A cumulative preference dividend of 1% is payable annually. The loan relates to the Group's increased investment in AmGeneral to acquire Kurnia during the financial year ended 30 June 2013.

### B. RECOGNITION AND MEASUREMENT

Trade and other receivables are stated at the amounts to be received in the future, inclusive of GST and less any impairment losses. The amounts are discounted where the effect of the time value of money is material. The recoverability of debts is assessed on an ongoing basis and provision for impairment is made based on objective evidence for individual receivables and having regard to past default experience. The impairment charge is recognised in profit or loss. Debts which are known to be uncollectible are written off.

## NOTE 2.7 TRADE AND OTHER PAYABLES

| | 2016 $m | 2015 $m |
|---|---|---|
| **A. COMPOSITION** | | |
| **I. Reinsurance premium payable[a]** | **848** | 1,440 |
| **II. Trade creditors[b]** | | |
| Commissions payable | **257** | 226 |
| Stamp duty payable | **116** | 120 |
| GST payable on premium receivable | **147** | 136 |
| Corporate treasury derivatives payable | **22** | - |
| Other[c] | **543** | 332 |
| | **1,085** | 814 |
| **III. Other payables[b]** | | |
| Other creditors and accruals | **371** | 453 |
| Investment creditors | **27** | 38 |
| Interest payable on interest bearing liabilities | **15** | 16 |
| | **2,346** | 2,761 |

(a) Under the agreement with National Indemnity Company (NICO), a Berkshire Hathaway (BH) Company, the Group has a right of offset, and settles on a net basis. This balance includes reinsurance premium payable to BH of $1,126 million (2015-$1,220 million), which has been offset with receivables due under the contract of $620 million (2015-$270 million). The relevant cash flows pertaining to the contract have been presented on a gross basis within the cash flow statement.

(b) Trade and other payables are unsecured, non interest bearing and are normally settled within 30 days to 12 months. Amounts have not been discounted because the effect of the time value of money is not material. The carrying amount of payables is a reasonable approximation of the fair value of the liabilities because of the short term nature of the liabilities.

(c) Other trade creditors includes $25 million (2015-$27 million) reinsurance collateral arrangements with various reinsurers to secure the Group reinsurance recoveries. The balance is anticipated to reduce through the settlement of amounts from reinsurers as they fall due. This payable is interest bearing.

### B. RECOGNITION AND MEASUREMENT

Trade and other payables are stated at the fair value of the consideration to be paid in the future for goods and services received, inclusive of GST. The amounts are discounted where the effect of the time value of money is material.

# 3. RISK

## SECTION INTRODUCTION

This section provides an overview of the Group's approach to risk and capital management.

The Group is exposed to multiple risks relating to the conduct of its general insurance business. IAG does not seek to avoid all risks, but to optimally manage and/or price them. Management of those risks is an integral part of delivering the strategy, decision making and IAG's long term sustainability. Risk management arrangements are designed to reflect the scope, scale and complexity of IAG's activities and where appropriate capital is held to support these activities.

IAG uses an enterprise wide approach to risk that includes five risk categories:

- Strategic
- Insurance
- Reinsurance
- Financial
- Operational

The risk categories, their definition and structured arrangements for their management are included in IAG's Risk Management Strategy (RMS). Risks rarely occur, or should be considered, in isolation. The interconnectivity of IAG's five risk categories and the key risks faced are understood and overseen. Key risks and their impact, likelihood, interconnectedness and velocity are considered in IAG's Enterprise Risk Profile (ERP).

## NOTE 3.1 RISK AND CAPITAL MANAGEMENT

### A. RISK MANAGEMENT OVERVIEW

The IAG Board has responsibility for setting risk strategy. The IAG Risk Committee (RC) assists the Board in fulfilling its risk management responsibilities, oversight of risk management, development of IAG's risk management framework (RMF) and policies and provides advice to the IAG Executives and Board. The RC monitors the effectiveness of the Risk Management function. The Group Chief Risk Officer (CRO) oversees risk management across the Group and is supported by a risk function. IAG's CRO and the Risk function provides regular reports to the RC on the operation of IAG's RMF, the status of key risks, risk and compliance incidents and risk framework changes.

IAG's RMF is in place to assist the Board and senior executive management in managing risk. The RMF is the totality of systems, structures, policies and processes within the Group that identify, assess, treat, monitor, report and/or communicate all internal and external sources of risk that could have a material impact on the Group's operations. The RMF supports management by:

- ensuring clear roles and responsibilities for the management of risk;
- standardising risk management language, definitions and processes so risks can be accurately benchmarked and compared;
- establishing common reporting standards, tools and risk management information; and
- defining input for risk management reports as well as the ERP.

IAG's written RMS describes the group-wide RMF and how it is implemented, including risk appetite (i.e. the levels, boundaries and nature of risk the organisation is willing to accept), the risk categories used, the major risk management processes, and roles and responsibilities for managing risk. The RMS is a Board-approved policy which brings together consistent strategies and sets the minimum acceptable standards for managing the full spectrum of risks associated with pursuing corporate objectives and fulfilling IAG's purpose. IAG uses Group policies and other supporting documents to help ensure the risk management requirements are clear across the Group, and provide context to implement risk management principles described in the RMS. The RMS must be adhered to along with the legal, regulatory and prudential requirements in all countries in which the organisation has operations.

Other key documents within the Group's RMF include:

- Reinsurance Management Strategy (REMS), which describes the systems, processes, procedures, controls and assurance to ensure IAG's reinsurance arrangements are prudently managed;
- Group Risk Appetite Statement (RAS), which articulates the levels, boundaries and nature of risk the Board is willing to accept in pursuit of IAG's strategic objectives; and
- Internal Capital Adequacy Assessment Process (ICAAP) and the ICAAP Summary Statement, which summarises the Group's risk assessment processes for capital management and describes the strategy for maintaining adequate capital over time.

The definitions of the risk categories and mitigation strategies are set out in the subsequent sections.

Risk culture and behaviours are the foundation for appropriate risk management and business sustainability. Conducting businesses in a manner aligned with IAG's Purpose is a core goal. Conduct related matters and risks are managed via IAG's enterprise approach to risk within established practices.

## B. STRATEGIC RISK

Strategic risk is defined as the risk of not achieving corporate or strategic goals due to:

- poor business decisions regarding future business plans and strategies, and/or
- lack of responsiveness to changes in the business environment.

Strategic risk is managed by the IAG Group Leadership Team with Board oversight. Key elements in the management of strategy and strategic risk include a rigorous strategic planning program and associated oversight arrangements, with progress against strategic priorities regularly considered. IAG implements active portfolio management of its insurance operations. This involves robust and regular review of the portfolios that leads to informed decisions on the allocation of assets (scarce resources) in the most efficient and value-accretive way in order to achieve the Group's strategic objectives. Consideration of both current and future value is critical in the process. Portfolio management can involve the acquisition or divestment of other entities, for which IAG has implemented a Merger & Acquisitions Framework to help ensure the associated risks are appropriately managed.

## C. INSURANCE RISK

Insurance risk is defined as the risk that the Group is exposed to financial loss as a result of:

- inadequate or inappropriate underwriting;
- inadequate or inappropriate product design and pricing;
- inadequate or inappropriate reserving including unforseen, unknown or unintended liabilities that may eventuate;
- inadequate or inappropriate claims management; and
- insurance concentration risk (e.g. by locality, segment, or distribution channel).

A fundamental part of the Group's overall risk management approach is the effective governance and management of the risks that affect the amount, timing and certainty of cash flows arising from insurance contracts. The level of insurance risk accepted by IAG is formally documented in its Insurance Business Licences, which each operating division is issued. The Insurance Business Licence is prepared by the Group Chief Underwriting Officer in consultation with the customer facing divisions and is approved by the Group CEO. The Insurance Business Licences are reviewed annually or more frequently if required. In addition to Insurance Business Licences, insurance risk is also managed through the implementation of the Insurance Risk Framework and the Insurance Risk Principles.

### I. Acceptance and pricing of risk

IAG adopts a disciplined approach to the underwriting of risks, rather than a premium volume or market share oriented approach. IAG believes this approach provides the greatest long term likelihood of being able to meet the objectives of all stakeholders, including policyholders, lenders, regulators and shareholders. IAG's significant underwriting and pricing expertise, coupled with data and analytics capability, allow the Group to effectively underwrite policies to the desired level of risk.

The underwriting by IAG of large numbers of less than fully correlated individual risks, predominantly short tail business, across a range of classes of insurance businesses in different regions reduces the variability in overall claims experience over time. A risk still remains that the actual amount of claims paid is different to the amount estimated at the time an insurance product was designed and priced. IAG's effective claims management and provisioning, reinsurance and capital management further mitigate the impact of this risk to the Group.

Business divisions underwrite to set criteria as contained in the Insurance Business Licence. Maximum limits are set for the acceptance of risk both on an individual insurance contract basis and for classes of business and specific risk groupings. Management information systems are maintained to provide up to date, reliable data on the risks to which the business is exposed at any point in time. Statistical models that combine historical and projected data (pricing, claims and market conditions) are used to calculate premiums and monitor claims patterns for each class of business.

### II. Claims management and provisioning

Once an incident has occurred, initial claim estimates are managed by claims officers with the requisite degree of experience and competence with the assistance, where appropriate, of a loss adjustor or other party with specialist knowledge of specific incidents. These case estimates are used to form part of the basis of the claims provisions. It is the Group's intention to respond to and settle all genuine claims quickly whenever possible and to pay claims fairly, based on policyholders' full entitlements. Efforts are made, including plain language policy terms, to ensure there is no misalignment between policyholders' perceived benefits when a policy is initially sold and their actual entitlement when a claim is made.

Claims provisions are established using actuarial valuation models, including a risk margin to cover inherent uncertainty in the ultimate cost of the claims, to ensure adequate capital is allocated to settle the claims that have occurred. Refer to note 2.2 claims and reinsurance and other recoveries on outstanding claims for further details.

### III. Concentrations of insurance risk

Each year the Group sets its tolerance for concentration risk by the use of various models to estimate the Group's maximum exposure to potential natural disasters and other catastrophes. The Group mitigates its exposure to concentrations of insurance risk by holding a portfolio diversified into many classes of business across different regions and by the utilisation of reinsurance, taking into account the cost of reinsurance and capital efficiency. The reinsurance cover limits the Group's financial exposure to a single event with a given probability, and also protects capital. The catastrophe reinsurance cover purchased affects the Insurance Concentration Risk Charge (ICRC) in the Australian Prudential Regulatory Authority (APRA) capital calculation.

Concentration risk is particularly relevant in the case of catastrophes, usually natural disasters including earthquakes, bushfires, hailstorms, tropical storms and high winds, which generally result in a concentration of affected policyholders being impacted by the same event. This aggregation of losses constitutes the largest individual potential financial loss to the Group. The Group is also exposed to certain large man-made catastrophic events such as industrial accidents and building fires. Catastrophe losses are an inherent risk of the general insurance industry that contributes to potentially material year-to-year fluctuations in the results of operations and financial position. The nature and level of catastrophes in any period cannot be predicted accurately but can be estimated through the utilisation of predictive models. The Group actively monitors and limits the aggregate exposure to catastrophe losses in regions that are subject to high levels of natural perils. Specific processes for monitoring identified key concentrations are set out below:

| RISK | SOURCE OF CONCENTRATION | RISK MANAGEMENT MEASURES |
|---|---|---|
| An accumulation of risks arising from a natural peril/catastrophe | Insured property concentrations | Accumulation risk modelling and reinsurance protection |
| A large property loss | Fire or accident affecting one building or a group of adjacent buildings | Maximum acceptance limits, property risk grading and reinsurance protection |
| Multiple liability retentions being involved in the same event | Response by a multitude of policies to the one event | Purchase of reinsurance clash protection |

The tables below provide an analysis of gross written premium by both region and product, which demonstrates the diversity of the Group's operations and its relatively limited exposure to additional risks associated with long tail classes of business (where there is increased uncertainty of the ultimate cost of claims due to the additional period of time to settlement):

| | **2016** | 2015 |
|---|---|---|
| | **%** | % |
| a. REGION | | |
| Australia | **77** | 77 |
| New Zealand | **19** | 20 |
| Asia | **4** | 3 |
| | **100** | 100 |
| b. PRODUCT | | |
| Motor | **32** | 30 |
| Home | **27** | 26 |
| Short tail commercial | **22** | 24 |
| CTP (motor liability) | **8** | 8 |
| Liability | **5** | 6 |
| Other short tail | **3** | 3 |
| Workers' compensation | **3** | 3 |
| | **100** | 100 |

### D. REINSURANCE RISK

Reinsurance risk is defined as the risk of:

- insufficient or inappropriate reinsurance coverage;
- inadequate underwriting and/or pricing of reinsurance exposures retained by IAG's reinsurance captives;
- inadequate or inappropriate reinsurance recovery management;
- reinsurance arrangements not legally binding;
- reinsurance concentration risk; and
- credit counterparty concentration risk to reinsurers, which is covered under the credit risk section of financial risk.

IAG's reinsurance program is an important part of the Group's overall approach to risk and capital management. It is used to limit exposure to large single claims as well as an accumulation of claims that arise from the same or similar events in order to stabilise earnings and protect capital resources. IAG's REMS outlines the reinsurance principles, including the requirement that the Group's reinsurance retention for catastrophe must not exceed 4% of net earned premium.

The Group determines its reinsurance requirements on a modified whole of portfolio basis (where modified whole of portfolio is the sum of all correlated risk). The limits purchased reflect a 1-in-250 year return period, which is more conservative than APRA's 1-in-200 year return period requirement. Dynamic financial analysis modelling is used to determine the optimal level at which reinsurance should be purchased for capital efficiency, compared with the cost and benefits of covers available in the market.

To facilitate the reinsurance process, manage counterparty exposure and create economies of scale, the Group has established a captive reinsurance operation across Australia, Singapore and Labuan. The operation acts as the reinsurer for the Group by being the main buyer of the Group's outwards reinsurance program. While the majority of business ceded by the Consolidated entity's subsidiaries is reinsured with the Group's captive reinsurance operation, individual business units do purchase specific additional reinsurance protection outside the Group.

The use of reinsurance introduces credit and basis risk. The management of credit risk includes the monitoring of reinsurers' credit ratings and controlling total exposures to limit counterparty default risk. Refer to the financial risk section of this note for further details. IAG mitigates basis risk by adopting a sound underwriting approach to the Group's reinsurance program through the specialist captive reinsurance operation. The Group's catastrophe reinsurance program is primarily purchased on a broad indemnity basis. Retained exposures sit within the Board risk appetite and appropriate capital is maintained.

