INSURANCE AUSTRALIA GROUP LIMITED
PRELIMINARY FINAL REPORT FOR THE YEAR ENDED 30 JUNE 2018

APPENDIX 4E (ASX Listing rule 4.3A)

RESULTS FOR ANNOUNCEMENT TO THE MARKET

	UP / DOWN	% CHANGE	2018 $m	2017* $m
Revenue from ordinary activities	Up	2.6 %	**16,411**	15,992
Net profit after tax from continuing operations attributable to shareholders of the Parent	Up	1.0 %	**947**	938
Net loss after tax from discontinued operations attributable to shareholders of the Parent	Up	166.7 %	**(24)**	(9)
Net profit attributable to shareholders of the Parent	Down	0.6 %	**923**	929

* Prior year comparatives have been re-presented due to the discontinued operations. Refer to Note 6.5 in Attachment A.

DIVIDENDS – ORDINARY SHARES	AMOUNT PER SECURITY	FRANKED AMOUNT PER SECURITY
Final dividend	20.0 cents	20.0 cents
Interim dividend	14.0 cents	14.0 cents

FINAL DIVIDEND DATE	
Record date	22 August 2018
Payment date	27 September 2018

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 23 August 2018. The DRP Issue Price will be based on a volume-weighted average price for a 10-day trading window from 27 August 2018 to 7 September 2018 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 2018 (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 2018

The Numbers

Annual Report 2018

Insurance Australia Group Limited

ABN 60 090 739 923

Contents

Key dates

2018 financial year end	30 June 2018
Full year results and dividend announcement	15 August 2018
Notice of meeting mailed to shareholders	10 September 2018
Final dividend for ordinary shares	
Record date	22 August 2018
Payment date	27 September 2018
Annual general meeting	26 October 2018
Half year end	31 December 2018
Half year results and dividend announcement	6 February 2019*
Interim dividend for ordinary shares	
Record date	13 February 2019*
Payment date	20 March 2019*
2019 financial year end	30 June 2019
Full year results and dividend announcement	8 August 2019*

* 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 2018 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 financial year 2018. This year's corporate governance report is available in the About Us area of our website (www.iag.com.au).

The financial statements are structured to provide prominence to the disclosures that are considered most relevant to the user's understanding of the operations, results and financial position of the Group.

IAG is a "dual listed issuer" that is listed on both the ASX and the NZX Debt Market. As such, IAG is subject to some, but not all of the NZX Main Board/Debt Market Listing Rules ("NZX Listing Rules"). In particular, the rules set out in Appendix 17 to the NZX Listing Rules do not apply to IAG.

All figures are in Australian dollars unless otherwise stated.

2018 annual review and safer communities report

This report should be read with the 2018 annual review and safer communities report, which provides a summary of IAG's operating performance, including the Chairman's, CEO's and CFO's reviews.

An interactive version of the annual review and safer communities report is available from the home page of our website at www.iag.com.au. Detailed information about the Group's shared value strategy and non-financial performance is available in the shared value area of our website.

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 99.

2018 annual general meeting

IAG's 2018 annual general meeting will be held on Friday, 26 October 2018, at the Sofitel Sydney Wentworth Hotel, 61-101 Phillip Street, Sydney, commencing at 9.30am. 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 online at www.iag.com.au, from Monday, 10 September 2018.

DIRECTORS' REPORT

The Directors present their report together with the consolidated financial report of Insurance Australia Group Limited and its subsidiaries for the financial year ended 30 June 2018 and the Auditor's Report.

The following terminology is used throughout the financial report:

- Company or Parent – Insurance Australia Group Limited; and
- IAG or Group – 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 B BRYAN AM

BA (Econ), MA (Econ) – Chairman and Independent Non-Executive Director

INSURANCE INDUSTRY EXPERIENCE

Elizabeth Bryan was appointed a Director of IAG on 5 December 2014, and became Chairman on 31 March 2016. She is the Chairman of the Nomination Committee, and attends all Board committee meetings in an ex-officio capacity. 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 30 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 Group.

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 Group, since 2015;
- Westpac Banking Corporation (2006-2016); and
- Caltex Australia Limited (2002-2015).

MANAGING DIRECTOR

PETER G HARMER

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 the Nomination Committee.

Peter joined IAG in 2010 as Chief Executive Officer, CGU Insurance and has held a number of senior roles. Prior to his current role, he was Chief Executive of the IAG Labs division, responsible for driving digital and innovation across IAG and its brands, and creating incubator areas to explore innovative opportunities across the fintech landscape.

Before this, Peter was Chief Executive of the Australian Commercial Insurance division.

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 nearly 40 years of 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 2015.

OTHER DIRECTORS

DUNCAN M BOYLE

BA (Hons), FCII, FAICD – Independent Non-Executive Director

INSURANCE INDUSTRY EXPERIENCE

Duncan Boyle was appointed a Director of IAG on 23 December 2016. He is Chairman of the Risk Committee and a member of the Audit Committee, People and Remuneration Committee and Nomination Committee.

Duncan is Chairman of TAL Dai-ichi Life and a former Non-Executive Director of QBE Insurance Group.

Duncan's executive career included senior roles with a variety of financial and corporate institutions, including Royal and Sun Alliance Insurance. He also held various board roles with the Association of British Insurers, Insurance Council of Australia, Global Aviation Underwriting Managers, AAMI and APIA.

OTHER BUSINESS AND MARKET EXPERIENCE

Duncan is a former Non-Executive Director of Stockland Group and Clayton Utz.

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

- Stockland Group (2007-2015).

HUGH A FLETCHER

BSc/BCom, MCom (Hons), MBA – Independent Non-Executive Director

INSURANCE INDUSTRY EXPERIENCE

Hugh Fletcher was appointed a Director of IAG on 1 September 2007 and Chairman of IAG New Zealand Limited on 1 September 2003. He is a member of the Risk Committee, People and Remuneration 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 a trustee of The University of Auckland Foundation. He 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 Officer.

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 and former Non-Executive Director of Vector Limited. He was also a 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 2008;
- Rubicon Limited, since 2001; and
- Vector Limited, (2001-2017).

SHEILA C MCGREGOR

BA (Hons), LLB, AICD Diploma – Independent Non-Executive Director

INSURANCE INDUSTRY EXPERIENCE

Sheila McGregor was appointed a Director of IAG on 13 March 2018. She is a member of the Audit Committee and Nomination Committee.

Sheila served on the boards of the Commonwealth Bank of Australia's life and general insurance subsidiaries (The Colonial Mutual Life Assurance Society Limited and Commonwealth Insurance Limited) between 2005 and 2009.

OTHER BUSINESS AND MARKET EXPERIENCE

Sheila is a Partner at Gilbert + Tobin and a member of its Board and Partner Remuneration Committee. She heads up the firm's national Technology + Digital Group, advising on business-critical technology and digital issues. Previously, she was a Senior Partner at Herbert Smith Freehills (then Freehills).

Sheila is a Non-Executive Director of Crestone Holdings Limited, which provides wealth advice and portfolio management services, and is Chairman of the Loreto Kirribilli School Board. Between 2009 and 2014, she was Chairman of the Royal Women's Hospital Foundation, established principally to raise public funds for the Royal Hospital for Women in Sydney and was previously a Director on the Board of the Australian Indigenous Chamber of Commerce.

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

- Seven West Media Limited (2015–2017).