#### I. Current reinsurance program

The external reinsurance program consists of a combination of the following reinsurance arrangement:

- a 20% whole-of-account quota share;
- a Group catastrophe cover which is placed in line with the strategy of buying to the level of a 1:250 year event on a modified whole of portfolio basis. IAG's catastrophe reinsurance protection runs to a calendar year and operates on an excess of loss basis, with the Group retaining the first $250 million ($200 million post-quota share) of each loss. It covers all territories in which IAG operates. The limit of catastrophe cover purchased was $7.0 billion placed to 80%. Should a loss event occur that is greater than $7.0 billion, the Group could potentially incur a net loss greater than the retention. The Group holds capital to mitigate the impact of this possibility;
- an aggregate sideways cover which protects against a frequency of attritional event losses in Australia, New Zealand and Asia, and operates below the Group catastrophe cover;
- excess of loss reinsurances which provide 'per risk' protection for retained exposures of the commercial property and engineering businesses in Australia, New Zealand, Thailand, Malaysia, Vietnam and Indonesia;
- excess of loss reinsurance for all casualty portfolios including CTP, public liability, workers' compensation and home owners warranty products;
- quota share protection for agency distributed financial lines products including Surety and Trade credit;
- quota share protection for Cyber;
- excess of loss reinsurance for all marine portfolios;
- excess of loss reinsurance cover for retained natural peril losses;
- Adverse Development Cover (ADC) and quota share protection on the CTP portfolio;
- ADC for the February 2011 Canterbury earthquake event; and
- a reinsurance arrangement in respect of IAG's asbestos exposure.

#### II. Changes during the year

In February 2016, IAG completed an innovative reinsurance transaction with BH that mitigates the Group's exposure to the Canterbury earthquakes and asbestos related liabilities. The transaction comprises:

- an ADC which provides NZ$600 million of protection above NZ$4.4 billion for the February 2011 Canterbury earthquake event; and
- a reinsurance arrangement in respect of IAG's asbestos exposure.

### E. FINANCIAL RISK

Financial risk is defined as the risk of:

- adverse movements in market prices (foreign exchange, equities, credit spreads, interest rates etc) or inappropriate concentration within the investments funds;
- a counterparty failing to meet its obligations (credit risk);
- inadequate liquidity; and
- inappropriate capital management.

Key aspects of the processes established by IAG to monitor and mitigate financial risks include:

- the Board Risk and Audit Committees with Non-Executive Directors as members;
- an Asset and Liability Committee (ALCo) comprising key Executives with relevant oversight responsibilities;
- value-at-risk analysis is performed, position limits are in place and monitored and monthly stress testing is undertaken to determine the impact of adverse market movements;
- maintenance of an approved Group Credit Risk Policy, Group Liquidity Policy, Group Foreign Exchange Policy and Group Investment Policy;
- active asset management, Board approved Strategic Asset Allocation and Investment Management Agreements;
- capital management activities, for further details refer to the capital management section (IV) of this note; and
- implementation of a Derivatives Risk Management Statement that considers the controls in the use of derivatives and sets out the permissible use of derivatives in relation to investment strategies. Derivatives are used solely to manage risk exposure.

### I. Market risk

#### a. FOREIGN EXCHANGE RISK

The Consolidated entity operates internationally and so is exposed to foreign exchange risk from various activities conducted in the normal course of business. Foreign exchange exposure is managed by IAG Asset Management and the Group Treasury function.

The key foreign exchange risk exposures and mitigation strategies are set out below:

| EXPOSURE | RISK MANAGEMENT MEASURES |
|---|---|
| Net investment in foreign operations - through the translation of the financial position (recognised directly in equity) and performance (recognised in profit or loss) of foreign operations that have a functional currency other than the Australian dollar. | Designated hedging instruments - forward foreign exchange contracts (derivatives). |
| Translation of interest bearing liabilities denominated in foreign currency. | Some designated as hedging instruments where the currency matches the functional currency of investments in foreign operations. |
| Translation of insurance liabilities denominated in currencies other than the Australian dollar (directly recognised in profit or loss). | Assets backing technical reserves are held in the same currency as the related insurance liabilities, mitigating any net foreign exchange exposure. |
| Translation of investments denominated in currencies other than Australian dollars. | Designated hedging instruments – forward foreign exchange contracts (derivatives). |

The table below provides information regarding the impact on the measurement of net investments in foreign operations held at reporting date of an instantaneous 10% depreciation of the Australian dollar compared with selected currencies on equity, net of related derivatives. An appreciation of the Australian dollar would broadly have the opposite impact.

| IMPACT OF 10% DEPRECIATION OF AUSTRALIAN DOLLAR | **2016** | 2015 |
|---|---|---|
| | **$m** | $m |
| | **Impact directly to equity** | Impact directly to equity |
| Net investments in foreign operations and related hedge arrangements | | |
| New Zealand dollar | **65** | 87 |
| Malaysian ringgit | **15** | 15 |
| Other currencies where considered significant | **14** | 15 |
| | **94** | 117 |

The sensitivity analysis demonstrates the effect of a change in one key assumption while other assumptions remain unchanged (isolated exchange rate movements).

#### b. PRICE RISK

The Group has exposure to equity price risk through its investments in equities (both directly and through certain trusts) and the use of equity related derivative contracts. The impact on the measurement of the investments held at reporting date of a change in equity values by +10% or -10% on profit before tax, net of related derivatives, is shown in the table below:

| IMPACT OF CHANGE IN EQUITY VALUE | | **2016** | 2015 |
|---|---|---|---|
| | | **$m** | $m |
| | | **Impact to profit** | Impact to profit |
| Investments – equity and trust securities and related equity derivatives | +10% | **115** | 115 |
| | -10% | **(115)** | (115) |

c. INTEREST RATE RISK

Fixed interest rate assets and liabilities are exposed to changes in market value derived from mark-to-market revaluations. Financial assets and liabilities with floating interest rates create cash flow variability.

The Group's interest rate risk arises primarily from fluctuations in the valuation of investments in fixed interest bearing securities recognised at fair value and from the underwriting of general insurance contracts, which creates exposure to the risk that interest rate movements materially impact the fair value of the insurance liabilities (the insurance liabilities are discounted with reference to the government yields). Movements in interest rates should have minimal impact on the insurance profit or loss due to the Group's policy of investing in assets backing insurance liabilities principally in fixed interest securities that are closely matched to the duration of the insurance liabilities (period to settlement). Therefore, movements in the fair value measurement of the assets broadly offset the impact of movements in the insurance liabilities from changes in interest rates.

The impact on the measurement of investments in fixed interest bearing securities held at reporting date of a change in interest rates by +1% or -1% on profit before tax, net of related derivatives, is shown in the following table. The sensitivity analysis provided demonstrates the effect of a change in interest rates only, whilst other assumptions remain unchanged.

| IMPACT OF CHANGE IN FIXED INTEREST BEARING SECURITIES VALUE | | **2016** | 2015 |
|---|---|---|---|
| | | **$m** | $m |
| | | **Impact to profit** | Impact to profit |
| Investments - interest bearing securities and related interest rate derivatives | +1% | **(228)** | (366) |
| | -1% | **245** | 389 |

Refer to note 2.2 claims and reinsurance and other recoveries on outstanding claims for details of the impact on the net outstanding claims liabilities before income tax to changes in key actuarial assumptions, including movements in discount rates.

**II. Credit risk**

Concentrations of credit risk exist where a number of counterparties have similar economic characteristics. The Group's credit risk arises predominantly from investment activities, reinsurance activities, premium debtors and dealings with other intermediaries. The Group maintains a credit risk appetite, which is approved by the Board, and a Group Credit Risk Policy that is consistent with the Board's risk appetite. The policy outlines the framework and procedures in place to ensure an adequate and appropriate level of monitoring and management of credit quality throughout the Group with the Group Treasury function responsible for implementation. Any new or amended credit risk exposures must be approved in accordance with the Group’s approval authority framework. The Group maintains sufficiently diverse credit exposures to avoid a concentration charge added to the regulatory capital requirement.

The maximum exposure to credit risk loss as at reporting date is the carrying amount of the assets/receivables on the balance sheet as they are measured at fair value.

a. INVESTMENTS

The Group is exposed to credit risk from investments in third parties, for example debt or similar securities issued by those companies. At the reporting date, there are material concentrations of credit risk to the banking sector, in particular the four major Australian banks. The credit risk relating to investments is regularly monitored and assessed, with maximum exposures limited by credit rating, counterparty, industry and geography. The assets backing insurance liabilities consist of high credit quality investments, including government securities and other investment grade securities, which reduce the risk of default.

The following table provides information regarding the credit risk relating to the interest bearing investments based on Standard & Poor’s counterparty credit ratings, which demonstrates the strong credit quality of the Group's investment book:

| CREDIT RATING OF INTEREST BEARING INVESTMENTS | **2016** | 2015 |
|---|---|---|
| | **$m** | $m |
| AAA | **4,747** | 5,821 |
| AA | **3,820** | 5,602 |
| A | **972** | 1,274 |
| BBB and below | **1,595** | 1,428 |
| | **11,134** | 14,125 |

### b. REINSURANCE RECOVERIES ON PAID CLAIMS

Reinsurance arrangements mitigate insurance risk but expose the Group to credit risk. Reinsurance is placed with companies (reinsurers) based on an evaluation of their financial strength, terms of coverage and price. At the reporting date, there are material concentrations of credit risk in relation to reinsurance recoverables, in particular to large global reinsurers. The Group has clearly defined policies for the approval and management of credit risk in relation to reinsurers. The Consolidated entity monitors the financial condition of its reinsurers on an ongoing basis and periodically reviews the reinsurers' ability to fulfil their obligations under respective existing and future reinsurance contracts. Some of the reinsurers are domiciled outside of the jurisdictions in which the Group operates and so there is the potential for additional risk such as country risk and transfer risk.

It is Group policy to only deal with reinsurers with credit ratings of at least Standard & Poor's BBB+ (or other rating agency equivalent) without collateralisation, other than a mandatory placement to meet local regulatory requirements. Where the credit rating of a reinsurer falls below the required quality during the period of risk a contractual right to replace the counterparty exists. Some of the reinsurance protection is purchased on a 'collateralised' basis, where reinsurers either deposit funds equivalent to their participation (trust or loss deposits) or provide other forms of collateral (letters of credit).

The following table provides the Group's exposure to reinsurance recoveries receivable on the outstanding claims balance, excluding other recoveries, by counterparty credit rating (Standard & Poor's) and the secured collateral:

| CREDIT RATING OF REINSURANCE RECOVERIES ON OUTSTANDING CLAIMS | **2016** | | 2015 | |
|---|---|---|---|---|
| | **$m** | **% of total** | $m | % of total |
| AAA | **-** | **-** | 1 | - |
| AA | **2,826** | **85** | 1,501 | 62 |
| A | **501** | **15** | 905 | 37 |
| BBB and below | **10** | **-** | 19 | 1 |
| Total | **3,337** | **100** | 2,426 | 100 |

Of these, approximately $1,127 million (2015-$720 million) is secured directly as follows, reducing the credit risk:

- deposits held in trust: $210 million (2015-$321 million);
- letters of credit: $907 million (2015-$388 million); and
- loss deposits: $10 million (2015-$11 million).

An ageing analysis for reinsurance recoveries on paid claims is provided below, which shows the largely current nature of the balance:

| | NOT OVERDUE | | OVERDUE | | TOTAL |
|---|---|---|---|---|---|
| | | <30 days | 30-120 days | >120 days | |
| | $m | $m | $m | $m | $m |
| **2016** | | | | | |
| Reinsurance recoveries on paid claims | **531** | **63** | **14** | **50** | **658** |
| 2015 | | | | | |
| Reinsurance recoveries on paid claims | 176 | 87 | 10 | 27 | 300 |

### c. PREMIUM RECEIVABLE

The majority of the premium receivable balance relates to policies which are paid on a monthly instalment basis. The late payment of amounts due under such arrangements allows for the cancellation of the related insurance contract eliminating both the credit risk and insurance risk for the unpaid amounts. Upon cancellation of a policy the outstanding premium receivable and revenue is reversed. The Group is exposed to the credit risk associated with brokers and other intermediaries when premium is collected via these intermediaries. The Group's exposure is regularly monitored by ALCo with reference to aggregated exposure, credit rating, internal credit limits and ageing of receivables by counterparty. Ageing analysis for premium receivable is provided below, with amounts aged according to their original due date, demonstrating the Group's limited exposure:

| | NOT OVERDUE | | OVERDUE | | TOTAL |
|---|---|---|---|---|---|
| | | <30 days | 30-120 days | >120 days | |
| | $m | $m | $m | $m | $m |
| **2016** | | | | | |
| Premium receivable | **2,745** | **272** | **317** | **36** | **3,370** |
| Provision for impairment | **(5)** | **(3)** | **(6)** | **(22)** | **(36)** |
| | **2,740** | **269** | **311** | **14** | **3,334** |
| 2015 | | | | | |
| Premium receivable | 2,773 | 233 | 244 | 40 | 3,290 |
| Provision for impairment | (5) | (3) | (6) | (25) | (39) |
| | 2,768 | 230 | 238 | 15 | 3,251 |

### III. Liquidity risk

The Group's liquidity position is derived from operating cash flows, access to liquidity through related bodies corporate and interest bearing liabilities (with some denominated in different currencies and with different maturities). The Group complies with its liquidity risk management practices, which include a Group policy, and has the framework and procedures in place to ensure an adequate and appropriate level of monitoring and management of liquidity. IAG also has an option to raise further share capital as part of the strategic relationship with Berkshire Hathaway Specialty Insurance Company, which provides IAG access to additional liquidity. See note 4.2 notes to the statement of changes in equity for further details.

#### a. OUTSTANDING CLAIMS LIABILITY AND INVESTMENTS

Underwriting insurance contracts expose the Group to liquidity risk through the obligation to make payment for claims of unknown amounts on unknown dates. The assets backing insurance liabilities can generally be readily sold or exchanged for cash to settle claims and are managed in accordance with the policy of broadly matching the overall maturity profile to the estimated pattern of claims payments.

A maturity analysis is provided below of the estimated net discounted outstanding claims liability (based on the remaining term to payment at the reporting date) and the investments that have a fixed term (provided by expected maturity). The timing of future claim payments is inherently uncertain. Actual maturities may differ from expected maturities because certain counterparties have the right to call or prepay certain obligations with or without penalties.

| MATURITY ANALYSIS | NET DISCOUNTED OUTSTANDING CLAIMS LIABILITY | | INVESTMENTS | |
|---|---|---|---|---|
| | **2016** | 2015 | **2016** | 2015 |
| | **$m** | $m | **$m** | $m |
| Floating interest rate (at call) | **-** | - | **723** | 1,002 |
| Within 1 year or less | **2,806** | 3,836 | **1,592** | 3,058 |
| Within 1 to 2 years | **1,510** | 1,549 | **2,109** | 1,192 |
| Within 2 to 5 years | **1,759** | 2,020 | **3,366** | 6,020 |
| Over 5 years | **977** | 1,569 | **3,344** | 2,853 |
| Total | **7,052** | 8,974 | **11,134** | 14,125 |

#### b. INTEREST BEARING LIABILITIES

The following table provides information about the residual maturity periods of the interest bearing liabilities of a capital nature based on the contractual maturity dates of cash flows:

| | CARRYING VALUE | MATURITY DATES OF CONTRACTUAL UNDISCOUNTED CASH FLOWS | | | | | |
|---|---|---|---|---|---|---|---|
| | | Within 1 year | 1 - 2 years | 2 - 5 years | Over 5 years | Perpetual | Total |
| | $m | $m | $m | $m | $m | $m | $m |
| **2016** | | | | | | | |
| Principal repayments[(a)] | **1,969** | **-** | **-** | **-** | **1,042** | **927** | **1,969** |
| Contractual interest payments[(a)] | | **93** | **89** | **230** | **-** | **-** | **412** |
| Total contractual undiscounted payments | | **93** | **89** | **230** | **1,042** | **927** | **2,381** |
| 2015 | | | | | | | |
| Principal repayments[(a)] | 1,768 | - | - | - | 841 | 927 | 1,768 |
| Contractual interest payments[(a)] | | 90 | 86 | 227 | - | - | 403 |
| Total contractual undiscounted payments | | 90 | 86 | 227 | 841 | 927 | 2,171 |

(a) All of the liabilities have call, reset or conversion dates which occur prior to any contractual maturity. Detailed descriptions of the instruments are provided in the note 4.1 interest bearing liabilities. The contractual interest payments are undiscounted and calculated based on underlying fixed interest rates or prevailing market floating rates as applicable at the reporting date. Interest payments have not been included beyond five years.

### IV. Capital management risk

The capital management strategy plays a central role in managing risk to create shareholder value whilst meeting the objective of maintaining an appropriate level of capital to protect policyholders' and lenders' interests, and meet regulatory requirements.

Under the APRA Prudential Standards, IAG is required to have a documented description of the capital management process (ICAAP) and to report annually on the operation of the ICAAP to the Board, together with a forward looking estimate of expected capital utilisation (as represented in the Group’s Capital Plan) and capital resilience (ICAAP Annual Report). Adequacy of the Group's capital position is judged relative to the Board's Capital RAS, with an internal capital model (ICM) used to assess the risks of breaching the minimum levels established in the Capital RAS. Scenario analysis and stress testing are important adjuncts to the ICM. The amount of capital required varies according to the business underwritten, extent of reinsurance and investment asset allocation.

The target level of capitalisation (risk appetite) for the Group is assessed by consideration of factors including:

- the probability of financial ruin over the next one to three years;
- the probability of falling below the APRA prescribed capital amount (PCA) over the next one to three years;
- other stakeholder perspectives on capitalisation, including rating agency capital models and associated ratings; and
- domestic and international levels of capitalisation.

a. REGULATORY CAPITAL

All insurers within the Group that carry on insurance business in Australia are registered with APRA and are subject to APRA's Prudential Standards. It is the Group's policy to ensure that each of the licensed insurers maintains an adequate capital position.

The Group's long term target capital ranges set out below remain unchanged:

- a total regulatory capital position equivalent to 1.4-1.6 times the PCA, compared to a regulatory requirement of 1.0 times; and
- Common Equity Tier 1 capital of 0.9-1.1 times the PCA, compared to a regulatory requirement of 0.6 times.

Internal policies are in place to ensure significant deviations from the benchmarks are considered by the Board as to how any shortfall should be made good, or any surplus utilised.

IAG uses the standardised framework detailed in the relevant prudential standards (APRA Level 2 Insurance Group requirements) to calculate regulatory capital.

| REGULATORY CAPITAL POSITION | **2016** | 2015 |
|---|---|---|
| | **$m** | $m |
| Common Equity Tier 1 capital (CET1 capital) | **2,838** | 3,212 |
| Additional Tier 1 capital | **707** | 762 |
| Total Tier 1 capital | **3,545** | 3,974 |
| Tier 2 capital | **1,074** | 811 |
| Total regulatory capital | **4,619** | 4,785 |
| Total PCA | **2,682** | 2,817 |
| PCA multiple | **1.72** | 1.70 |
| CET1 multiple | **1.06** | 1.14 |

At 30 June 2016, the Group's Insurance Concentration Risk Charge (ICRC) from a catastrophe event was $200 million (2015-$200 million).

Consideration is given to the operational capital needs of the business. Targeting a capital multiple above the minimum regulatory requirement aims to ensure ongoing strength and security of the Group, while suitably protecting policyholders and lenders.

The capital objectives are achieved through dynamic management of the balance sheet and capital mix, the use of a risk based capital adequacy framework that relies on explicit quantification of uncertainty or risk and the use of modelling techniques that provide the capacity to understand the risk/return trade-off as well as valuable inputs to the capital management process. The influences on capital, such as product mix, reinsurance program, catastrophe exposure, investment strategy, profit margins and capital structure, are all assessed through using dynamic financial analysis modelling.

An important influence on the Group's capital level is the payment of dividends. The Consolidated entity aims to maintain cash earnings payouts within a ratio range approved by the Board (refer to note 4.4 dividends).

b. CAPITAL COMPOSITION

The balance sheet capital mix at reporting date is shown in the table below:

| CAPITAL MIX | **Target** | **2016** | 2015 |
|---|---|---|---|
| | % | % | % |
| Ordinary equity less goodwill and intangible assets | **60-70** | **63.2** | 66.2 |
| Interest bearing liabilities - hybrid securities and debt | **30-40** | **36.8** | 33.8 |
| Total capitalisation | | **100** | 100 |

**F. OPERATIONAL RISK**

Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events.

When controls fail, an operational risk incident can cause injury, damage to reputation, have legal or regulatory implications or can lead to financial loss. The Group does not aim to eliminate all operational risks, but manages these by initiating an appropriate control framework and by monitoring and managing potential risks. The Board is responsible for oversight of the Operational Risk Framework and approval of the Operational Risk Management Policy, and any changes to it. The Board and Group Leadership Team believe an effective, documented and structured approach to operational risk is a key part of the broader RMF that is outlined in IAG's RMS.

IAG's Operational Risk Framework, inclusive of the Group Operational Risk Policy, operates within IAG's RMF. The Operational Risk Framework and supporting Operational Risk Policy and procedures aim to ensure that consistent governance mechanisms and practices are in place, and that activities undertaken which involve operational risk are continually assessed and managed with appropriate regard to the Group's RAS and the achievement of IAG's objectives. The Operational Risk Framework is supported by aligned frameworks, policies and procedures for key aspects of operational risk. For example, Compliance, Fraud and Business Continuity Frameworks and policies are in place as are various other operational risk policies. Compliance (including regulatory compliance) is a key aspect of operational risk. The Group's general insurance operations are subject to regulatory supervision in the jurisdictions in which they operate, with various regulatory frameworks continuing to evolve. The Group works closely with regulators and regularly monitors developments across its international operations to assess potential impacts on its ongoing ability to meet the various regulatory requirements.

Management and staff are responsible for identifying, assessing and managing operational risks in accordance with their roles and responsibilities. The Group's Internal Audit function also reviews the effectiveness of controls and processes surrounding operational risk.

# 4. CAPITAL STRUCTURE

## SECTION INTRODUCTION

This section provides disclosures on the capital structure of the Group, which demonstrates how IAG finances its overall operations and growth through the use of different sources of funds, including ordinary equity and debt and hybrid instruments. Reinsurance is also an increasingly important source of long-term capital for the Group - reinsurance specific disclosures are included in section 2 insurance disclosures.

The capital that IAG maintains provides financial security to its policyholders, whilst ensuring adherence to the capital adequacy requirements of industry regulators. The Group also seeks to maintain, and where possible enhance, the overall diversity and efficiency of its capital structure to support the delivery of targeted returns to shareholders. The Group measures its capital mix on a net tangible equity basis i.e. after deduction of goodwill and intangibles, giving it strong alignment with both regulatory and rating agency models. IAG's target is a capital mix of ordinary equity (net of goodwill and intangibles) at 60-70% and debt and hybrids at 30-40%.

## NOTE 4.1 INTEREST BEARING LIABILITIES

| | | **2016** | | 2015 | |
|---|---|---|---|---|---|
| | Section | **CARRYING VALUE $m** | **FAIR VALUE $m** | CARRYING VALUE $m | FAIR VALUE $m |
| **A. COMPOSITION** | | | | | |
| **I. Capital nature[(a)]** | | | | | |
| a. TIER 1 REGULATORY CAPITAL[(b)] | | | | | |
| Convertible preference shares | B. I | **377** | **383** | 377 | 383 |
| Reset exchangeable securities | B. II | **550** | **550** | 550 | 567 |
| b. TIER 2 REGULATORY CAPITAL | | | | | |
| GBP subordinated term notes | B. III | **178** | **177** | 205 | 210 |
| NZD subordinated bonds | B. IV | **179** | **180** | 286 | 297 |
| AUD subordinated convertible term notes | B. V | **350** | **352** | 350 | 358 |
| NZD subordinated convertible term notes[(c)] | B. VI | **335** | **329** | - | - |
| **II. Operational nature** | | | | | |
| Other interest bearing liabilities | | **2** | **2** | 2 | 2 |
| Less: capitalised transaction costs | | **(9)** | | (8) | |
| | | **1,962** | | 1,762 | |

(a) Capital instruments above cannot be reconciled to the regulatory capital section of note 3.1 risk and capital management due to APRA transitional arrangements.

(b) Instruments issued prior to 1 January 2013 are eligible for inclusion in the relevant category of regulatory capital up to limits prescribed by APRA under transitional arrangements. Any capital that is ineligible to be included in Tier 1 capital as a consequence may be included in Tier 2 capital to the extent there is residual capacity within Tier 2 transitional limits.

(c) At the reporting date, the Company recognised accrued interest of $1 million (2015-nil) which is presented within trade and other payables.

### B. SIGNIFICANT TERMS AND CONDITIONS

**I. Convertible preference shares (CPS)**

- face value of $377 million and issued by the Company;
- non-cumulative floating rate distribution payable semi-annually, the payments are expected to be fully franked;
- distribution rate equals the sum of six month bank bill rate plus CPS margin of 4.00% per annum multiplied by (1–tax rate);
- payments of distributions can only be made subject to meeting certain conditions. If no distribution is made, no dividends can be paid and no returns of capital can be made on ordinary shares until the next CPS dividend payment date;
- the CPS are scheduled for conversion on 1 May 2019, provided the mandatory conversion conditions are satisfied;
- IAG may exchange or redeem CPS on an exchange date, or upon occurrence of certain events, subject to APRA approval. The first optional exchange date is 1 May 2017; and
- the CPS must be converted into ordinary shares upon request by APRA on occurrence of a non-viability trigger event.

**II. Reset exchangeable securities (RES)**

- face value of $550 million and were issued by IAG Finance (New Zealand) Limited, a wholly owned subsidiary of the Company;
- non-cumulative floating rate distribution payable quarterly and expected to be fully franked;
- distribution rate equals the sum of the three month bank bill rate plus RES margin of 4.00% per annum multiplied by (1-tax rate);
- payments of distributions can only be made subject to meeting certain conditions. If no distribution is made, no dividends can be paid and no returns of capital can be made on ordinary shares unless IAG takes certain actions; and
- the RES may be exchanged by IAG or the holder on a reset date, or upon certain events. The next reset date is 16 December 2019. On exchange, IAG may convert RES into IAG ordinary shares, arrange a third party to acquire RES for their face value or redeem RES for their face value (subject to APRA approval).

**III. GBP subordinated term notes**

- face value of £250 million (equivalent to $625 million at date of issue) and issued by the Company. A total of £150 million of the notes has since been bought back;
- fixed interest rate of 5.625% per annum payable annually; and
- the notes mature on 21 December 2026 (non-callable for the first 10 years). If the notes are not redeemed by 21 December 2016, all notes become floating rate notes with an interest rate of the three month GBP LIBOR plus 1.62%.

**IV. NZD subordinated bonds**

- face value of NZ$325 million (equivalent to $246 million at date of issue) and issued by the Company. A total of NZ$138 million of the notes has since been bought back;
- fixed interest rate of 7.5% per annum, payable quarterly;
- the bonds mature on 15 December 2036 with the issuer having the option to redeem at par from 15 December 2016 and at subsequent interest payment dates, subject to approval from APRA;
- if the bonds are not redeemed by 15 December 2016, the interest rate will equal the sum of the five year New Zealand swap rate on 15 December 2016 and each fifth anniversary thereafter plus a margin of 3.78% per annum; and
- the bonds may also be redeemed by the issuer upon certain events subject to APRA's approval.

**V. AUD subordinated convertible term notes**

- face value of $350 million and issued by Insurance Australia Limited (IAL), a wholly owned subsidiary of the Company;
- floating interest rate equal to the three month bank bill swap rate (BBSW) plus a margin of 2.80% per annum is payable quarterly;
- the notes mature on 19 March 2040 unless converted or redeemed earlier, subject to rights of conversion or redemption;
- IAL has an option to redeem the securities at face value between years five and six and for certain tax and regulatory events (in each case subject to APRA’s prior written approval);
- the securities are convertible into IAG ordinary shares at the option of holders on certain dates from year eight;
- if APRA determines IAG or IAL to be non-viable, the securities will convert into IAG ordinary shares or, if that is not possible, the securities will be written off; and
- the number of IAG ordinary shares received on conversion will be based on a volume-weighted average price (VWAP) over a certain period, less a discount of 1%. The number of IAG ordinary shares will be capped to a maximum number by reference to the VWAP at the issue date (50% of that VWAP for conversion at the holder’s option and 20% of that VWAP for conversion on non-viability).

**VI. NZD subordinated convertible term notes**

- face value of NZ$350 million (equivalent to $332 million at date of issue) and issued by the Company on 15 June 2016;
- all remain outstanding as at the reporting date;
- fixed interest rate of 5.15% per annum, payable quarterly;
- the notes mature on 15 June 2043 with the issuer having the option to redeem at par from (and including) 15 June 2022 and at each subsequent interest payment date to and including 15 June 2023, subject to approval from APRA;
- if the notes are not redeemed on 15 June 2022, the interest rate will become the applicable three month Bank Bill rate plus the margin of 2.60% per annum;
- the notes can be converted into a variable number of IAG ordinary shares (subject to a maximum of 113,979,109 shares) at the option of holders from (and including) 15 June 2025 and at each subsequent interest payment date and the maturity date of 15 June 2043; and
- the notes must be converted into a variable number of IAG ordinary shares (subject to a maximum of 284,947,773 shares) or written off if APRA determines the Company to be non-viable.

## C. RECOGNITION AND MEASUREMENT

The interest bearing liabilities are initially measured at fair value (net of transaction costs) and subsequently measured at amortised cost. Based on market conditions at any point in time, the carrying value of the liabilities may not be representative of the fair value of the liabilities. The fair value for all interest bearing liabilities is calculated using their quoted market price (fair value hierarchy level 1).

## NOTE 4.2 NOTES TO THE STATEMENT OF CHANGES IN EQUITY

| | **2016** | 2015 | **2016** | 2015 |
|---|---|---|---|---|
| | **Number of shares in millions** | Number of shares in millions | **$m** | $m |
| **A. SHARE CAPITAL** | | | | |
| Balance at the beginning of the financial year | **2,431** | 2,341 | **7,275** | 6,775 |
| Shares issued under institutional placement, net of transaction costs | **-** | 90 | **-** | 500 |
| Balance at the end of the financial year | **2,431** | 2,431 | **7,275** | 7,275 |

**B. STRATEGIC RELATIONSHIP WITH BH**

As part of the strategic relationship with BH, the Company and NICO entered into a subscription agreement dated 16 June 2015 (Subscription Agreement). The components of the Subscription Agreement may impact future ordinary share capital of the Company. The terms of the Subscription Agreement were released to the ASX on 16 June 2015 (attached to the Appendix 3B on that date).

**I. Put option**

IAG has an option to place up to a further 121,569,233 new shares at a maximum issue price of $6.50 per share to NICO within 24 months after the date of the Subscription Agreement. Under standstill terms of the Subscription Agreement, NICO can only increase its shareholding in IAG above 14.9% with majority Board agreement and receipt of requisite regulatory approvals.