JONATHAN (JON) B NICHOLSON

BA – Independent Non-Executive Director

INSURANCE INDUSTRY EXPERIENCE

Jon Nicholson was appointed a Director of IAG on 1 September 2015. He is Chairman of the People and Remuneration Committee and a member of the 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.

HELEN M NUGENT AO

BA (Hons), PhD, MBA, HonsDBus – Independent Non-Executive Director

INSURANCE INDUSTRY EXPERIENCE

Helen Nugent was appointed a Director of IAG on 23 December 2016. She is a member of the Audit Committee, Nomination Committee and Risk Committee.

OTHER BUSINESS AND MARKET EXPERIENCE

Helen is Chairman of Ausgrid and the National Disability Insurance Agency.

She has over 30 years of experience in the financial services sector. This includes having been Chairman of Veda Group, Funds SA, Swiss Re (Australia) and Swiss Re (Life and Health) Australia, as well as being a Non-Executive Director of Macquarie Group, Mercantile Mutual and the State Bank of New South Wales. She has also been Chairman of Australian Rail Track Corporation and a Non-Executive Director of Origin Energy.

Other former senior roles include Director of Strategy at Westpac Banking Corporation, Professor and Director of the MBA Program at the Australian Graduate School of Management and Principal of McKinsey & Company, where she specialised in the financial services and resources sectors.

Helen has given back to the community in education and the arts, having been Chancellor of Bond University, President of Cranbrook School, Chairman of the National Opera Review, Chairman of the Major Performing Arts Inquiry and Deputy Chairman of Opera Australia. She is currently Chairman of the National Portrait Gallery of Australia.

Helen is an Officer of the Order of Australia (AO) and has received a Centenary Medal as well as an Honorary Doctorate in Business from the University of Queensland.

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

- Origin Energy Limited (2003-2017); and
- Veda Group (2013-2016).

THOMAS (TOM) W POCKETT

CA, BCom – Independent Non-Executive Director

INSURANCE INDUSTRY EXPERIENCE

Tom Pockett was appointed a Director of IAG effective 1 January 2015. He is Chairman of the Audit Committee and a member of the Risk Committee and Nomination Committee.

OTHER BUSINESS AND MARKET EXPERIENCE

Tom is Chairman and Non-Executive Director of Stockland Group, Chairman and Non-Executive Director of Autosports Group Limited and a Director of Sunnyfield Independence Association and of O'Connell Street 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 has also held senior finance roles at Commonwealth Bank, Lend Lease Corporation and Deloitte.

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

- Autosports Group Limited, since 2016; and
- Stockland Group, since 2014.

MICHELLE TREDENICK

BSc, FAICD, F Fin – Independent Non-Executive Director

INSURANCE INDUSTRY EXPERIENCE

Michelle Tredenick was appointed a Director of IAG on 13 March 2018 and is a member of the People and Remuneration Committee and Nomination Committee.

Michelle has held a number of senior executive roles in major Australian companies. She was Chief Information Officer (CIO) for Suncorp, MLC and National Australia Bank, as well as Head of Strategy for MLC and Head of Strategy and Marketing for Suncorp. She was also CEO of MLC's Corporate Superannuation business and Head of their New Zealand Insurance and Wealth Management businesses.

OTHER BUSINESS AND MARKET EXPERIENCE

Michelle is a Non-Executive Director of the Bank of Queensland (since 2011), where she chairs the Information Technology Committee. She is a Director of Cricket Australia (since 2015) and Urbis Pty Ltd (since 2016). Michelle is also a member of The Ethics Centre Board and a member of the Senate of The University of Queensland. She is a former Chairman of the IAG & NRMA Superannuation Plan (2012-2018).

She was awarded Banking and Finance CIO of the Year in 1998 and 2006 and is a Fellow of the Australian Institute of Company Directors.

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

- Bank of Queensland Limited (since 2011); and
- Vocation Limited (2013-2015).

PHILIP J TWYMAN AM

BSc, MBA – Independent Non-Executive Director

INSURANCE INDUSTRY EXPERIENCE

Philip Twyman was appointed a Director of IAG on 9 July 2008. He is a member of the Audit Committee, Risk Committee and Nomination Committee.

Philip was formerly Group Executive Director of Aviva plc 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 insurance operations in Asia, Australia, Europe and North America. He was also responsible for starting and nurturing new insurance businesses in China, India, Indonesia and Hong Kong. Overall, Philip has 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 from April 2007 to July 2008.

OTHER BUSINESS AND MARKET EXPERIENCE

Philip is also a director 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

Alison Deans was a Director from 1 February 2013 to 20 October 2017.

SECRETARY OF INSURANCE AUSTRALIA GROUP LIMITED

CHRISTOPHER (CHRIS) J 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 and 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 has more than 30 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.

On 10 July 2018, IAG announced that Chris Bertuch has decided to leave IAG effective 30 September 2018.

REBECCA FARRELL

LLB (Hons), BA

Rebecca is currently the Acting Group General Counsel and Company Secretary. Rebecca joined IAG in July 2017 when she was appointed Deputy Group General Counsel and Company Secretary, being formally appointed as Company Secretary on 22 August 2017.

Rebecca is a senior legal and governance professional with over 20 years of experience advising boards and senior management, including in roles for Amcor (Zurich, Switzerland), Westpac Banking Corporation and the Future Fund. Rebecca started her career as a corporate and M&A lawyer at King & Wood Mallesons in Melbourne, before moving to New York where she worked with Fried Frank. On returning from New York, Rebecca joined the Head Office Advisory Team at Herbert Smith Freehills in Melbourne before moving to Sydney to assist in the set-up of that team in the Sydney market.

SEJIL MISTRY-MOODLEY

BProc, LLM, FGIA, FCIS

Sejil was appointed Deputy Company Secretary and Legal Counsel on 18 September 2015. Sejil has over 20 years' experience in the insurance industry. She is a member of the Law Society and a Fellow of the Governance Institute of Australia.

MEETINGS OF DIRECTORS

The number of meetings each Director was eligible to attend and actually attended during the financial year, including those attended in an ex-officio capacity, is summarised below:

DIRECTOR	BOARD OF DIRECTORS				PEOPLE AND REMUNERATION COMMITTEE		AUDIT COMMITTEE		RISK COMMITTEE		BOARD SUB COMMITTEE		NOMINATION COMMITTEE	
	Scheduled		Unscheduled											
Total number of meetings held	7		5		4		5		5		2		1	
	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	7	7	5	5	-	4	-	5	-	5	2	2	1	1
Peter Harmer	7	7	5	5	-	4	-	5	-	5	2	2	1	1
Duncan Boyle(1)	7	7	5	5	2	2	5	5	5	5	-	-	1	1
Alison Deans(2)	2	2	-	-	1	1	2	2	-	1	-	-	1	1
Hugh Fletcher	7	7	5	5	4	4	-	2	5	5	2	2	1	1
Sheila McGregor(3)	3	3	1	-	-	2	1	1	-	1	-	-	-	-
Jon Nicholson	7	7	5	5	4	4	-	2	5	5	-	-	1	1
Helen Nugent(4)	7	7	5	5	2	2	5	5	1	4	-	-	1	1
Tom Pockett	7	6	5	5	-	-	5	5	5	4	-	-	1	1
Michelle Tredenick(5)	3	3	1	1	2	2	-	-	-	1	-	-	-	-
Philip Twyman	7	6	4	3	-	1	5	5	5	5	-	-	1	1

(1) Duncan Boyle was appointed to the People and Remuneration Committee on 14 February 2018.

(2) Alison Deans was a member of the Board, Audit Committee, People and Remuneration Committee and Nomination Committee until 20 October 2017.

(3) Sheila McGregor was appointed to the Board, Audit Committee and Nomination Committee on 13 March 2018.

(4) Helen Nugent was a member of the People and Remuneration Committee until 13 February 2018. She was appointed to the Risk Committee on 14 February 2018.

(5) Michelle Tredenick was appointed to the Board, People and Remuneration Committee and Nomination Committee on 13 March 2018.

PRINCIPAL ACTIVITY

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

<table>
<tr><th>DIVISION</th><th>OVERVIEW</th><th>PRODUCTS</th></tr>
<tr><td>Consumer division (Australia)

54% of Group gross written premium (GWP)</td><td>Consumer insurance products are sold in Australia through branches, call centres, the internet and representatives, under the following brands:
■ NRMA Insurance in NSW, ACT, Queensland and Tasmania;
■ SGIO in Western Australia;
■ SGIC in South Australia;
■ RACV in Victoria, via a distribution agreement with RACV;
■ Coles Insurance nationally, via a distribution agreement with Coles; and
■ CGU through affinity and financial institution partnerships and broker and agent channels.

Consumer division also includes travel insurance, life insurance and income protection products which are underwritten by third parties.</td><td>Short-tail insurance
■ Motor vehicle
■ Home and contents
■ Lifestyle and leisure, such as boat, veteran and classic car and caravan

Long-tail insurance
■ Compulsory Third Party (motor injury liability)</td></tr>
<tr><td>Business division (Australia)

25% of Group GWP</td><td>Business insurance products are sold in Australia through a network of around 2,000 intermediaries, such as brokers, agents and financial institutions and directly through call centre and online channels. Business division is a leading provider of business and farm insurance in Australia.

Business division operates across Australia under the following brands:
■ CGU Insurance;
■ WFI;
■ NRMA Insurance;
■ RACV;
■ SGIO; and
■ SGIC.</td><td>Short-tail insurance
■ Business packages
■ Farm and crop
■ Commercial property
■ Construction and engineering
■ Commercial motor and fleet motor
■ Marine

Long-tail insurance
■ Workers' compensation
■ Professional indemnity
■ Directors' and officers'
■ Public and products liability</td></tr>
<tr><td>New Zealand

21% of Group GWP</td><td>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.</td><td>Short-tail insurance
■ Motor vehicle
■ Home and contents
■ Commercial property, motor and fleet motor
■ Construction and engineering
■ Niche, such as pleasure craft, boat, caravan and travel
■ Rural and horticultural
■ Marine

Long-tail insurance
■ Personal liability
■ Commercial liability</td></tr>
<tr><td>Corporate and other</td><td>Corporate and other comprises other activities, including corporate services, capital management activity, shareholders' funds investment activities, inward reinsurance from associates, and investment in associates in Malaysia and India.</td><td></td></tr>
</table>

OPERATING AND FINANCIAL REVIEW

OPERATING RESULT FOR THE FINANCIAL YEAR

IAG delivered an improved reported insurance margin, of 18.3%, which slightly exceeded updated guidance of 16-18%. This was driven by a favourable net natural peril claim cost outcome, which was over $80 million below allowance, and higher than anticipated prior period reserve releases, which equated to 4% of net earned premium (NEP). IAG's underlying insurance margin increased to 14.1% (2017: 12.4%). Approximately 125 basis points (bps) of this improvement attached to the inception of the combined 12.5% quota share agreements, from 1 January 2018. The balance was derived from pricing and operational actions, translating to improved loss and expense ratios.

GWP growth of 1.8% was in line with IAG's guidance of 'low single digit growth', with like-for-like growth exceeding 4% after allowance for ceased activities, NSW Compulsory Third Party (CTP) scheme reform impacts and foreign exchange translation effects. Underpinning this outcome were positive rate movements in short-tail lines, of both a personal and commercial nature. Overall volumes were relatively flat, with advances in CTP and New Zealand personal lines offset by shrinkage in commercial segments.

In February 2018, IAG announced a strategic review to assess the options available for its Asian businesses. As a result in June 2018, IAG disclosed the agreed sale of its interests in Thailand, Indonesia and Vietnam, which have been reclassified as discontinued operations for accounting purposes. Consequently, the after-tax earnings contribution from these operations has been aggregated in a single line item within the Statement of Comprehensive Income ('Loss after income tax from discontinued operations'). In addition, all related assets and liabilities are aggregated on either side of the balance sheet and captioned 'held for sale' at 30 June 2018. Options to divest IAG's investment in China continue to be pursued. The minority interests in joint ventures in Malaysia and India continue to be held. The announced Asian divestments are expected to realise a net profit after tax of at least $200 million, after allowance for related costs and foreign currency translation reserve effects, which will be recognised in the 2019 financial year. The vast majority of indicated proceeds of over $525 million relate to the sale of the business in Thailand, which is expected to settle by 31 August 2018.

At 30 June 2018, IAG had a Prescribed Capital Amount (PCA) multiple of 2.03 compared to its targeted benchmark of 1.4 to 1.6, and a Common Equity Tier 1 (CET1) multiple of 1.26 compared to its targeted benchmark of 0.9 to 1.1. In acknowledgement of IAG's surplus capital position to its targeted benchmarks, the absence of significant operational demands on its capital and the anticipated completion of the sale of the Thailand business by the end of August 2018, IAG has announced a $592 million capital management initiative of 25.0 cents per ordinary share which is expected to occur on or around 26 November 2018. This is expected to comprise a capital return of 19.5 cents, a fully franked special dividend of 5.5 cents and a share consolidation which would reduce ordinary shares on issue by approximately 2.4% and preserve consistency of earnings per share (EPS) calculation. The capital return and share consolidation components are subject to shareholder approval, which is being sought at IAG's Annual General Meeting (AGM) on 26 October 2018. IAG has made payment of the special dividend conditional on that approval being obtained.

Net profit after tax

The Group's profit after tax for the year was $1,001 million (2017: $1,005 million). After adjusting for non-controlling interests in the Group result, net profit attributable to the shareholders of the Company was $923 million (2017: $929 million), similar to the prior year. This outcome included:

- a near-11% increase in insurance profit to $1,407 million, from the combination of improved underlying profitability, lower reserve releases and a markedly more favourable net natural peril claims cost;
- a greater than $80 million contraction in contribution from investment income on shareholders' funds, including the effect of lower equity market returns;
- a higher effective tax rate of 27.2% (2017: 24.4%); and
- a $34 million increase in amortisation and impairment expense, after the recognition of a write-down on certain Asian assets in the first half.

Gross written premium

GWP in the current financial year increased 1.8% to $11,647 million. Like-for-like growth exceeded 4%, after allowing for:

- rate reductions and premium refunds stemming from NSW CTP scheme reform, which lowered reported GWP by approximately $190 million;
- a greater than $40 million reduction in GWP as a result of the decisions to exit motor dealership and motorcycle activities of Swann Insurance in Australia; and
- an adverse foreign exchange movement in respect of New Zealand, which reduced reported GWP by over $60 million compared to the prior year.

Whilst a factor in the first half, the reintroduction of the Emergency Services Levy (ESL) in NSW had a negligible impact on GWP for the full year.

Underlying GWP growth in the year was of the order of $500 million, across Australia and New Zealand, driven by:

- mid-single-digit rate increases in short-tail motor and home; and
- higher average rates in short-tail commercial lines, offset by some volume loss.