**II. Anti-dilution right**

On entry by the Company and NICO into the Subscription Agreement, the Company granted NICO a right to maintain, by way of a right to participate in any issue of shares or to subscribe for shares, its percentage interest in the issued share capital of the Company (Anti-dilution Right) in respect of a diluting event which occurs or is announced after 16 June 2015.

**C. NATURE AND PURPOSE OF EQUITY**

**I. Ordinary shares**

All ordinary shares on issue are fully paid and have no par value. Ordinary shares entitle the holder to a vote at a general meeting of the Company and to participate in the dividends and the proceeds on winding up of the Company in proportion to the number of, and amounts paid on, the shares held.

Shares are classified as equity when there is no obligation to transfer cash or other assets to the holder. Transaction costs directly attributable to the issue of equity instruments are shown in equity as a deduction from the proceeds, net of tax.

**II. Treasury shares held in trust**

To satisfy obligations under the various share based remuneration plans, shares are generally bought on-market at or near grant date of the relevant arrangement and are managed using in-house trusts, one for Australia and one for New Zealand, which are controlled by the Consolidated entity. The shares are measured at cost and are presented as a deduction from equity. No gain or loss is recognised in profit or loss on the sale, cancellation or reissue of the shares. The shares are derecognised as treasury shares held in trust when the shares vest or are released to the participant. The total number of treasury shares acquired on-market during the financial year was fifty-four thousand (2015-6 million) at an average price per share of $5.50 (2015-$6.57).

**III. Foreign currency translation reserve**

The foreign currency translation reserve records the foreign currency differences arising from the translation of the financial position and performance of subsidiaries and investments in associates that have a functional currency other than Australian dollars.

**IV. Share based remuneration reserve**

The share based remuneration reserve is used to recognise the fair value of equity settled share based remuneration obligations issued to employees. The total amount expensed over the vesting period through the consolidated statement of comprehensive income is calculated by reference to the fair value of the rights at grant date. The fair value of the rights is calculated at the grant date using a Black-Scholes valuation model. The volatility assumption has been set considering the Company's historic share price. Some of the assumptions are based on historical data which is not necessarily indicative of future trends. Reasonable changes in these assumptions would not have a material impact on the amounts recognised in the financial statements.

The Company provides benefits to employees (including senior management and Executives) through share based incentives to create a link between shareholder value creation and rewarding employees, and assist with retention of key personnel. The senior management and Executive share plan arrangements consist of two separate arrangements working together. These two arrangements are the Deferred Award Rights Plan (DAR Plan) and Executive Performance Rights Plan (EPR Plan). The People and Remuneration Committee (PARC) approves the participation of each individual in the plans.

The obligations under share based payment arrangements are covered by the on-market purchase of IAG ordinary shares which are held in trust. The number of shares purchased to cover each allocation of rights is determined by the trustee based on independent actuarial advice.

## NOTE 4.3 EARNINGS PER SHARE

| | 2016 cents | 2015 cents |
|---|---|---|
| **A. REPORTING PERIOD VALUES** | | |
| Basic earnings per ordinary share[(a)] | **25.79** | 31.22 |
| Diluted earnings per ordinary share[(b)] | **25.34** | 30.45 |

(a) The basic earnings per ordinary share is determined by dividing the profit or loss attributable to shareholders of the Parent by the weighted average number of shares of the Parent on issue during the reporting year. The treasury shares held in trust are deducted, but earnings attributable to those shares are included.

(b) Diluted earnings per share is determined by dividing the profit or loss attributable to shareholders of the Parent, adjusted for the finance costs of dilutive convertible instruments, by the weighted average number of ordinary shares and dilutive potential ordinary shares, primarily as a result of debt instruments that possess a conversion feature.

| | 2016 $m | 2015 $m |
|---|---|---|
| **B. RECONCILIATION OF EARNINGS USED IN CALCULATING EARNINGS PER SHARE** | | |
| Profit/(loss) attributable to shareholders of the Parent which is used in calculating basic and diluted earnings per share | **625** | 728 |
| Finance costs of convertible securities, net of tax | **25** | 26 |
| Profit/(loss) attributable to shareholders of the Parent which is used in calculating diluted earnings per share | **650** | 754 |

| | 2016 Number of shares in millions | 2015 Number of shares in millions |
|---|---|---|
| **C. RECONCILIATION OF WEIGHTED AVERAGE NUMBER OF ORDINARY SHARES USED IN CALCULATING EARNINGS PER SHARE** | | |
| Weighted average number of ordinary shares on issue (adjusted for treasury shares held in trust) used in the calculation of basic earnings per share | **2,423** | 2,332 |
| **Weighted average number of dilutive potential ordinary shares relating to:** | | |
| Convertible securities | **134** | 131 |
| Unvested share based remuneration rights supported by treasury shares held in trust | **8** | 13 |
| | **2,565** | 2,476 |

## NOTE 4.4 DIVIDENDS

| | 2016 $m | 2015 $m |
|---|---|---|
| **A. ORDINARY SHARES** | | |
| 2016 special dividend (paid 30 March 2016): $0.10 (2015-nil) per ordinary share fully-franked at 30% | **243** | - |
| 2016 interim dividend (paid 30 March 2016): $0.13 (2015-$0.13) per ordinary share fully-franked at 30% | **316** | 304 |
| 2015 final dividend (paid 7 October 2015): $0.16 (2014-$0.26) per ordinary share fully-franked at 30% | **389** | 609 |
| | **948** | 913 |
| **B. DIVIDEND NOT RECOGNISED AT REPORTING DATE** | | |
| 2016 final dividend: $0.13 (2015: $0.16) per ordinary share fully-franked at 30% to be paid on 5 October 2016. | **316** | 389 |
| **C. DIVIDEND FRANKING AMOUNT** | | |
| Franking credits available for subsequent financial periods based on a tax rate of 30% | **212** | 374 |

The consolidated amounts above are calculated from the balance of the franking account as at the end of the reporting period, adjusted for franking credits that will arise from the settlement, after the end of the reporting date, of liabilities or receivables for income tax and dividends and the franking credits that will be utilised for dividends determined but not recognised at the reporting date.

The Company, after payment of the final dividend, has a franking balance of $111 million franking credits available for subsequent financial periods and is capable of fully franking a further $259 million of distributions.

### D. DIVIDEND REINVESTMENT

A Dividend Reinvestment Plan (DRP) operates which allows shareholders with ordinary shares to elect to receive their dividend entitlement in the form of IAG shares. The price of DRP shares is the volume weighted average share price, less a discount if determined by the Directors, calculated over the pricing period (which is at least five trading days) as determined by the Directors for each dividend payment date. A copy of the terms and conditions for the DRP is available at www.iag.com.au/shareholder-centre/dividends/reinvestment.

The DRP for the 2016 interim and special dividends paid on 30 March 2016 was settled with the on-market purchase of 17.4 million shares priced at $5.4894 per share (based on a daily volume weighted average price for 15 trading days from 3 March 2016 to 23 March 2016 inclusive, with no discount applied).

### E. RESTRICTIONS THAT MAY LIMIT THE PAYMENT OF DIVIDENDS

There are currently no restrictions on the payment of dividends by the Parent other than:

- the payment of dividends is subject to the provisions of the Corporations Act 2001 and IAG's constitution;
- the payment of dividends generally being limited to profits, subject to ongoing solvency obligations, and under the APRA Level 2 Insurance Group supervision requirements, IAG is required to obtain approval from APRA before payment of dividends on ordinary shares that exceed the Group's after tax earnings as defined by APRA; and
- no dividends can be paid and no returns of capital can be made on ordinary shares if distributions are not paid on the convertible preference shares or reset exchangeable securities, unless certain actions are taken by IAG. For further details refer to note 4.1 interest bearing liabilities.

### F. RECOGNITION AND MEASUREMENT

Provision for dividends is made in respect of ordinary shares where the dividends are declared on or before the reporting date, but have not yet been distributed at that date.

## NOTE 4.5 DERIVATIVES

### A. REPORTING DATE POSITIONS

| | **2016** | | | 2015 | | |
|---|---|---|---|---|---|---|
| | **Notional contract amount** | **Fair value asset** | **Fair value liability** | Notional contract amount | Fair value asset | Fair value liability |
| | **$m** | **$m** | **$m** | $m | $m | $m |
| **I. Net investment hedges (hedge accounting applied)** | | | | | | |
| Forward foreign exchange contracts | **1,627** | **7** | **(21)** | 1,643 | 97 | (4) |
| **II. Investment related derivatives (derivatives without hedge accounting applied)** | | | | | | |
| Bond futures | **1,920** | **-** | **-** | 4,548 | - | - |
| Share price index futures | **40** | **-** | **-** | 271 | - | - |
| Forward foreign exchange contracts | **1,624** | **30** | **(7)** | 711 | - | (10) |
| **III. Treasury related derivatives (derivatives without hedge accounting applied)** | | | | | | |
| Forward foreign exchange contracts | **1,851** | **20** | **(30)** | 1,356 | 11 | (101) |
| Interest rate swaps | **335** | **2** | **-** | 200 | - | - |

All derivatives contracts are expected to be settled within 12 months, except for interest rate swaps which mature in more than five years.

### B. RECOGNITION AND MEASUREMENT

Derivatives are initially recognised at trade date at fair value, which is determined by reference to current market quotes or generally accepted valuation principles. The investment related derivatives are presented together with the underlying investments or as payables when the fair value is negative. The treasury related derivatives are presented as receivables when the fair value is positive or as payables when the fair value is negative.

#### I. Hedge accounting

Hedge accounting may be applied to derivatives designated as hedging instruments provided certain criteria are met. To qualify for hedge accounting, at the inception of the hedge and throughout its life, each hedge must be expected to be highly effective. Actual effectiveness in the range of 80% to 125% must also be demonstrated on an ongoing basis. When it is determined that a derivative for which hedge accounting has been designated is not (or ceases to be) effective, hedge accounting is discontinued prospectively from the date of ineffectiveness. The hedging relationships have been effective throughout the current financial year, or since inception.

The foreign currency exposures arising on translation of net investments in foreign operations are hedged (net investment hedge) using forward exchange contracts and the designation of certain foreign currency borrowings as hedging instruments. The fair value is determined using observable inputs (level 2 in the fair value hierarchy).

Any gain or loss on the net investment hedges relating to the effective portion of the hedge is recognised in equity, while the gain or loss relating to the ineffective portion is immediately recognised in profit or loss. Gains and losses accumulated in the equity reserve are recognised in profit or loss upon the disposal of the foreign operation.

#### II. Derivatives without hedge accounting applied

For derivatives that do not qualify for hedge accounting, the changes in fair value are immediately recognised in profit or loss. Transaction costs for purchases of derivatives are expensed as incurred.

The fair value of the bond futures and share price index futures are measured using a quoted price in an active market (level 1 in the fair value hierarchy), whilst the fair value of the interest rate swaps and forward foreign exchange contracts are determined using observable inputs (level 2 in the fair value hierarchy).

# 5. OTHER BALANCE SHEET DISCLOSURES

**SECTION INTRODUCTION**

This section provides disclosures on other components of the Group's financial position, including:

- Goodwill and intangible assets - these balances primarily relate to the difference between the total consideration paid and the net tangible assets acquired in relation to past business acquisitions as well as internally developed capitalised software. These assets support the generation of future earnings and are subject to impairment testing. For example, an impairment will arise if future earnings can no longer support the carrying value of the assets in question.
- Income tax - the note summarises both the comprehensive income (profit or loss and other comprehensive income) and balance sheet items related to income tax. The profit or loss disclosure includes a reconciliation between the income tax expense reported and the proforma amount when applying the Australian company tax rate (30%). The balance sheet disclosure focuses on deferred tax balances, which arise due to timing differences between the accounting treatment of taxable income or expenses and the treatment adopted by the relevant tax authority. For example, the Group recognises a deferred tax asset in relation to the Earthquake losses incurred by its New Zealand operations since the 2011 financial year. This asset will unwind over time as the tax benefit recognised for accounting purposes is used to offset future taxable income.
- Provisions - this balance primarily includes employee related costs, for example an annual leave entitlement representing amounts owing to employees at the balance date based on past service.

## NOTE 5.1 GOODWILL AND INTANGIBLE ASSETS

| | Goodwill | Software development expenditure | Distribution channels | Customer relationships | Brands and other | Total |
|---|---|---|---|---|---|---|
| | $m | $m | $m | $m | $m | $m |
| **2016** | | | | | | |
| **A. COMPOSITION** | | | | | | |
| Cost | **2,953** | **776** | **158** | **169** | **125** | **4,181** |
| Accumulated amortisation and impairment | **-** | **(636)** | **(64)** | **(81)** | **(25)** | **(806)** |
| Net foreign exchange movements | **29** | **(8)** | **2** | **5** | **7** | **35** |
| Balance at the end of the financial year | **2,982** | **132** | **96** | **93** | **107** | **3,410** |
| **B. RECONCILIATION OF MOVEMENTS** | | | | | | |
| Balance at the beginning of the financial year | **2,890** | **343** | **114** | **114** | **100** | **3,561** |
| Additions acquired and developed | **44** | **62** | **11** | **2** | **7** | **126** |
| Disposal through sale of businesses | **(6)** | **-** | **(5)** | **(2)** | **-** | **(13)** |
| Amortisation | **-** | **(80)** | **(28)** | **(23)** | **(3)** | **(134)** |
| Accelerated amortisation and impairment | **-** | **(198)** | **-** | **-** | **-** | **(198)** |
| Net foreign exchange movements | **54** | **5** | **4** | **2** | **3** | **68** |
| Balance at the end of the financial year | **2,982** | **132** | **96** | **93** | **107** | **3,410** |
| 2015 | | | | | | |
| **C. COMPOSITION** | | | | | | |
| Cost | 2,915 | 714 | 152 | 169 | 118 | 4,068 |
| Accumulated amortisation and impairment | - | (358) | (36) | (58) | (22) | (474) |
| Net foreign exchange movements | (25) | (13) | (2) | 3 | 4 | (33) |
| Balance at the end of the financial year | 2,890 | 343 | 114 | 114 | 100 | 3,561 |
| **D. RECONCILIATION OF MOVEMENTS** | | | | | | |
| Balance at the beginning of the financial year | 2,899 | 288 | 155 | 144 | 113 | 3,599 |
| Additions acquired and developed | 17 | 118 | 2 | - | 10 | 147 |
| Disposal through sale of businesses | - | - | (10) | - | - | (10) |
| Amortisation | - | (59) | (31) | (28) | (21) | (139) |
| Net foreign exchange movements | (26) | (4) | (2) | (2) | (2) | (36) |
| Balance at the end of the financial year | 2,890 | 343 | 114 | 114 | 100 | 3,561 |

## E. IMPAIRMENT

During the current financial year, a review was undertaken of the Group's software platforms in the context of both the growing impact of digital disruption and IAG's overarching strategic priorities around simplification and scalability. As a result of this review, a reduction in the carrying value of capitalised software expenditure of $198 million (2015-nil) was recognised. The assets have a lower recoverable amount reflecting the rapid changes in technology and the reduced useful life of software development expenditure. Associated accelerated amortisation and impairment is recognised as a separate line item on the face of the statement of comprehensive income. A portion of the expense relates to accelerated amortisation following a change by the Group in the current year to increase the threshold for the capitalisation of software development costs to $10 million, reflecting the increasingly shorter useful life of smaller items of software. Going forward, increased costs related to software development will be recognised in the profit or loss, but offset by a lower amortisation charge.