Insurance margin

IAG's current year reported insurance profit of $1,407 million (2017: $1,270 million) was 10.8% higher than the prior year. The reported insurance margin increased to 18.3% (2017: 15.5%). The higher reported insurance margin included:

- an improved underlying business performance;
- a favourable natural peril experience which saw related net claim costs of $541 million (2017: $816 million), which was over $80 million below allowance;
- lower net prior period reserve releases of $305 million (2017: $456 million), which represented 4.0% of NEP and compared to prior guidance of around 3%; and
- a similarly favourable credit spread impact of $14 million (2017: $20 million).

Underlying margin

IAG's underlying insurance margin increased to 14.1% (2017: 12.4%), and included approximately 125bps of improvement arising from the 12.5% quota share agreements which commenced on 1 January 2018. The improvement in underlying margin also included:

- rate-driven growth in earned premium in short-tail personal and commercial classes in both Australia and New Zealand;
- related alleviation of claim cost pressures, notably in short-tail motor, as rate increases at least matched increases in average claim costs;
- some respite from lower large loss experience in Australian commercial property;
- improved NSW CTP profitability following initial reform measures; and
- the absorption of approximately $10 million of Royal Commission related costs in the second half of the year.

IAG defines its underlying margin as the 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.

	2018		2017*	
INSURANCE MARGIN	**$m**	**%**	$m	%
Reported insurance margin*	**1,407**	**18.3**	1,270	15.5
Net natural peril claim costs (below)/in excess of allowance	**(84)**	**(1.1)**	138	1.7
Reserve releases in excess of 1% of NEP	**(228)**	**(3.0)**	(374)	(4.6)
Credit spread movements	**(14)**	**(0.1)**	(20)	(0.2)
Underlying insurance margin	**1,081**	**14.1**	1,014	12.4

* Reported insurance margin is the insurance profit/(loss) as a percentage of NEP as disclosed in the Statement of Comprehensive Income. Prior year comparatives have been re-presented due to the discontinued operations.

Tax expense

IAG reported a tax expense of $384 million (2017: $328 million), representing an effective tax rate of 27.2% (2017: 24.4%).

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.

Investment income on shareholders' funds

Net investment income on shareholders' funds was a profit of $165 million, a reduction of 33% compared to the profit of $246 million in the prior year. This included more modest equity market returns compared to the prior year, particularly in the second half of the year.

At 30 June 2018, the weighting to defensive assets (fixed interest and cash) within shareholders' funds was 57%, compared to 47% at the end of the first half of the year. Increased funds in the second half, including those derived from the $350 million subordinated note issue in March 2018, were directed towards fixed interest and cash, alongside some reduction in equity exposures.

DIVISIONAL HIGHLIGHTS

A. AUSTRALIA

Australia accounted for 79% of Group GWP with an improved reported insurance margin of 19.6% (2017: 17.5%) and a sound underlying margin of 12.9% (2017: 11.5%).

I. Premiums

Australia reported slightly higher GWP of $9,144 million (2017: $9,081 million). Like-for-like growth was over 3% after allowance for impacts from discontinued business areas and the influence of NSW CTP reform. The overall Australian GWP outcome includes:

- solid rate-driven growth of over 5% in short-tail motor, largely in response to claims inflation pressures;
- home GWP growth of over 4%, as an adverse ESL effect in the first half fully unwound in the second half of the year;
- ongoing average rate momentum of approximately 5% in commercial lines, as targeted increases were applied in most classes;
- approximately $40 million reduction in GWP from exiting the Swann Insurance motor dealership and motorcycle activities; and
- significantly lower NSW CTP GWP, with scheme reform-related reductions and premium refunds amounting to over $190 million.

Consumer division

IAG is the largest personal lines insurer in Australia, offering short-tail motor and home products across the country under a range of brands, as well as long-tail CTP offerings in NSW, the ACT and South Australia. The Australian Consumer division accounted for 54% of Group GWP and produced a strong underlying insurance margin of 15.5% (2017: 13.9%).

Consumer GWP increased by 1.6% to $6,214 million (2017: $6,119 million). Excluding the effect of NSW CTP-related changes, like-for-like Consumer GWP growth was over 4%.

Short-tail personal lines GWP represented 87% of Consumer GWP, with 97% of this derived from motor and home classes. Compared to the prior year, overall short-tail GWP growth of 4.4% was predominantly rate-driven.

Long-tail (CTP) GWP decreased by over 14%, compared to the prior year, largely owing to rate reductions and refunds associated with NSW scheme reform. Changes to legal cost regulations enacted in late calendar 2016 resulted in lower claim frequency under the old NSW scheme, warranting average rate reductions of 4% in July 2017 and a further 4% in September 2017. Broader reforms to the NSW scheme took effect from 1 December 2017. Changes in scheme design, including defined benefits for low severity injuries and access to common law for only the most seriously injured, are expected to reduce future claim costs. In response, IAG reduced its average NSW CTP premiums by an additional 22% from 1 December 2017.

Business division

IAG sells a range of commercial insurance products across Australia. The Australian Business division accounted for 25% of Group GWP and produced an underlying insurance margin of 7.8% (2017: 6.9%).

Business GWP declined by 1.1% to $2,930 million (2017: $2,962 million). Like-for-like Business GWP was marginally higher, after allowance for discontinued Swann Insurance activities.

The overall Business GWP outcome included:
- a continuation of rate increases across most business classes;
- remediation of the property and fleet portfolios;
- underwriting agency-derived growth, primarily from NTI;
- retention levels in key portfolios which were slightly lower than last year, however higher than expected;
- lower new business volumes; and
- an approximately $40 million reduction from divested or discontinued Swann Insurance activities.

II. Insurance profit

Australia reported an insurance profit of $1,190 million, compared to $1,145 million in the prior year. This equates to a higher reported insurance margin of 19.6% (2017: 17.5%), which includes the net effect of:
- an initial impact from the combined 12.5% quota share agreements which took effect from 1 January 2018, adding approximately 125bps to the current year margin and 250bps to that for the second half;
- lower prior period reserve releases;
- lower net natural peril claim costs; and
- a slightly lower favourable credit spread impact of $14 million.

III. Underlying margin

Australia's underlying performance was sound, with an underlying margin of 12.9%. Excluding the effect of the new combined 12.5% quota shares (approximately 125bps), this was slightly above the prior year. Contributory factors were:
- reduced pressure on motor profitability from higher claim costs, as increased rates earned through;
- increased flow-through impact of average rate increases across commercial portfolios;
- lower large loss levels in the commercial property portfolio, notably in the first half; and
- improved current year profitability in NSW CTP, reflecting lower average claim size and frequency.

IV. Fee-based business

The principal source of fee income for the Business division is its role as agent under both the NSW and Victorian workers' compensation schemes, which are underwritten by the respective state governments. In March 2017, IAG decided to withdraw from the NSW scheme by 31 December 2017 after assessment of associated risks and returns. As part of the withdrawal, anticipated redundancy costs associated with the exit were fully provided for in the prior year.

Total net income from fee-based operations in the current year was a reduced loss of $5 million, compared to $28 million in the prior year. The improved outcome contained:
- an absence of restructuring costs associated with the withdrawal from NSW, which amounted to $13 million in the prior year;
- a $4 million increase in prior period fee income for the Victorian scheme, to $9 million, largely recognised in the first half;
- an improvement in the Victorian business with a higher return from incentive fees combined with lower operating expenses; and
- increased fee income from NSW, as negotiated under the revised 2017 calendar year remuneration model and recognised in the first half.