An impairment charge is recognised in profit or loss when the carrying value of the asset, or Cash Generating Unit (CGU), exceeds the calculated recoverable amount. The impairment charge for goodwill cannot be subsequently reversed, whereas for identified intangibles the charge can be reversed where estimates used to determine the recoverable amount have changed. For assets with indefinite useful lives, which include goodwill, the recoverability of the carrying value of the assets is reviewed for impairment at each reporting date, or more frequently if events or changes in circumstances indicate that it might be impaired. The carrying amount of intangible assets with finite useful lives are reviewed at each reporting date by determining whether there is an indication that the carrying value may be impaired. If any such indication exists, the asset is tested for impairment.

### I. Impairment testing of goodwill

For the purpose of impairment testing goodwill is allocated to CGUs. The recoverable amount of goodwill is determined by value-in-use calculations, which estimate the present value of future cash flows by using a post tax discount rate that reflects current market assessment of the risks specific to the CGUs. The carrying value of identified intangible assets is deducted from the value generated from the cash flow projections to arrive at a recoverable value for goodwill which is then compared with the carrying value of goodwill. Where an impairment is determined, impairment losses relating to CGUs are allocated first to reduce goodwill and then to other CGU assets on a pro-rata basis.

Goodwill is allocated to the following CGUs:

| | **2016** | 2015 |
|---|---|---|
| | **$m** | $m |
| Consumer Division operations - Australia | **771** | 771 |
| Business Division operations - Australia | **1,496** | 1,452 |
| New Zealand operations | **658** | 611 |
| Asia operations | **57** | 56 |
| | **2,982** | 2,890 |

The following describes the key assumptions on which management based its cash flow projections to undertake the impairment testing:

- Cash flow forecasts are based on ten year valuation forecasts for growth and profitability. Twenty year periods are used only in emerging markets, to enable appropriate phasing to terminal values.
- Terminal value is calculated using a perpetuity growth formula based on the cash flow forecast for year five or ten, terminal growth rate in profit or premium and, where appropriate, terminal insurance margin. Terminal growth rates and insurance margins are based on past performance and management's expectations for future performance in each segment and country. The terminal growth rate assumptions used in the Group's impairment assessment for significant CGU's as at 30 June 2016 are: the Australian Consumer Division 4.5% (2015-4.5%), the Australian Business Division 4.3% (2015-4.5%) and New Zealand 3.5% (2015-3.5%).
- Discount rates reflect a beta and equity risk premium appropriate to the Group, with risk adjustments for individual segments and countries where applicable. The post-tax discount rates used for significant CGU's as at 30 June 2016 are: the Australian Consumer Division 9.7% (2015-10.2%), the Australian Business Division 9.7% (2015-10.2%) and New Zealand 10.3% (2015-10.8%).

### II. Impairment testing of identified intangible assets

Where the recoverable amount is determined by a value-in-use calculation, it involves the use of accounting estimates and assumptions to determine the projected net cash flows, which are discounted using an appropriate discount rate to reflect current market assessment of the risk associated with the assets or CGU. A description of the nature of significant intangible assets is provided below.

- The value of distribution channels is derived from future revenue expected to be generated as a result of the existing relationships with the broker networks.
- Customer relationships represent the present value of future profits expected to arise from existing customer relationships (developed prior to acquisition of the business). The assumptions for the useful life and customer attrition rates are determined based on historical information.
- Brands represents the revenue generating value of the acquired brand and is determined using the relief from royalty method.
- An impairment charge for capitalised software is incurred if there is evidence of obsolescence or significant changes impacting the manner in which an asset is used or expected to be used or evidence indicating the economic performance of the asset is not as intended by management.

**F. RECOGNITION AND MEASUREMENT**

All of the goodwill and intangible assets, other than components of capitalised software development expenditure (internally generated), have been acquired.
Intangible assets are initially recorded at cost at the date of acquisition, being the fair value of the consideration. Internally generated intangible assets comprise all directly attributable costs necessary to create, produce and prepare the asset to be capable of operating in the manner intended by management. Goodwill is generated as a result of business acquisition and is initially measured as the excess of the purchase consideration over the fair value of the net identifiable assets and liabilities acquired. At the date of disposal of a business, attributed goodwill is used to calculate the gain or loss on disposal.

Intangible assets with an indefinite useful life, including goodwill and certain brands, are not subject to amortisation but to impairment testing. Intangible assets with finite useful lives are amortised on a straight line basis over the period in which the related economic benefits are expected to be realised. Amortisation rates and residual values are reviewed annually and any changes are accounted for prospectively. Amortisation is recognised within fee based, corporate and other expenses in the consolidated statement of comprehensive income, whilst the amortisation of capitalised software is recognised within the insurance profit. The useful lives for each category of intangible assets are as follows:

- capitalised software: up to 3 years;
- distribution channels: 5 to 10 years;
- customer relationships: 5 to 10 years; and
- brands and other: up to 20 years.

## NOTE 5.2 INCOME TAX

| | 2016 $m | 2015 $m |
|---|---|---|
| **A. INCOME TAX EXPENSE** | | |
| Current tax | **291** | 332 |
| Deferred tax | **-** | (240) |
| (Over)/under provided in prior year | **(73)** | 27 |
| Income tax expense/(credit) | **218** | 119 |
| **Deferred income tax expense/(credit) included in income tax comprises** | | |
| (Increase)/decrease in deferred tax assets | **4** | (191) |
| Increase/(decrease) in deferred tax liabilities | **(4)** | (49) |
| | **-** | (240) |
| **B. RECONCILIATION OF PRIMA FACIE TAX TO INCOME TAX EXPENSE** | | |
| Profit for the year before income tax | **920** | 949 |
| Income tax calculated at 30% (2015-30%) | **276** | 285 |
| **Amounts which are not deductible/(taxable) in calculating taxable income** | | |
| Difference in tax rate | **19** | (205) |
| Rebateable dividends | **(8)** | (9) |
| Interest on convertible preference shares | **5** | 5 |
| Other | **(1)** | 16 |
| Income tax expense/(credit) applicable to current year | **291** | 92 |
| Adjustment relating to prior year | **(73)** | 27 |
| Income tax (credit)/expense attributable to profit/(loss) for the year after impact of tax consolidation | **218** | 119 |
| **C. DEFERRED TAX ASSETS** | | |
| **I. Composition** | | |
| a. AMOUNTS RECOGNISED IN PROFIT | | |
| Property and equipment | **119** | 75 |
| Employee benefits | **83** | 91 |
| Insurance provisions | **118** | 122 |
| Investments | **47** | 30 |
| Provisions | **17** | 11 |
| Tax losses | **447** | 444 |
| Other | **7** | - |
| | **838** | 773 |
| b. AMOUNTS RECOGNISED DIRECTLY IN OTHER COMPREHENSIVE INCOME | | |
| Defined benefit superannuation plans | **23** | 9 |
| | **861** | 782 |
| c. AMOUNTS SET-OFF AGAINST DEFERRED TAX LIABILITIES | **(258)** | (283) |
| | **603** | 499 |

| | 2016 $m | 2015 $m |
|---|---|---|
| **II. Reconciliation of movements** | | |
| Balance at the beginning of the financial year | **782** | 652 |
| Credited/(charged) to profit or loss | **(4)** | 191 |
| Credited/(charged) to equity | **14** | (13) |
| Adjustments relating to prior year | **35** | (23) |
| Foreign exchange differences | **34** | (25) |
| Balance at the end of the financial year prior to set-off | **861** | 782 |

**III. Tax losses**

The Consolidated entity has an unrecognised deferred tax asset of nil (2015-$11 million) in relation to discontinued operation tax losses.

| | 2016 $m | 2015 $m |
|---|---|---|
| **D. DEFERRED TAX LIABILITIES** | | |
| **I. Composition** | | |
| a. AMOUNTS RECOGNISED IN PROFIT | | |
| Investments | **90** | 35 |
| Intangible assets | **34** | 56 |
| Other | **129** | 165 |
| | **253** | 256 |
| b. AMOUNTS RECOGNISED DIRECTLY IN OTHER COMPREHENSIVE INCOME | | |
| Hedges | **5** | 27 |
| | **258** | 283 |
| c. AMOUNTS SET-OFF AGAINST DEFERRED TAX ASSETS | **(258)** | (283) |
| | **-** | - |
| **II. Reconciliation of movements** | | |
| Balance at the beginning of the financial year | **283** | 328 |
| Charged/(credited) to profit or loss | **(4)** | (49) |
| Charged/(credited) to equity | **(22)** | 15 |
| Acquisitions of subsidiaries | **1** | - |
| Adjustments relating to prior year | **-** | (12) |
| Foreign exchange differences | **-** | 1 |
| Balance at the end of the financial year prior to set-off | **258** | 283 |

## E. RECOGNITION AND MEASUREMENT

**I. Income tax**

Income tax expense for a reporting year comprises current and deferred tax. Income tax is recognised in profit or loss, except to the extent that it relates to items recognised directly in either equity or other comprehensive income.

**II. Current tax**

Current tax assets and liabilities are the expected tax recoverable or payable on the taxable income for the year, using tax rates for each jurisdiction, and any adjustment to tax payable in respect of previous financial periods. These include any rates or laws enacted or substantially enacted at the balance sheet date.

**III. Deferred tax**

Deferred tax liabilities are recognised for all taxable temporary differences between the carrying amount and tax bases. Deferred tax assets (deductible temporary differences, carried forward unused tax assets and unused tax losses) are recognised to the extent it is probable that future taxable profit will be available to utilise them before the unused tax losses or credits expire. In making this assessment, IAG considers historical trends of profit generation.

The following demonstrates other circumstances when no deferred tax asset or liability is recognised:

- 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;
- temporary differences between the carrying amount and tax bases of investments in subsidiaries where it is probable that the differences will not reverse in the foreseeable future; and
- temporary differences relating to the initial recognition of goodwill.

**IV. Tax consolidation**

IAG and its Australian resident wholly owned subsidiaries adopted the tax consolidation legislation with effect from 1 July 2002 and are therefore taxed as a single entity from that date. IAG is the head entity within the tax-consolidated group.

## NOTE 5.3 PROVISIONS

| | 2016 $m | 2015 $m |
|---|---|---|
| **A. EMPLOYEE BENEFITS** | | |
| **I. Expense recognised in the consolidated statement of comprehensive income** | | |
| Defined contribution superannuation plans | **122** | 116 |
| Defined benefit superannuation plans | **8** | 10 |
| Share based remuneration | **29** | 28 |
| Salaries and other employee benefits expense | **1,530** | 1,605 |
| | **1,689** | 1,759 |
| **II. Provision recognised on the consolidated balance sheet** | | |
| Annual leave | **97** | 101 |
| Long service leave | **90** | 90 |
| Cash based incentive arrangements | **88** | 110 |
| Defined benefit superannuation plans | **61** | 16 |
| Other employee benefits | **8** | 7 |
| | **344** | 324 |

The employee benefits provision includes $122 million (2015-$79 million) which is expected to be settled after more than 12 months from reporting date.

| | 2016 $m | 2015 $m |
|---|---|---|
| **B. RESTRUCTURING PROVISION** | | |
| Balance at the beginning of the financial year | **59** | 50 |
| Additions | **25** | 27 |
| Amounts settled | **(58)** | (18) |
| Balance at the end of the financial year | **26** | 59 |

The provision primarily comprises restructuring costs in respect of the operating model changes in Australia. All of the provision outstanding at the reporting date is expected to be settled within 12 months (2015–all).

### C. RECOGNITION AND MEASUREMENT

**I. Annual leave**

Liability for annual leave is recognised at the nominal amounts unpaid at the reporting date using remuneration rates that are expected to be paid when the liability is settled, including on-costs.

**II. Long service leave**

A liability for long service leave is recognised as the present value of estimated future cash outflows to be made in respect of services provided by employees up to the reporting date. The estimated future cash outflows are discounted using corporate bond yields which have terms to maturity that match, as closely as possible, the estimated future cash outflows. Factors which affect the estimated future cash outflows such as expected future salary increases, experience of employee departures and period of service, are incorporated in the measurement.

**III. Short term incentive plan**

The short term incentive plan continued in operation during the current reporting year. Eligible employees have the capacity to earn a proportion of their base pay as a cash incentive annually. The incentive opportunity is set depending on an employee's role and responsibilities. The majority of employees are on a 10%, 15% or 20% plan. The incentive payments are determined based on an assessment of individual performance and achievement of a range of business unit and individual goals.

**IV. Superannuation**

For defined benefit superannuation plans, the net financial position of the plans is recognised on the balance sheet and the movement in the net financial position is recognised in profit or loss, except for remeasurements of defined benefit plans (experience adjustments and changes in actuarial assumptions), which are recognised directly in retained earnings. For defined contribution superannuation plans, obligations for contributions are recognised in profit or loss as they become payable.

**V. Restructuring provision**

A restructuring provision is recognised for the expected costs associated with restructuring where there is a detailed formal plan for restructure and a valid expectation has been raised in those persons expected to be affected. The provision is based on the direct expenditure to be incurred which is both directly and necessarily caused by the restructuring and may include termination benefits. It does not include costs associated with ongoing activities. The adequacy of the provision is reviewed regularly and adjusted if required. Revisions to the estimated amount of a restructuring provision are reported in the period in which the revision to the estimate occurs.

# 6. GROUP STRUCTURE

## SECTION INTRODUCTION

This section provides disclosures on the Group structure, including details of the significant controlled entities and equity accounted investments. It also provides details of the significant acquisitions and divestments during the year.

## NOTE 6.1 ACQUISITIONS AND DISPOSALS OF BUSINESSES

### A. ACQUISITION OF SUBSIDIARIES

**I. For the financial year ended 30 June 2016**

ACCIDENT & HEALTH INTERNATIONAL PTY LIMITED (AHI)

On 1 July 2015, the Group acquired the remaining 50% of AHI for a consideration of approximately $25 million. The subsidiary has been consolidated from this date. AHI is an underwriting agency in Australia that has been in operation since 1998 and currently underwrites personal accident, medical and travel insurance.

### B. DISPOSAL OF SUBSIDIARIES

**I. For the financial year ended 30 June 2016**

RUNACRES AND ASSOCIATES LIMITED

During December 2015, the Group disposed of its interest in Runacres and Associates Limited for a consideration of approximately $32 million.

### C. RECOGNITION AND MEASUREMENT

Business combinations are accounted for using the acquisition method. The consideration transferred for the acquisition is the fair value of the assets transferred, the equity instruments issued and the liabilities incurred or assumed at the date of exchange. The consideration includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Acquisition related costs are expensed as incurred.

Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured at fair value on the acquisition date. The Group measures any non-controlling interest, on a transaction-by-transaction basis, either at fair value or at the non-controlling interest's proportionate share of the fair value of the identifiable assets and liabilities.

Where settlement of any part of cash consideration is contingent upon some future event or circumstance, the estimated amounts payable in the future are discounted to their present value at the date of exchange. When the contingent consideration is classified as a liability, the impact on any subsequent changes in fair value is recognised as profit or loss in the statement of comprehensive income.

If the business combination is achieved in stages, the acquisition fair value of the acquirer's previously held equity interest in the acquiree is remeasured to fair value at the acquisition date through profit or loss.

Where the initial accounting for a business combination is determined only provisionally by the first reporting date after acquisition date, the business combination is accounted for using those provisional values. Any subsequent adjustments to those provisional values are recognised within 12 months of the acquisition date and are applied effective from the acquisition date.

## NOTE 6.2 DETAILS OF SUBSIDIARIES

The following table details the Group's general insurance operations and other significant controlled entities:

| | COUNTRY OF INCORPORATION/ FORMATION | EXTENT OF BENEFICIAL INTEREST IF NOT 100% | |
|---|---|---|---|
| | | **2016** | 2015 |
| | | **%** | % |
| **A. ULTIMATE PARENT** | | | |
| Insurance Australia Group Limited | Australia | | |
| **B. SUBSIDIARIES** | | | |
| **I. Australian general insurance operations** | | | |
| CGU Insurance Limited | Australia | | |
| CGU-VACC Insurance Limited | Australia | | |
| HBF Insurance Pty Ltd | Australia | | |
| IAG Re Australia Limited | Australia | | |
| Insurance Australia Limited | Australia | | |
| Insurance Manufacturers of Australia Pty Limited | Australia | **70.00** | 70.00 |
| Mutual Community General Insurance Proprietary Limited | Australia | | |
| Swann Insurance (Aust) Pty Ltd | Australia | | |
| WFI Insurance Limited | Australia | | |

| | COUNTRY OF INCORPORATION/ FORMATION | EXTENT OF BENEFICIAL INTEREST IF NOT 100% 2016 % | 2015 % |
|---|---|---|---|
| **II. New Zealand general insurance operations** | | | |
| AMI Insurance Limited | New Zealand | | |
| IAG New Zealand Limited | New Zealand | | |
| Lumley General Insurance (NZ) Limited | New Zealand | | |
| **III. International general insurance operations** | | | |
| AAA Assurance Corporation | Vietnam | **63.17** | 63.17 |
| IAG Re Labuan (L) Berhad | Malaysia | | |
| IAG Re Singapore Pte Ltd | Singapore | | |
| PT Asuransi Parolamas | Indonesia | **80.00** | 80.00 |
| Safety Insurance Public Company Limited | Thailand | **98.61** | 98.61 |
| **IV. Corporate operations** | | | |
| IAG Finance (New Zealand) Limited | Australia | | |

## NOTE 6.3 NON-CONTROLLING INTERESTS

### A. SUMMARISED FINANCIAL INFORMATION

Set out below is summarised financial information (before intercompany eliminations) of controlled entities where significant non-controlling interests exist, being Insurance Manufacturers of Australia Pty Limited of which the Group's beneficial interest is 70%.

| | INSURANCE MANUFACTURERS OF AUSTRALIA PTY LIMITED 2016 $m | 2015 $m |
|---|---|---|
| **I. Summarised statement of comprehensive income** | | |
| Net premium revenue | **2,806** | 2,686 |
| Profit/(loss) after tax attributable to IAG shareholders | **181** | 237 |
| Profit/(loss) after tax attributable to non-controlling interest | **78** | 101 |
| Other comprehensive income | **(3)** | 3 |
| Total comprehensive income | **256** | 341 |
| **II. Summarised balance sheet** | | |
| Total assets | **3,601** | 3,498 |
| Total liabilities | **(2,876)** | (2,845) |
| Net assets | **725** | 653 |
| Carrying amount of non-controlling interest | **218** | 196 |
| **III. Summarised cash flow** | | |
| Net cash flows from operating and investing activities | **247** | 444 |
| Dividends paid to other Group entities | **(128)** | (302) |
| Dividends paid to non-controlling interest | **(56)** | (129) |
| Total net cash flows | **63** | 13 |

# NOTE 6.4 INVESTMENT IN JOINT VENTURE AND ASSOCIATES

## A. INTERESTS IN JOINT VENTURE AND ASSOCIATES

Summarised information of interests in material joint venture and associates accounted for on an equity basis is as follows:

| | COUNTRY OF INCORPORATION/ FORMATION | PRINCIPAL ACTIVITY | CARRYING VALUE | | OWNERSHIP INTEREST | |
|---|---|---|---|---|---|---|
| | | | **2016** | 2015 | **2016** | 2015 |
| | | | **$m** | $m | **%** | % |
| AmGeneral Holdings Berhad (AmGeneral) | Malaysia | Insurance underwriting | **360** | 358 | **49.00** | 49.00 |
| SBI General Insurance Company Limited (SBI General) | India | Insurance underwriting | **111** | 118 | **26.00** | 26.00 |
| Bohai Property Insurance Company Ltd (Bohai) | China | Insurance underwriting | **-** | 67 | **-** | 20.00 |
| Other | | | **15** | 18 | | |
| | | | **486** | 561 | | |

Effective 29 December 2015, Bohai ceased to be recognised as an associate following dilution of the Group interest to 16.92% and loss of significant influence. From the effective date, Bohai is recognised as a financial asset (see the note 2.3 investments).

## B. SUMMARISED FINANCIAL INFORMATION

Summarised financial information of material joint venture and associates is provided below. The summarised financial information represents the financial position and performance of the entities as a whole (100% stand-alone basis) and not just IAG's share. The financial statements below are for the year ended 31 March 2016 for AmGeneral and SBI General.

| | **2016** | | 2015 | | |
|---|---|---|---|---|---|
| | **AmGeneral Holdings Berhad** | **SBI General Insurance Company Limited** | AmGeneral Holdings Berhad | SBI General Insurance Company Limited | Bohai Property Insurance Company Ltd |
| | **$m** | **$m** | $m | $m | $m |
| **I. Summarised statement of comprehensive income** | | | | | |
| Revenue | **573** | **483** | 588 | 345 | 433 |
| Profit/(loss) after tax | **59** | **(25)** | 82 | (20) | (13) |
| Other comprehensive income | **-** | **-** | 6 | - | 3 |
| Total comprehensive income | **59** | **(25)** | 88 | (20) | (10) |
| Dividends received from associate | **23** | **-** | 46 | - | - |
| **II. Summarised balance sheet** | | | | | |
| Total assets | **1,849** | **713** | 1,939 | 622 | 717 |
| Total liabilities | **(1,206)** | **(572)** | (1,178) | (445) | (526) |
| Net assets as at reporting date | **643** | **141** | 761 | 177 | 191 |
| Group's ownership interest | **315** | **37** | 373 | 46 | 38 |
| Other adjustments* | **45** | **74** | (15) | 72 | 29 |
| Carrying value as at 30 June | **360** | **111** | 358 | 118 | 67 |

* Other adjustments include IFRS adjustments, foreign exchange revaluations, goodwill, intangibles, and share of profit/(loss) from financial statement date to 30 June.

None of the associates are listed on a stock exchange. Those entities that do not have a 30 June financial year end are equity accounted using financial information for the reporting year to 30 June which includes, at least in part, unaudited management results.

### C. RECOGNITION AND MEASUREMENT

The Group's investments in its associates and joint ventures are accounted for using the equity method and are those entities over which it exercises significant influence or joint control, generally reflecting a shareholding of between 20% and 50% of the voting rights of an entity. The investment in associates is initially recognised at cost (fair value of consideration provided plus directly attributable costs) and subsequently adjusted for the post-acquisition change in the investor's share of net assets of the investee. The investor's share of the profit or loss of the investee is included in the profit or loss of the Consolidated entity and disclosed as a separate line in the consolidated statement of comprehensive income. Distributions received reduce the carrying amount of the investment and are not included as dividend revenue of the Consolidated entity. Movements in the total equity of the investee that are not recognised in the profit or loss of the investee are recognised directly in equity of the Consolidated entity and disclosed in the statement of changes in equity. The carrying values of the investments are reviewed annually for impairment.

Where an entity either began or ceased to be an associate during the current financial reporting year, the investment is equity accounted from the date significant influence commenced or up to the date significant influence ceased.

The financial statements of associates are adjusted where necessary to comply with the significant accounting policies of the Consolidated entity.

When the investor's share of losses exceeds its interest in the investee, the carrying amount of the investment is reduced to nil and recognition of further losses is discontinued except to the extent that the investor has incurred obligations or made payments, on behalf of the investee.

## NOTE 6.5 PARENT ENTITY DISCLOSURES

The ultimate Parent entity in the Consolidated entity is Insurance Australia Group Limited, which is incorporated in Australia. The following information of the Parent entity is disclosed as required by the current regulatory requirements in Australia.

| | | PARENT |
|---|---|---|
| | **2016** | 2015 |
| | **$m** | $m |
| **A. FINANCIAL RESULTS** | | |
| Profit/(loss) for the year | **439** | 463 |
| Total comprehensive income and (expense) for the year, net of tax | **439** | 463 |
| **B. FINANCIAL POSITION** | | |
| Current assets | **287** | 259 |
| Total assets | **13,704** | 13,917 |
| Current liabilities | **28** | 216 |
| Total liabilities | **4,630** | 4,362 |
| **C. SHAREHOLDERS' EQUITY** | | |
| Share capital | **7,275** | 7,275 |
| Reserves | **-** | (29) |
| Retained earnings | **1,799** | 2,309 |
| Total shareholders' equity | **9,074** | 9,555 |

### D. CONTINGENT LIABILITIES

There are no known material exposures to the Parent or events that would require it to satisfy the guarantees or take action under a support agreement.

**Recognition and measurement**

Contingent liabilities are not recognised on the balance sheet but are disclosed where the possibility of settlement is less than probable but more than remote. Provisions are not required with respect to these matters as it is not probable that a future sacrifice of economic benefits will be required or the amount is not reliably measurable. If settlement becomes probable, a provision is recognised. The best estimate of the settlement amount is used in measuring a contingent liability for disclosure.

### E. COMMITMENTS

The Parent has no material commitments.

# 7. OFF-BALANCE SHEET DISCLOSURES

**SECTION INTRODUCTION**

This section provides an overview of those items that are not required to be recognised in the financial statements, but may have informative content in relation to the Group's performance or financial position and is required to be disclosed under the accounting standards. These include:

- contingencies – these primarily relate to contingent liabilities that are only recognised in the financial statements when their settlement becomes probable or the amount to be settled can be reliably measured;
- commitments – this note provides information on the Group's future contractual obligations, which includes those in relation to signed property lease agreements; and
- events subsequent to reporting date - information is included on non-adjusting events, favourable and unfavourable, that occur between the end of the reporting period and the date when the financial statements are authorised for issue. For example, disclosure of the final dividend in relation to a financial year as it is declared to be paid by the Board subsequent to the reporting date.

## NOTE 7.1 CONTINGENCIES

In the normal course of business, transactions are entered into that may generate a range of contingent liabilities. These include litigation arising out of insurance policies and the Consolidated entity's undertakings for maintenance of net worth and liquidity support to subsidiaries. Such undertakings constitute a statement of present intent only and are not intended to give rise to any binding legal obligation. The Directors are of the opinion that provisions are not required in respect of these matters, as it is either not probable that a future sacrifice of economic benefits will be required or the amount is not capable of reliable measurement.

The Consolidated entity conducts fiduciary activities in the form of investment management as it operates as manager, custodian or trustee for a number of investments and trusts. The funds managed on behalf of third parties which are not included in the Consolidated entity's balance sheet had a fair value as at the reporting date of $289 million (2015-$407 million).

## NOTE 7.2 COMMITMENTS

| | **2016** | 2015 |
|---|---|---|
| | **$m** | $m |
| **A. OPERATING LEASE COMMITMENTS** | | |
| **I. Property** | | |
| Due within 1 year | **128** | 130 |
| Due within 1 to 2 years | **107** | 113 |
| Due within 2 to 5 years | **254** | 192 |
| Due after 5 years | **519** | 40 |
| | **1,008** | 475 |
| **II. Equipment** | | |
| Due within 1 year | **20** | 20 |
| Due within 1 to 2 years | **21** | 12 |
| Due within 2 to 5 years | **22** | 13 |
| | **1,071** | 520 |

**B. RECOGNITION AND MEASUREMENT**

Certain properties, motor vehicles and computer equipment are leased under non-cancellable operating leases. Most leases are subject to annual reviews and, where appropriate, a right of renewal has been incorporated into the lease agreements. There are no options to purchase the relevant assets on expiry of the lease.

Operating lease payments are recognised as an expense in the consolidated statement of comprehensive income on a straight line basis over the term of the lease. The operating lease incentives received are initially recognised as a liability, presented as trade and other payables and are subsequently reduced through recognition in profit or loss on a straight line basis over the period of the lease.

## NOTE 7.3 EVENTS SUBSEQUENT TO REPORTING DATE

As the following transactions occurred after reporting date and did not relate to conditions existing at reporting date, no account has been taken of them in the financial statements for the current reporting year ended 30 June 2016. These include:

- on 19 August 2016, the Board determined to pay a final dividend of 13 cents per share, 100% franked. The dividend will be paid on 5 October 2016. The dividend reinvestment plan will operate by acquiring shares on-market for participants with no discount applied; and
- on 19 August 2016, IAG announced, as part of the Group's active capital management program, an off-market share buy-back (via a tender process) of up to $300 million. The share buy-back is expected to represent over 2% of IAG's outstanding issued ordinary share capital. The capital component of the share buy-back is expected to be $2.99 and the balance deemed to be a fully franked dividend. The proceeds of the share buy-back are expected to be dispatched to participating shareholders on 17 October 2016.

# 8. ADDITIONAL DISCLOSURES

**SECTION INTRODUCTION**
This section includes other information that must be disclosed to comply with the Accounting Standards, Corporations Act and ASX listing rules, but which are considered less relevant to understanding the Group's performance or financial position.

## NOTE 8.1 NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT

| | 2016 $m | 2015 $m |
|---|---|---|
| **A. COMPOSITION OF CASH AND CASH EQUIVALENTS** | | |
| Cash held for operational purposes | **263** | 306 |
| Cash and short term money held in investments | **841** | 1,127 |
| Cash and cash equivalents | **1,104** | 1,433 |
| **B. RECONCILIATION OF PROFIT/(LOSS) FOR THE YEAR TO NET CASH FLOWS FROM OPERATING ACTIVITIES** | | |
| Profit/(loss) for the year | **702** | 830 |
| **I. Non-cash items** | | |
| Net (gains) and losses on investments | **(89)** | (241) |
| Amortisation and impairment of intangible assets and goodwill | **332** | 139 |
| Depreciation of property and equipment | **62** | 67 |
| Impairment of investment in associate | **-** | 60 |
| Other non-cash items | **(76)** | 47 |
| **II. Movement in operating assets and liabilities** | | |
| Insurance assets | **(994)** | (1,490) |
| Insurance liabilities | **(1,470)** | 1,713 |
| Net movement in other operating assets and liabilities | **(137)** | (141) |
| Net movement in tax assets and liabilities | **(263)** | (269) |
| Provisions | **(13)** | (17) |
| Net cash flows from operating activities | **(1,946)** | 698 |

The movement in net cash flows from operating activities during the year ended 30 June 2016 primarily reflects two items that are not expected to be as prominent a feature of the Group's cash flows going forward, namely:

- an increase in claims costs paid of $711 million, mainly attributable to the settlement of various natural peril events that occurred in the 2015 financial year. The overall quantum of natural peril losses in that year was unusually high; and
- an increase in outwards reinsurance premium expense paid of $2,602 million which predominantly relates to the BH quota share and the run-off portfolio reinsurance protection placement.