A secondary source of fee income is the division's interest in authorised representative brokers.

B. NEW ZEALAND

New Zealand accounted for 21% of Group GWP with a higher reported insurance margin of 13.8% (2017: 7.6%) and a higher underlying insurance margin of 17.6% (2017: 14.8%).

I. Premiums

New Zealand's current year GWP grew by 6.3% to $2,486 million, compared to prior year GWP of $2,339 million. This increase includes an adverse foreign exchange translation effect, with local currency GWP increasing by 8.9%, to NZ$2,696 million (2017: NZ$2,475 million). This result was driven by the combination of:

- continued GWP growth in the Consumer division, led by the private motor vehicle portfolio on higher volumes and increased rates; and
- strong GWP growth in the Business division, as rate increases were attained in both commercial and personal lines, partially offset by lower new business volumes as the business continues to adhere to its strong underwriting disciplines.

II. Insurance profit

The New Zealand business produced a 74% increase in insurance profit to $218 million (2017: $125 million). This equates to a reported insurance margin of 13.8% (2017: 7.6%), with the improvement reflecting the combination of:

- an initial impact from the combined 12.5% quota share agreements which took effect from 1 January 2018, adding approximately 125bps to the current year margin and 250bps to that for the second half;
- higher gross earned premium, driven by good growth in both the Consumer and Business divisions;
- lower net natural peril claim costs, despite significant peril activity in the second half and an overrun against the full year allowance;
- continued focus on disciplined expense management; and
- some offset from prior period reserve strengthening.

Net prior period reserve strengthening of $39 million was recognised in the current year. This primarily relates to:

- potential claims under architect/engineer professional indemnity policies relating to residual risk (e.g. negligence) from post-earthquake building damage and rebuild activity, as recognised in the first half;
- adverse development of prior year storm events; and
- a favourable review of long-tail reserve assumptions in the second half.

III. Canterbury Rebuild

The settlement of claims associated with the financial year 2011 Canterbury earthquake events continues to make sound progress. At 30 June 2018:

- over NZ$6.7 billion of claim settlements had been completed;
- over 98% of all claims by number had been fully settled;
- close to 99% of commercial claims had been fully settled; and
- over 98% of residential claims had been settled, with the balance either in construction or negotiation for cash settlement.

During the first half of the year, IAG increased its gross reserved position on the three major earthquakes in financial year 2011, with no further movement in the second half. This falls to the account of IAG's reinsurers, with no earnings impact to IAG. Following this increase in earthquake reserves, IAG had utilised approximately 10% of the NZ$600 million adverse development cover in excess of NZ$4.4 billion on the February 2011 event.

C. CORPORATE AND OTHER

A pre-tax profit of $5 million was reported, which compares to a profit of $102 million in the prior year. The movement primarily reflects the reduction in net investment income on shareholders' funds of $81 million in the current year. This outcome also includes a portion of the write-down of Asian assets recognised in the first half of the 2018 financial year, reflecting updated assumptions and forecasts in relation to the current operating landscape. Following the classification of IAG's consolidated businesses in Thailand, Vietnam and Indonesia as discontinued operations, the interests in Malaysia and India which continue to be treated as associates have been reclassified to the Corporate and other segment. Further details on the operating segments are set out in Note 1.3 within the financial statements.

I. Share of net profit/(loss) of associates

The Group's share of associates was a profit of $31 million (2017: $19 million) including allocated regional development costs. This result includes AmGeneral Holdings Berhad (AmGeneral) in Malaysia and SBI General Insurance Company Limited (SBI General) in India.

IAG's share of AmGeneral's profit for the current year increased to $40 million (2017: $28 million). The outcome comprised the net effect of:

- effective pricing actions and portfolio management;
- higher bodily injury-related prior period reserve releases; partially offset by
- reduced net earned premium from lower average premiums and motor volumes; and
- increased marketing expenses.

IAG's share of SBI General's profit for the current year decreased to $10 million (2017: $14 million). This included an unfavourable mark-to-market movement in shareholders' funds income. IAG's share of SBI General's reported insurance profit of $9 million (2017: $8 million) comprised the net effect of:

- a relatively benign monsoon season in the current year, reducing seasonal losses;
- a favourable one-off effect from the finalisation of a reinsurance treaty for the long-term home portfolio, as recognised in the first half;
- an improved expense ratio from the benefit of increased scale; and
- lower investment income due to unfavourable mark-to-market movements.

REVIEW OF FINANCIAL CONDITION

A. FINANCIAL POSITION

The total assets of the Group as at 30 June 2018 were $29,766 million, compared to $29,597 million as at 30 June 2017. Movements within the overall net increase in assets of $169 million include:

- reclassification of $655 million of assets to those held for sale and associated with the discontinued Asian operations;
- an increase in deferred insurance expenses of $673 million predominantly related to the recognition of the combined 12.5% quota share agreements from 1 January 2018, partially offset by a $111 million reclassification to assets held for sale;
- an increase of $164 million of reinsurance and other recoveries on outstanding claims primarily relating to recoveries on the Group's whole-of-account quota share agreements, partially offset by recoveries received on prior period events;
- a decrease in investments of $1,129 million relating to the funds outflow associated with the payments of the 2017 final dividend and 2018 interim dividend, net settlements of the whole-of-account quota share arrangements, and a reclassification of $282 million to assets held for sale, partially offset by proceeds from the issuance of $350 million subordinated convertible term notes; and
- a decrease of $149 million in goodwill and intangible assets, which includes $65 million reclassified to assets held for sale, the sale of the retail warranty business and foreign exchange movements.

The total liabilities of the Group as at 30 June 2018 were $22,825 million, compared to $22,805 million as at 30 June 2017. Movements within the overall net increase in liabilities of $20 million include:

- recognition of $444 million of liabilities as those held for sale associated with our discontinued Asian operations;
- an increase in interest-bearing liabilities of $336 million reflecting the issuance of $350 million subordinated convertible term notes;
- an increase in other liabilities of $188 million predominantly related to the recognition of deferred reinsurance commissions associated with the combined 12.5% quota share agreements;
- a $158 million increase in trade and other payables primarily related to the recognition of net sums payable to counterparties to the 12.5% quota share agreements and partially offset by lower unsettled investment trades at the year end; and
- a decrease in the gross outstanding claims liability of $961 million primarily due to reduction in long-tail reserves driven by prior year reserve releases and payments, settlement of prior period natural peril claims, including the Canterbury earthquakes, and a reclassification of $157 million of reserves to liabilities held for sale.

IAG shareholders' equity (excluding non-controlling interests) increased from $6,562 million to $6,669 million as at 30 June 2018, reflecting the combined effect of:

- a sound earnings performance in the current year resulting in a net profit attributable to shareholders of $923 million; and
- payment of 2017 final and 2018 interim dividends, totalling $803 million.

B. CASH FROM OPERATIONS

The net cash outflows from operating activities for the year ended 30 June 2018 were $53 million compared to net cash inflows of $636 million for the prior year. The movement is mainly attributable to the net effect of:

- an increase in outwards reinsurance premium expense paid of $687 million, predominantly related to the inception of payments on the combined 12.5% quota share agreements;
- an increase in income taxes paid of $242 million predominantly driven by a higher final tax liability for the 2017 financial year paid in the current year, combined with higher monthly instalment rates for the current year; and
- an increase in other operating receipts of $236 million, predominantly driven by reinsurance commissions received in respect of the combined 12.5% quota share agreements.