**C. SIGNIFICANT NON-CASH TRANSACTIONS RELATING TO FINANCING AND INVESTING TRANSACTIONS**
There were no financing or investing transactions during the year which have had a material effect on the assets and liabilities that did not involve cash flows.

**D. RECOGNITION AND MEASUREMENT**
Cash and cash equivalents represent cash at bank and on hand, deposits at call and short term money held in investments, net of any bank overdraft. Money held in investments is readily convertible to cash within two working days and subject to insignificant risk of change in value. The majority of the amounts bear variable rates of interest based on daily bank deposit rates. Those balances bearing a fixed rate of interest mature in less than one year.

## NOTE 8.2 RELATED PARTY DISCLOSURES

### A. KEY MANAGEMENT PERSONNEL

#### I. Details of compensation

Key management personnel (KMP) are those persons having authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, including any Director (whether Executive or otherwise) of that entity. It is important to note that the Company's Non-Executive Directors are specifically required to be included as KMP in accordance with AASB 124 Related Party Disclosures. However, the Non-Executive Directors do not consider that they are part of 'management'. The aggregate compensation disclosed in the table below represents the KMP's estimated compensation received from the Group in relation to their involvement in the activities within the Consolidated entity.

| | **2016** | 2015 |
|---|---|---|
| | **$000** | $000 |
| Short term employee benefits | **20,012** | 19,371 |
| Post-employment benefits | **499** | 429 |
| Other long term benefits | **53** | 199 |
| Termination benefits | **3,736** | - |
| Share based payments | **19,082** | 12,676 |
| | **43,382** | 32,675 |

#### II. Other benefits

Remuneration does not include premiums paid by IAG for an insurance contract covering current and former Non-Executive Directors' and Executives' liabilities and legal expenses incurred in respect of the relevant office, as the insurance policies do not specify premiums paid to individual Non-Executive Directors and Executives and the terms of contract specifically prohibit the disclosure of the premium paid. Insurance products provided by the Group are available to all Non-Executive Directors and Executives on the same terms and conditions available to other employees.

## NOTE 8.3 REMUNERATION OF AUDITORS

| | **2016** | 2015 |
|---|---|---|
| | **$000** | $000 |
| **A. KPMG** | | |
| Audit of the financial statements prepared for the Parent and subsidiaries | **7,853** | 7,927 |
| Audit of statutory returns in accordance with regulatory requirements | **1,047** | 1,051 |
| Other assurance services | **151** | 174 |
| Advisory services | **1,369** | 1,075 |
| | **10,420** | 10,227 |
| **B. OTHER AUDITORS** | | |
| Audit of the financial statements prepared for subsidiaries | **26** | 39 |
| Total remuneration of auditors | **10,446** | 10,266 |

## NOTE 8.4 NET TANGIBLE ASSETS

| | **2016** | 2015 |
|---|---|---|
| | **$** | $ |
| Net tangible assets per ordinary share | **1.30** | 1.34 |

Net tangible assets per ordinary share have been determined using the net assets on the balance sheet adjusted for non-controlling interests, intangible assets and goodwill.

## NOTE 8.5 IMPACT OF NEW AUSTRALIAN ACCOUNTING STANDARDS ISSUED

### A. ISSUED AND EFFECTIVE

The Australian Accounting Standards and Interpretations applicable for the current reporting year are:

| TITLE | DESCRIPTION |
|---|---|
| AASB 2015-3 | Amendments to Australian Accounting Standards arising from Withdrawal of AASB 1031 Materiality |

### B. ISSUED BUT NOT YET EFFECTIVE

As at the date of this financial report, there are a number of new and revised accounting standards published by the Australian Accounting Standards Board for which the mandatory application dates fall after the end of this current reporting year.

None of these standards have been early adopted and applied in the current reporting year.

| TITLE | DESCRIPTION | OPERATIVE DATE | NOTE |
|---|---|---|---|
| AASB 9 | Financial Instruments | 1 January 2018 | A |
| AASB 15 | Revenue from Contracts with Customers | 1 January 2018 | A |
| AASB 16 | Leases | 1 January 2019 | B |
| AASB 1057 | Application of Australian Accounting Standards | 1 January 2016 | A |
| AASB 2010-7 | Amendments to Australian Accounting Standards arising from AASB 9 | 1 January 2018 | A |
| AASB 2014-1 (Part E) | Amendments to Australian Accounting Standards – Financial Instruments | 1 January 2018 | A |
| AASB 2014-3 | Amendments to Australian Accounting Standards – Accounting for Acquisitions if Interests in Joint Operations | 1 January 2016 | A |
| AASB 2014-4 | Amendments to Australian Accounting Standards – Clarification of Acceptable Methods of Depreciation and Amortisation | 1 January 2016 | A |
| AASB 2014-7 | Amendments to Australian Accounting Standards arising from AASB 9 (December 2014) | 1 January 2018 | A |
| AASB 2014-9 | Amendments to Australian Accounting Standards – Equity Method in Separate Financial Statements | 1 January 2016 | A |
| AASB 2014-10 | Amendments to Australian Accounting Standards – Sale or Contribution of Assets between an Investor and its Associate | 1 January 2018 | A |
| AASB 2015-1 | Amendments to Australian Accounting Standards – Annual Improvements to Australian Accounting Standards 2012-2014 | 1 January 2016 | A |
| AASB 2015-2 | Amendments to Australian Accounting Standards – Disclosure Initiative: Amendments to AASB 101 | 1 January 2016 | A |
| AASB 2015-5 | Amendments to Australian Accounting Standards – Investment Entities: Applying the Consolidation Exception | 1 January 2016 | A |
| AASB 2015-8 | Amendments to Australian Accounting Standards – Effective Date of AASB 15 | 1 January 2018 | A |
| AASB 2015-9 | Amendments to Australian Accounting Standards – Scope and Application Paragraphs | 1 January 2016 | A |
| AASB 2015-10 | Amendments to Australian Accounting Standards – Effective Date of Amendments to AASB 10 and AASB 128 | 1 January 2018 | A |
| AASB 2016-1 | Amendments to Australian Accounting Standards – Recognition of Deferred Tax Assets for Unrealised Losses | 1 January 2017 | A |
| AASB 2016-2 | Amendments to Australian Accounting Standards – Disclosure Initiative: Amendments to AASB 107 | 1 January 2017 | A |
| AASB 2016-3 | Amendments to Australian Accounting Standards – Clarifications to AASB 15 | 1 January 2018 | A |

TABLE NOTE

A These changes are not expected to have a significant, if any, financial and disclosure impact.

B The changes may have financial impact, however the assessment has not been completed yet.

# DIRECTORS' DECLARATION

In the opinion of the Directors of Insurance Australia Group Limited:

- the financial statements and notes 1 to 8.5, including all the remuneration disclosures that are contained in the Remuneration Report of the Directors' Report, are in accordance with the Corporations Act 2001 including:
  - giving a true and fair view of the financial position of the Company and Consolidated entity as at 30 June 2016 and of their performance, as represented by the results of their operations and their cash flows, for the year ended on that date;
  - complying with Australian Accounting Standards and the Corporations Regulations 2001; and
  - the financial report also complies with International Financial Reporting Standards as disclosed in note 1.2.B; and
- the Remuneration Report of the Directors' Report complies with the Corporations Act 2001 and Australian Accounting Standards; and
- there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.

The Directors have been given the declaration required by section 295A of the Corporations Act 2001 from the Chief Executive Officer and the Chief Financial Officer for the financial year ended 30 June 2016.

Signed at Sydney this 19th day of August 2016 in accordance with a resolution of the Directors.

**Peter Harmer**
Director

# INDEPENDENT AUDITOR'S REPORT

## TO THE SHAREHOLDERS OF INSURANCE AUSTRALIA GROUP LIMITED

### REPORT ON THE FINANCIAL REPORT

We have audited the accompanying financial report of Insurance Australia Group Limited (Company), which comprises the consolidated balance sheet as at 30 June 2016, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated cash flow statement for the year ended on that date, notes 1 to 8.5 comprising a summary of significant accounting policies and other explanatory information and the Directors' Declaration of the Group comprising the Company and the entities it controlled at the year's end or from time to time during the financial year.

### 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 1.2.B, the Directors also state, in accordance with Australian Accounting Standard AASB 101 Presentation of Financial Statements, that the financial statements of the Group 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 of the financial report that gives a true and fair view 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.

We performed the procedures to assess whether in all material respects the financial report presents fairly, in accordance with the Corporations Act 2001 and Australian Accounting Standards, a true and fair view which is consistent with our understanding of the Company's financial position and of its performance.

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

### INDEPENDENCE

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

### AUDITOR'S OPINION

In our opinion:

- the financial report of Insurance Australia Group Limited is in accordance with the Corporations Act 2001, including:
  - giving a true and fair view of the Company's financial position as at 30 June 2016 and of its performance for the year ended on that date; and
  - complying with Australian Accounting Standards and the Corporations Regulations 2001.
- the financial report also complies with International Financial Reporting Standards as disclosed in note 1.2.B.

**REPORT ON THE REMUNERATION REPORT**
We have audited the Remuneration Report included on pages 17 to 34 of the Directors' Report for the year ended 30 June 2016. The Directors of the Company are responsible for the preparation and presentation of the Remuneration Report in accordance with Section 300A of the Corporations Act 2001. Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with auditing standards.

**AUDITOR'S OPINION**
In our opinion, the Remuneration Report of Insurance Australia Group Limited for the year ended 30 June 2016 complies with Section 300A of the Corporations Act 2001.

KPMG

**KPMG**

Terblanché

**Dr Andries B Terblanché**
Partner

Ian Moyser

**Ian Moyser**
Partner

Sydney
19 August 2016

# SHAREHOLDER INFORMATION

Information about Insurance Australia Group Limited including Company announcements, presentations and reports can be accessed at www.iag.com.au.

## ASX CODES

Insurance Australia Group Limited's shares are listed on the ASX under:
- IAG (ordinary shares); and
- IAGPC (convertible preference shares).

Insurance Australia Group Limited's wholly owned subsidiary IAG Finance (New Zealand) Limited issued reset exchangeable securities (RES) in January 2005 which are listed on the ASX under IANG.

## ANNUAL REPORT

Under the Corporations Act 2001 regarding the provision of Annual Reports to shareholders, the default option for receiving Annual Reports is an electronic copy via IAG's website at www.iag.com.au.

## ANNUAL GENERAL MEETING

The 2016 annual general meeting (AGM) of Insurance Australia Group Limited will be held on Friday, 21 October 2016 commencing at 10am at The Wesley Conference Centre, 220 Pitt Street, Sydney NSW 2000, Australia. The AGM will be webcast live on the internet at www.iag.com.au/shareholder-centre/annual-meetings and an archive version will be placed on the website to enable the AGM to be viewed at a later time.

## ONLINE VOTING

Shareholders can lodge voting instructions electronically either as a direct vote or by appointing a proxy for the 2016 AGM at www.iag.com.au. The information required to log on and use online voting is shown on your voting form.

## SHAREHOLDER QUESTIONS

If you would like to submit a written question to the Company or the Company's auditor with regard to the AGM or any of the resolutions to be discussed please use the form supplied and return it with your completed Voting Form in the pre-addressed envelope provided or by fax to +61 (0)3 9473 2555. Please note your questions for the auditor must be received by 5pm on 14 October 2016.

You may also submit a question after completing your voting instructions online at www.iag.com.au. Members will also be given a reasonable opportunity to ask questions of the Company and the auditor at the AGM.

During the course of the AGM IAG intends to answer as many of the frequently asked questions as practicable but will not be responding to individual written questions. Responses to the most commonly asked questions will be added to the website at www.iag.com.au/shareholder-centre/annual-meetings.

## DIVIDEND PAYMENT METHODS

Insurance Australia Group Limited no longer issues dividend payments by cheque to shareholders resident in Australia. Shareholders should provide the share registry with their alternative instructions as detailed below:

**IAG ordinary shares**
- Paid directly into a New Zealand bank account or to an Australian bank, credit union, building society or nominated account; or
- Eligible shareholders can choose to participate in IAG's Dividend Reinvestment Plan (DRP), if available, providing the option to increase your shareholding without incurring brokerage or GST.

**IAGPC convertible preference shareholders**
- Paid directly into an Australian bank, credit union, building society or nominated account.

## MANAGE YOUR HOLDING

Using your Shareholder Reference Number (SRN) or Holder Identification Number (HIN) and postcode of your registered address you can view your holding online through IAG's share registry, Computershare, by following the easy prompts on their website at www.investorcentre.com where you will be able to:
- view your holding balance;
- review your dividend payment history;
- access shareholder forms; and
- retrieve holding statements, including recent dividend payment advices.

The share registry investor centre site will also allow you to update or add details to your shareholding. If you wish to amend or update any of the current details you will be asked to register by choosing a User ID and Password which you can easily remember for additional security purposes.

You will also be asked to enter answers to three personal questions for verification purposes should you forget your password in the future.

If you have previously used the Investor Centre site you will be asked to key in your password only.

Once you have completed these steps you are then able to update your details and submit your changes to the share register including:

- change or amend your address if you are registered with an SRN;
- nominate or amend your direct credit payment instructions;
- set up or amend your DRP instructions;
- sign up for electronic shareholder communications, including the annual report via email; and
- add/change TFN/ABN details.

A confirmation/receipt number will be shown on-screen for your online transaction which should be recorded should you have a question in the future.

You are strongly advised to lodge your TFN, ABN or exemption. If you choose not to lodge these details with the share registry, then IAG is obliged to deduct tax at the highest marginal tax rate (plus the Medicare levy) from the unfranked portion of any dividend or interest payment.

Shareholders may also complete a number of transactions or request a form over the phone by contacting the share registry on 1300 360 688.

## EMAIL ALERT SERVICE

You can register to receive an email alert advising of new IAG media releases, financial announcements or presentations. You simply need to visit IAG's website at www.iag.com.au, click on the email alert button in the right hand margin and register your email address.

IAG has an email alert service that allows you to choose to receive email alerts about specific subjects (annual meetings, annual reports, careers information, company announcements, government submissions, results and sustainability reports).

## EMAIL ENQUIRIES

If you have a question, you can email your enquiry directly to IAG's share registry at iag@computershare.com.au. If your question relates to an IAG Company matter and the answer is not on IAG's website, you can email your question to investor.relations@iag.com.au.