C. INVESTMENTS

The Group's investments totalled $11.0 billion as at 30 June 2018, excluding investments held in joint ventures and associates, with nearly 58% represented by the technical reserves portfolio. The decrease in total investments since 30 June 2017 ($12.1 billion) reflects the combined effect of:

- a reduction in technical reserves, in response to further quota share and prior period reserve release effects; and
- an increase in shareholders' funds, including $350 million of inflow from the subordinated note issue in March 2018 and operating earnings in excess of dividend payments.

IAG's overall investment allocation is conservatively positioned, with 82% of total investments in fixed interest and cash as at 30 June 2018. Technical reserves are 100% invested in fixed interest and cash, while shareholders' funds comprise a mix of growth asset categories and fixed interest and cash. IAG's allocation to growth assets in shareholders' funds was approximately 43% at 30 June 2018, and is consistent with IAG's investment strategy target range.

D. INTEREST-BEARING LIABILITIES

IAG's interest-bearing liabilities stood at $1,960 million at 30 June 2018, compared to $1,624 million at 30 June 2017. The net increase reflects the issue in March 2018 of $350 million of subordinated notes which qualify as Tier 2 Capital.

E. CAPITAL MIX

IAG 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 remains 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 2018, IAG's capital mix was close to the mid-point of targeted ranges. Debt and hybrids represented 34.3% of total tangible capitalisation, with the increase since the first half reflecting the issue of $350 million of subordinated notes referenced above.

F. CAPITAL MANAGEMENT
IAG remains strongly capitalised under the Australian Prudential Regulatory Authority's (APRA) Prudential Standards, with regulatory capital of $5,018 million at 30 June 2018 (2017: $4,526 million). IAG 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 2018, IAG had a PCA multiple of 2.03 (2017: 1.70) and a CET1 multiple of 1.26 (2017: 1.09).

Further capital management details are set out in Note 3.1 within the financial statements.

STRATEGY AND RISK MANAGEMENT
A. STRATEGY

At IAG, our purpose is to make your world a safer place: IAG's purpose means that whether you are a customer, partner, employee, shareholder or part of the communities IAG serves, 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.

IAG's strategy is to optimise its core insurance business while creating future growth options.

Financial targets
IAG is focused on delivering through-the-cycle targets of:

- cash return on equity (ROE) 1.5x weighted average cost of capital (WACC);
- a dividend payout of 60-80% of cash earnings;
- top quartile total shareholder return (TSR); and
- approximately 10% compound earnings per share (EPS) growth.

Strategic priorities
IAG has identified three key strategic priorities, supported by organisational capabilities, to deliver its strategy:

I. Customer – world-leading customer experiences:
- Create a delivery platform that transforms customer experiences;
- Better connect customers and automate processes, enabling IAG to reach more customers in a timely manner;
- Develop an innovation approach which provides the ability to think differently and deliver quickly;
- Embed cognitive capabilities and artificial intelligence that anticipate customers' needs; and
- Use data to power decision-making, allowing IAG to better understand its customers.

II. Simplification – simplified, modular and lower cost operating model:
- Reduce organisational complexity by consolidating technology platforms, harmonising products, simplifying processes and systems, and executing the technology strategy;
- Leverage operational partners to optimise the operating model and drive scale economies across the value chain; and
- Improve allocation and maximise utilisation of the preferred repairer network to reduce average claim size.

III. Agility – an agile organisation distinguished by innovation, speed and execution skills:
- Create a disciplined approach to IAG's management and leadership, including building stronger role clarity and introducing agile ways of working;
- Build a talent pipeline based on the skills required to deliver IAG's strategy and help IAG people transition to the future of work; and
- Be recognised as a purpose-led organisation that shapes its internal and external environment.

B. BUSINESS RISK AND RISK MANAGEMENT

IAG acknowledges that it has to take risk in an informed manner in pursuit of its strategic objectives and to meet industry and stakeholder expectations. This means that IAG needs to manage its baseline compliance obligations and beyond that, take risk in a manner that is aligned with customer, shareholder, industry, regulatory and other key stakeholder expectations.

IAG uses an enterprise approach to risk and its risk management framework is a core part of the governance structure, which includes internal policies, key management processes and culture. The Group 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 Chief Risk Office function provides regular reports to the RC on the operation of and any changes to IAG's risk management framework, the status of key risks, risk and compliance incidents, risk trends and IAG's risk profile. 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 Nomination Committee, are set out in the Corporate Governance section of the IAG website.

IAG is exposed to multiple risks relating to the conduct of its general insurance business. The risks noted below are not meant to represent an exhaustive list, but outline those risks faced by IAG that have been identified in IAG's RMS:
- strategic risk – the risk of not achieving corporate or strategic goals due to poor business decisions regarding future business plans and strategies and/or a lack of responsiveness to changes in the business environment;
- insurance risk – the risk that IAG 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 unforeseen, unknown or unintended liabilities that may eventuate, inadequate or inappropriate claims management, and insurance concentration risk (e.g. by locality, segment, or distribution channel);
- reinsurance risk – the risk of insufficient or inappropriate reinsurance coverage, inadequate underwriting and/or pricing of reinsurance exposures retained, inadequate or inappropriate reinsurance recovery management, reinsurance arrangements not being legally binding, reinsurance concentration risk and credit counterparty concentration risk to reinsurers;
- financial risk – the risk of adverse movements in market prices (foreign exchange, equities, credit spreads, interest rates, etc) or inappropriate concentration within the investment funds, a counterparty failing to meet its obligations (credit risk), inadequate liquidity and inappropriate capital management;
- operational risk – the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events; and
- regulatory risk and compliance – the failure or inability to comply with applicable laws, regulations or codes excluding failure of staff to adhere to internal policies/procedures and meeting contractual obligations.

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 IAG's overall risk management framework, which is outlined in the RMS, is set out in Note 3.1 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

Economic, environmental and social sustainability risks are identified and managed as part of IAG's risk management framework, as overseen by the Board. Through risk profiling and ongoing trend analysis, information on these risks is collected and reported to the Group Leadership Team (GLT) and Board, and used to update IAG's strategy at appropriate intervals. This is supported by IAG's annual materiality process and engagement with IAG's Shared Value Advisory Council to identify and develop mitigation approaches to these risks.

As a general insurer, IAG is exposed to economic, environmental and social sustainability risks and opportunities. The IAG Board has overarching responsibility for these areas, which are managed by the business and supported by IAG's shared value and sustainability subject matter experts. Performance and risk management is formally reported to the Board annually, with ad hoc updates as required.

The Consumer Advisory Board and Ethics Committee provide external stakeholder input into the understanding of economic, environmental and social sustainability risk. The Shared Value Advisory Council is an internal governance body that acts as a forum to make decisions on how the Company responds through its approach to shared value, sustainability and broader community activity. Established in 2014, the Shared Value Advisory Council fulfils the role of a sustainability committee for IAG. It meets at least quarterly, 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.

Annually IAG undertakes a materiality assessment to help guide IAG's shared value and sustainability approach and ensure its reporting addresses risks and opportunities that matter most to IAG's stakeholders and business. The Shared Value Advisory Council plays an active role in the finalisation of the material issues, which are signed off by the Group Executive, People, Performance and Reputation.

IAG 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 IAG's commitment to help make communities Safer, Stronger and More Confident. IAG's sustainability performance is managed within this framework and supported by a number of policies and position statements including IAG's Social & Environmental Policy and Public Policy Position on Climate Change.