## ORDINARY SHARES INFORMATION

| IMPORTANT DATES* | 2016 |
|---|---|
| IAG year end | 30 June |
| Full year results and dividend announced | 19 August |
| Annual report and notice of meeting mailout commences | 6 September |
| Record date for final dividend | 7 September |
| Final dividend paid | 5 October |
| Written questions for the auditor close (5pm) | 14 October |
| Proxy return close (10am) | 19 October |
| Annual general meeting (10am) | 21 October |
| IAG half year end | 31 December |

* Please note that some dates are subject to change.

| TWENTY LARGEST ORDINARY SHAREHOLDERS AS AT 1 AUGUST 2016 | NUMBER OF SHARES | % OF ISSUED CAPITAL |
|---|---|---|
| HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED | **443,922,873** | **18.26** |
| J P MORGAN NOMINEES AUSTRALIA LIMITED | **315,119,281** | **12.96** |
| NATIONAL NOMINEES LIMITED | **197,587,466** | **8.13** |
| CITICORP NOMINEES PTY LIMITED | **144,365,817** | **5.94** |
| NATIONAL INDEMNITY COMPANY | **89,766,607** | **3.69** |
| BNP PARIBAS NOMS PTY LTD <DRP> | **59,487,351** | **2.45** |
| BNP PARIBAS NOMINEES PTY LTD <AGENCY LENDING DRP A/C> | **49,996,214** | **2.06** |
| RBC INVESTOR SERVICES AUSTRALIA NOMINEES PTY LIMITED <PI POOLED A/C> | **29,555,574** | **1.22** |
| CITICORP NOMINEES PTY LIMITED <COLONIAL FIRST STATE INV A/C> | **28,012,513** | **1.15** |
| RBC INVESTOR SERVICES AUSTRALIA NOMINEES PTY LIMITED <BKCUST A/C> | **23,320,880** | **0.96** |
| ARGO INVESTMENTS LIMITED | **6,981,075** | **0.29** |
| HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED <NT-COMNWLTH SUPER CORP A/C> | **6,949,618** | **0.29** |
| AMP LIFE LIMITED | **6,536,587** | **0.27** |
| MILTON CORPORATION LIMITED | **5,805,282** | **0.24** |
| IAG SHARE PLAN NOMINEE PTY LIMITED <IAG DAP UNALLOCATED ACCOUNT> | **5,578,175** | **0.23** |
| NATIONAL NOMINEES LIMITED <DB A/C> | **4,123,356** | **0.17** |
| AUSTRALIAN FOUNDATION INVESTMENT COMPANY LIMITED | **3,839,215** | **0.16** |
| NAVIGATOR AUSTRALIA LTD <SMA ANTARES INV DV BUILD A/C> | **3,492,504** | **0.14** |
| UBS NOMINEES PTY LTD | **3,291,738** | **0.14** |
| HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED | **3,200,962** | **0.13** |
| Total for top 20 | **1,430,933,088** | **58.88** |

| RANGE OF ORDINARY SHAREHOLDERS AS AT 1 AUGUST 2016 | NUMBER OF HOLDERS | NUMBER OF SHARES | % OF ISSUED CAPITAL |
|---|---|---|---|
| 1-1,000 | **434,227** | **228,230,646** | **9.39** |
| 1,001-5,000 | **280,254** | **505,820,789** | **20.80** |
| 5,001-10,000 | **13,805** | **95,154,182** | **3.91** |
| 10,001-100,000 | **5,037** | **101,276,472** | **4.17** |
| 100,001 and over | **163** | **1,500,902,566** | **61.73** |
| Total | **733,486** | **2,431,384,655** | **100.00** |

| | | | |
|---|---|---|---|
| Shareholders with less than a marketable parcel of 82 shares as at 1 August 2016 | **8,513** | **272,435** | |

**DIVIDEND DETAILS**

| SHARE CLASS | DIVIDEND | FRANKING | AMOUNT PER SHARE | DRP ISSUE PRICE | PAYMENT DATE |
|---|---|---|---|---|---|
| Ordinary | Interim | Fully franked | 13 cents | $5.4894 | 30 March 2016 |
| Ordinary | Special | Fully franked | 10 cents | $5.4894 | 30 March 2016 |
| Ordinary | Final | Fully franked | 13 cents | * | 5 October 2016 |

* The DRP issue price for the final dividend is scheduled to be announced on 23 September 2016.

## SUBSTANTIAL SHARE HOLDINGS AS AT 1 AUGUST 2016

As at 1 August 2016 there were no substantial shareholders holding more than 5.00% of the issued capital.

## IAGPC CONVERTIBLE PREFERENCE SHARES INFORMATION

| IMPORTANT DATES* | 2016 |
|---|---|
| Record date for dividend | 24 October 2016 |
| Dividend paid | 1 November 2016 |

* Please note that some dates are subject to change.

| TWENTY LARGEST CONVERTIBLE PREFERENCE SHAREHOLDERS AS AT 1 AUGUST 2016 | NUMBER OF SHARES | % OF ISSUED CAPITAL |
|---|---|---|
| J P MORGAN NOMINEES AUSTRALIA LIMITED | **561,889** | **14.89** |
| HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED | **202,529** | **5.37** |
| IOOF INVESTMENT MANAGEMENT LIMITED <IPS SUPER A/C> | **151,135** | **4.00** |
| BNP PARIBAS NOMS PTY LTD <DRP> | **88,969** | **2.36** |
| NATIONAL NOMINEES LIMITED | **87,222** | **2.31** |
| CITICORP NOMINEES PTY LIMITED <DPSL> | **71,112** | **1.88** |
| NAVIGATOR AUSTRALIA LTD <MLC INVESTMENT SETT A/C> | **61,125** | **1.62** |
| HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED-A/C 2 | **60,617** | **1.61** |
| AUSTRALIAN MASTERS YIELD FUND NO 3 LIMITED | **48,750** | **1.29** |
| NULIS NOMINEES (AUSTRALIA) LIMITED <NAVIGATOR MAST PLAN SETT A/C> | **43,651** | **1.16** |
| AUSTRALIAN EXECUTOR TRUSTEES LIMITED <NO 1 ACCOUNT> | **41,864** | **1.11** |
| THE TRUST COMPANY SUPERANNUATION LIMITED <GPMSF2 - FUTURE SUPER A/C> | **39,898** | **1.06** |
| EASTCOTE PTY LTD <VAN LIESHOUT FAMILY A/C> | **30,000** | **0.79** |
| IOOF INVESTMENT MANAGEMENT LIMITED <IPSIDPS A/C> | **23,555** | **0.62** |
| ADTEC NO 2 PTY LTD | **22,410** | **0.59** |
| EDSGEAR PTY LIMITED | **19,703** | **0.52** |
| CITICORP NOMINEES PTY LIMITED | **18,837** | **0.50** |
| NAVIGATOR AUSTRALIA LTD <JB WERE LIST FIX INTSMA A/C> | **17,358** | **0.46** |
| THE WYATT BENEVOLENT INSTITUTION INC | **15,517** | **0.41** |
| EASTHAM HOLDINGS PTY LTD | **14,530** | **0.39** |
| Total for top 20 | **1,620,671** | **42.94** |

| RANGE OF CONVERTIBLE PREFERENCE SHAREHOLDERS AS AT 1 AUGUST 2016 | NUMBER OF HOLDERS | NUMBER OF SHARES | % OF ISSUED CAPITAL |
|---|---|---|---|
| 1-1,000 | **4,049** | **1,305,375** | **34.59** |
| 1,001-5,000 | **301** | **630,121** | **16.70** |
| 5,001-10,000 | **23** | **171,092** | **4.53** |
| 10,001-100,000 | **21** | **751,587** | **19.92** |
| 100,001 and over | **3** | **915,553** | **24.26** |
| Total | **4,397** | **3,773,728** | **100.00** |

| | | | |
|---|---|---|---|
| Shareholders with less than a marketable parcel of five shares as at 1 August 2016 | **8** | **10** | |

**DIVIDEND DETAILS**

| SHARE CLASS | DIVIDEND | FRANKING | AMOUNT PER SHARE | PAYMENT DATE |
|---|---|---|---|---|
| Preference | Interim | Fully franked | 2.1501 | 2 May 2016 |
| Preference | Final | Fully franked | 2.2040 | 1 November 2016 |

# CORPORATE DIRECTORY

## SHARE REGISTRY

**COMPUTERSHARE INVESTOR SERVICES PTY LIMITED**
GPO Box 4709
Melbourne VIC 3001
Australia

**Hand deliveries to**
Level 4
60 Carrington Street
Sydney NSW 2000

**Telephone**
(within Australia) 1300 360 688
(outside Australia) +61 (0)3 9415 4210

**Fax**
(general) +61 (0)3 9473 2470

**Email**
iag@computershare.com.au

## REGISTERED OFFICE

**INSURANCE AUSTRALIA GROUP LIMITED**
Level 26
388 George Street
Sydney NSW 2000
Australia

**Telephone**
+61 (0)2 9292 9222

**Fax**
+61 (0)2 9292 8072

**Website**
www.iag.com.au

# FIVE YEAR FINANCIAL SUMMARY

| | **2016** | 2015 | 2014 | 2013 | 2012[a] |
|---|---|---|---|---|---|
| | **$m** | $m | $m | $m | $m |
| Gross written premium | **11,367** | 11,440 | 9,779 | 9,498 | 8,495 |
| Premium revenue | **11,411** | 11,525 | 9,721 | 9,135 | 8,046 |
| Outwards reinsurance premium expense | **(3,183)** | (1,196) | (1,077) | (817) | (700) |
| Net premium revenue | **8,228** | 10,329 | 8,644 | 8,318 | 7,346 |
| Net claims expense | **(5,397)** | (6,941) | (5,201) | (4,982) | (5,421) |
| Underwriting expenses | **(2,116)** | (2,847) | (2,303) | (2,178) | (1,994) |
| Underwriting profit/(loss)[b] | **715** | 541 | 1,140 | 1,158 | (69) |
| Net investment income on assets backing insurance liabilities | **463** | 562 | 439 | 270 | 914 |
| Management reported insurance profit[b] | **1,178** | 1,103 | 1,579 | 1,428 | 845 |
| Net investment income from shareholders' funds | **97** | 223 | 396 | 347 | 89 |
| Other income | **204** | 187 | 199 | 175 | 164 |
| Share of net profit/(loss) of associates[c] | **17** | 6 | (8) | (29) | (13) |
| Finance costs | **(99)** | (107) | (98) | (95) | (97) |
| Corporate and administration expenses[d] | **(423)** | (383) | (255) | (208) | (205) |
| Amortisation expense and impairment charges of acquired intangible assets and goodwill | **(54)** | (80) | (11) | (25) | (20) |
| Profit before income tax | **920** | 949 | 1,802 | 1,593 | 763 |
| Income tax expense | **(218)** | (119) | (472) | (424) | (177) |
| Profit after tax from continuing operations | **702** | 830 | 1,330 | 1,169 | 586 |
| (Loss) after tax from discontinued operation | **-** | - | - | (287) | (321) |
| Net profit attributable to non-controlling interests | **(77)** | (102) | (97) | (106) | (58) |
| Net profit attributable to IAG shareholders | **625** | 728 | 1,233 | 776 | 207 |
| Ordinary shareholders' equity ($ million) | **6,563** | 6,817 | 6,568 | 4,786 | 4,343 |
| Total assets ($ million)[e] | **30,030** | 31,402 | 29,748 | 24,859 | 25,132 |
| **KEY RATIOS** | | | | | |
| Gross written premium growth | **(0.6)%** | 17.0 % | 3.0 % | 11.8 % | n/a |
| Loss ratio[f] | **65.6 %** | 67.2 % | 60.2 % | 59.9 % | 73.8 % |
| Expense ratio[g] | **25.7 %** | 27.6 % | 26.7 % | 26.2 % | 27.1 % |
| Combined ratio[h] | **91.3 %** | 94.8 % | 86.9 % | 86.1 % | 100.9 % |
| Insurance margin[i] | **14.3 %** | 10.7 % | 18.3 % | 17.2 % | 11.5 % |
| **SHARE INFORMATION** | | | | | |
| Dividends per ordinary share - fully franked (cents) | **36.00** | 29.00 | 39.00 | 36.00 | 17.00 |
| Basic earnings per ordinary share (cents) | **25.79** | 31.22 | 56.09 | 37.57 | 10.01 |
| Diluted earnings per ordinary share (cents) | **25.34** | 30.45 | 53.62 | 36.44 | 9.96 |
| Ordinary share price at 30 June ($) (ASX: IAG) | **5.45** | 5.58 | 5.84 | 5.44 | 3.48 |
| Convertible preference share price at 30 June ($) (ASX: IAGPC) | **101.50** | 101.60 | 106.44 | 101.88 | 98.10 |
| Reset exchangeable securities price at 30 June ($) (ASX: IANG) | **100.00** | 103.10 | 107.00 | 102.80 | 99.30 |
| Issued ordinary shares (million) | **2,431** | 2,431 | 2,341 | 2,079 | 2,079 |
| Issued convertible preference shares (million) | **4** | 4 | 4 | 4 | 4 |
| Market capitalisation (ordinary shares) at 30 June ($ million) | **13,249** | 13,565 | 13,671 | 11,310 | 7,235 |
| Net tangible asset backing per ordinary share ($)[e] | **1.30** | 1.34 | 1.27 | 1.38 | 1.20 |

(a) The financial information for 2012 has been re-presented to reflect the treatment of the United Kingdom business as a discontinued operation.
(b) A reconciliation between the statutory results to five year financial summary presentation is outlined in the Operating and Financial Review section of the Directors' Report.
(c) Share of net profit/(loss) of associates includes regional support and development costs.
(d) Includes a $198 million impairment of capitalised software for 2016 and a $60 million impairment of the investment in Bohai Insurance for 2015.
(e) The financial information for 2014 has been restated to reflect the fair value adjustments to the net assets acquired in respect of the former Wesfarmers business in 2014.
(f) The loss ratio refers to the net claims expense as a percentage of net premium revenue.
(g) The expense ratio refers to underwriting expenses as a percentage of net premium revenue.
(h) The combined ratio refers to the sum of the loss ratio and expense ratio.
(i) Insurance margin is a ratio of insurance profit over net premium revenue.

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iag

## AUSTRALIA

NRMA Insurance, SGIO, SGIC, Swann Insurance

RACV[1], CGU, WFI, Coles Insurance[2]

## NEW ZEALAND

State, NZI, AMI Insurance, Lumley

## VIETNAM

AAA Assurance[3]

## THAILAND

Safety Insurance[4], NZI[4]

## INDIA

SBI General Insurance[5]

## MALAYSIA

AmAssurance[6], Kurnia Insurans[6]

## INDONESIA

Asuransi Parolamas[7]

**100% owned unless marked with a footnote**

1 IAG's short tail personal insurance products are distributed in Victoria under the RACV brand, via a distribution relationship and underwriting joint venture with RACV. These products are distributed by RACV and manufactured by Insurance Manufacturers of Australia Pty Limited (IMA), which is 70% owned by IAG and 30% by RACV.

2 IAG owns 100% of WFI Insurance Limited (WFI), the underwriter of general insurance products under the Coles Insurance brand. These products are distributed by Coles under an authorised representative agreement with WFI.

3 IAG owns 63.17% of AAA Assurance Corporation, based in Vietnam.

4 IAG holds a 98.61% beneficial interest in Safety Insurance, based in Thailand, which trades under the Safety and NZI brands.

5 IAG owns 26% of SBI General Insurance Company, a joint venture with State Bank of India.

6 IAG owns 49% of the general insurance arm of Malaysian-based AmBank Group, AmGeneral Holdings Berhad (AmGeneral), which trades under the AmAssurance and Kurnia brands.

7 IAG owns 80% of PT Asuransi Parolamas, based in Indonesia.

All ownership percentages are as at 30 June 2016.