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

Detail of IAG's material issues, how IAG manages related risks and opportunities and details of other shared value and sustainability activities can be found in the 2018 Annual Review and Safer Communities Report, which is available at www.iag.com.au/shared-value/our-performance. IAG's management of Economic, Environmental and Social Sustainability Risk is outlined in detail in Principle 7.4 of the Corporate Governance Statement, which is available at www.iag.com.au/about-us/corporate-governance.

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.

IAG's Corporate Governance Statement has been approved by the Board. Throughout the financial year ended 30 June 2018, IAG has complied with the Australian Securities Exchange Corporate Governance Council Principles and Recommendations (3rd edition) and is compliant as at 15 August 2018. 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 expects to report further improvement in its underlying performance in financial year 2019. IAG's GWP guidance is growth of 2-4%. This is expected to be derived from:

- further rate increases across short-tail personal and commercial classes;
- modest volume increases in personal lines categories, notably motor; and
- a slight decline in commercial volumes, including those from further remediation activity.

Higher underlying GWP growth is anticipated, after allowance for residual NSW CTP scheme reform effects (approximately $80 million) and ceased or exited business activities (approximately $40 million) including retail warranty and consumer credit.

IAG's financial year 2019 reported insurance margin guidance is a range of 16.0-18.0%. Underlying assumptions are:

- a net improvement in pre-tax profit of approximately $100 million from optimisation program initiatives;
- net losses from natural perils in line with an allowance of $608 million (increased to $900 million, pre-quota share);
- prior period reserve releases of around 2% of NEP; and
- no material movement in foreign exchange rates or investment markets.

The reported insurance margin guidance also incorporates a further uplift of approximately 125bps from a full year's effect of the combined 12.5% quota share agreements which commenced on 1 January 2018.

Excluding the factors outlined above, IAG's overall underlying performance in financial year 2019 is expected to reflect:

- steady profitability in short-tail personal lines within Australia Consumer;
- a lower contribution from long-tail CTP in Australia Consumer stemming from changed scheme design in NSW which came into force on 1 December 2017;
- an improved Australia Business margin, from ongoing momentum in average commercial line rates;
- the maintenance of strong profitability in New Zealand; and
- a higher non-quota share reinsurance expense as a result of:
  - increased protection from the 2019 financial year stop loss cover which extends directly from the 2019 financial year natural perils allowance; and
  - increased renewal costs attached to commercial line per risk excess of loss cover, reflecting recent high large loss experience.

While IAG expects prior period reserve releases of around 2% of NEP in financial year 2019, it remains the Group's belief that long-term reserve releases of around 1% of NEP are a recurring feature of its reported operating results in benign inflationary periods.

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 Note 4.4.

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

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

CASH EARNINGS	**2018 $m**	2017 $m
Net profit after tax	**923**	929
Acquired intangible amortisation and impairment (post-tax)	**107**	59
	1,030	988
Non-recurring items:		
Corporate expenses	**9**	8
Tax effect on corporate expenses	**(5)**	(6)
Cash earnings*	**1,034**	990
Interim dividend	**331**	307
Final dividend	**474**	474
Dividend payable	**805**	781
Cash payout ratio*	**77.9%**	78.9%

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

The Board has determined to pay a final fully franked dividend of 20.0 cents per ordinary share (cps) (2017: 20.0cps). This brings the full year dividend to 34.0 cents per share (2017: 33.0cps), an increase of 3%. The final dividend is payable on 27 September 2018 to shareholders registered as at 5pm Australian Eastern Standard Time (AEST) on 22 August 2018.

The full year dividend equates to a payout ratio of 77.9% of cash earnings, and is in accordance with IAG's dividend policy to pay out 60-80% of cash earnings in any financial year.

As at 30 June 2018, and after allowance for payment of the final dividend, IAG's franking balance was $100 million, giving it the capacity to fully frank a further $234 million of distributions. IAG's franking balance includes its 70% entitlement to franking held by IMA, which at 30 June 2018 amounted to $164 million.

IAG's franking credit balance has reduced in recent years, owing to past capital management measures and the move to a higher dividend payout policy. Following the special dividend component of the initiative planned to occur in November 2018, it is anticipated that IAG's franking balance will further reduce. As a result, IAG may not be in a position to fully frank distributions on its securities from the second half of calendar 2019 onwards, with franking from that date expected to be in the range of 70% to 100%.

The dividend reinvestment plan (DRP) will operate for the final dividend for shareholders registered for the DRP as at 5pm on 23 August 2018. The issue price per share for the final dividend will be the Average Market Price as defined in the DRP terms, and there will be no discount for participants. Shares allocated under the DRP will be purchased on-market. Information about IAG's DRP is available at: http://www.iag.com.au/shareholder-centre/dividends/reinvestment.

SIGNIFICANT CHANGES IN STATE OF AFFAIRS

During the financial year the following changes became effective:

- On 19 July 2017, IAG announced the creation of a single Australian division led by Mark Milliner as CEO Australia. The Australian division simplifies IAG's operating model by bringing together the former Australian Consumer, Australian Business, Operations and Satellite divisions. There has been no change to the reportable segments in the current reporting period as financial information was prepared and reviewed by the chief operating decision maker based on the pre-existing segment structure for Australia.
- On 1 August 2017, IAG consolidated its nine Australian insurance licences into two licences following Federal Court approval received in July 2017. The consolidation transferred the insurance assets and liabilities of seven entities into a related entity, Insurance Australia Limited, with no impact to IAG's consolidated financial performance or position. Following the transfer, IAG retains two authorised insurers in Australia being Insurance Australia Limited and Insurance Manufacturers of Australia Pty Limited. The transfer is part of IAG's focus on becoming a simpler, more efficient and agile business.
- On 8 December 2017, IAG announced it had entered into three agreements to quota share a combined 12.5% of its consolidated business from 1 January 2018. The agreements, with Munich Re, Swiss Re and Hannover Re, are on a whole-of-account basis, covering IAG's consolidated business in Australia, New Zealand and Thailand and have an average initial period of more than five years. Expected benefits include reduced earnings volatility, reduced reliance on catastrophe reinsurance cover and exposure to future volatility in reinsurance rates, and reduced regulatory capital requirements.
- On 29 March 2018, the Company issued $350 million of subordinated convertible term notes. The subordinated notes qualify as Tier 2 Capital under APRA's Prudential Framework for General Insurance.
- On 19 June 2018, IAG announced it had entered into a sale agreement with Tokio Marine & Nichido Fire Insurance Co., Ltd (Tokio Marine) for IAG's operations in Thailand and Indonesia. Separate to the transactions with Tokio Marine, IAG has reached an agreement to sell its interest in AAA Assurance Corporation, based in Vietnam. All transactions are expected to conclude in the financial year ending 30 June 2019, subject to regulatory approvals or notifications. As a result of the sale agreements, the Asian businesses have been identified as discontinued operations in the current financial year and comparative figures have been re-presented accordingly. The interests in Malaysia and India continue to be treated as associates, but have been reclassified to Corporate and other within IAG's segment reporting.

EVENTS SUBSEQUENT TO REPORTING DATE

Details of matters subsequent to the end of the financial year are set out below and in Note 7.3 within the financial statements. These include:

- On 15 August 2018, the Board determined to pay a final dividend of 20.0 cents per share, 100% franked. The dividend will be paid on 27 September 2018. The DRP will operate by acquiring shares on-market for participants with no discount applied.
- On 15 August 2018, IAG announced a capital management initiative amounting to 25.0 cents per ordinary share, or $592 million, expected to comprise a 19.5 cents capital return and a 5.5 cents fully franked special dividend, with a share consolidation which would reduce IAG's ordinary issued shares by approximately 2.4% and preserve consistency of EPS calculation. The capital return and share consolidation are subject to shareholder approval at the AGM, and IAG has made payment of the special dividend conditional on approval being obtained. If approved, the capital management initiative is expected to occur on or around 26 November 2018.

NON-AUDIT SERVICES

During the financial year, KPMG performed certain other services for IAG 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 IAG'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 did 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 $2,741 thousand (refer to Note 8.3 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 40 and forms part of the Directors' Report for the year ended 30 June 2018.

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 is prohibited by the relevant contract of insurance.

REMUNERATION REPORT
EXECUTIVE SUMMARY

IAG's remuneration approach focuses Executives on generating strong financial outcomes for shareholders, while creating a world-leading experience for IAG's customers and fostering an agile culture among employees. In doing this, IAG seeks to reward Executives for short-term outperformance and for building long-term sustainable success.

The value IAG has created is reflected in the remuneration provided to Executives.

IAG rewards Executives for the value they help create through a combination of fixed pay, short-term incentives (STI) and long-term incentives (LTI). IAG delivered improved business performance on an underlying basis in the 2018 financial year. During the year, further steps were taken to reduce earnings volatility and regulatory capital requirements via greater use of reinsurance quota share capital. The announced sale of IAG assets in Thailand, Vietnam and Indonesia will result in a profit in the next financial year and, in tandem with quota share effects, is facilitating a considerable return of capital to shareholders.

The Board considers overall Group performance, together with an assessment of each Executive's personal performance, to determine individual STI outcomes. Reflecting IAG's strong performance during the year ended 30 June 2018, the Group Balanced Scorecard outcome was 74% of the maximum achievable. Consistent with this outcome, the average STI payment for Executives was 71% of the maximum achievable, with payments to individual Executives ranging from 50% to 84%.

Based on strong returns over the three-year period up to 30 June 2017, the cash Return on Equity (ROE) hurdle of the 2014/2015 LTI award vested in full. The Board reviewed the ROE vesting outcome to ensure it appropriately reflects the value created for shareholders. Consistent with the approach used when calculating cash ROE in previous tests, the cash earnings result was reduced by the value of the software impairments announced to the market on 19 August 2016.

On 30 September 2017, the relative Total Shareholder Return (TSR) hurdle of the 2013/2014 LTI award was tested. IAG's TSR was ranked at the 42nd percentile of the peer group and consequently this award did not vest. During the year, the TSR hurdle of the 2012/2013 LTI award was tested for the final time. IAG's TSR was ranked at the 69th percentile of its peer group, resulting in a final vesting outcome of 88%. Given that 56% of this award had vested previously, Executives received an additional 32% vesting during the year. This was the last LTI grant issued with a retesting provision and there will be no further retests of any LTI grant.

In determining variable pay outcomes for Executives, the Board considers IAG's risk culture and evaluates how well risks have been identified, assessed and mitigated. This process ensures remuneration practices encourage behaviour that supports sound risk management practices and IAG's long-term financial soundness. In order to inform the Board's assessment, the Group CEO provided the Board with his evaluation of IAG's risk management performance. In addition, the Board also separately received input from the acting Chief Risk Officer and the Chair of the Risk Committee. The Board's assessment of IAG's risk management performance was considered both in determining STI outcomes for the year, and also in determining whether there were any material risk events that warranted an adjustment to unvested awards of LTI or deferred STI. Based on the assessment undertaken by the Board, no adjustment for material risk failings was applied to the STI awards for the 2018 financial year, nor to the deferred STI or LTI awards granted to Executives in prior years that will vest by 1 September 2018. The Board will continue to consider risk-based adjustments when determining STI awards and when elements of deferred pay come due.

In the 2018 financial year, Craig Olsen, Chief Executive, New Zealand, was the only Executive to receive a fixed pay increase as part of the August 2017 review to meet market pay levels.

For the 2019 financial year, the Board has approved fixed pay increases for four Executives. Peter Harmer was appointed Group CEO in 2015. At this time, the Board determined that his fixed pay should be rebased downwards relative to the previous Group CEO. Reflecting this decision, his fixed pay was set at $1.7 million and was unchanged for the two subsequent financial years. For the August 2018 pay review, the Board has determined to increase his fixed pay from $1.7 million to $1.9 million to better reflect market pay levels and his performance in the role. During the August 2018 fixed pay review, the Board also determined to increase the fixed pay of Mark Milliner, Chief Executive Officer, Australia, to reflect a change in role and market relativities; and Craig Olsen, Chief Executive, New Zealand and Julie Batch, Chief Customer Officer to reflect market pay levels and performance in the role. These increases will be reflected in the Remuneration Report for the year ending 30 June 2019.

IAG considers the interests of Non-Executive Directors and Executives should be aligned with those of shareholders. To support this alignment, Non-Executive Directors and Executives are required to hold a significant number of IAG shares after a set period. Non-Executive Directors who had served at least three years, and Executives who had served at least four years as at 30 June 2018 were each assessed, and all met this requirement.

IAG continues to evolve its remuneration framework to focus the Executives on generating value for all of IAG's stakeholders.

Issues highlighted through the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, APRA's review of remuneration practices across regulated organisations, the 'Retail Banking Remuneration Review' (Sedgwick Report) and the Banking Executive Accountability Regime, have significant implications for the design and governance of remuneration frameworks. The Board is reviewing IAG's approach to executive remuneration to ensure it remains aligned to IAG's Purpose and strategy, while also reflecting broader community expectations. As part of this review, the following enhancements to IAG's remuneration approach were introduced for the year ended 30 June 2018:

- Applying a more rigorous process for considering risk when assessing performance;
- Formalising the role of the Chair of the Risk Committee and Chief Risk Officer in informing the Board's assessment of risk management performance;
- Reducing the variable component of the Chief Risk Officer's remuneration mix to further support the independence of this role; and
- Reviewing IAG's sales incentive plans with the aim of improving the customer outcomes and supporting IAG's Purpose.

In addition to the changes described above, the Board has determined that the following changes to IAG's remuneration approach will apply for the year ending 30 June 2019:

- The proportion of an Executive's STI award that is deferred will increase from one third to one half. This change will apply to any Executive STI awards made from September 2019; and
- The performance period for the cash ROE hurdle will be extended from three to four years.

The Board will continue to review the remuneration framework to ensure it is fit for purpose and further changes may be made in future years.

CONTENTS

A. KEY MANAGEMENT PERSONNEL COVERED IN THIS REPORT

This report sets out the remuneration details for IAG's key management personnel (KMP). Although the Non-Executive Directors are disclosed in the report, they do not have management responsibility. Therefore, their remuneration is dealt with separately.

The accounting standards define KMP to include Non-Executive Directors and executives who have ultimate accountability for planning, directing and controlling the activities of the organisation, either directly or indirectly.

Previously, IAG determined that all members of the Group Leadership Team were KMP. However, as a result of cumulative changes, including the changes to the Group Leadership Team structure announced to the market in July 2017, the Board considered it appropriate to reconsider the composition of IAG's KMP. Accordingly, following a comprehensive review, the Board determined that effective 1 July 2017, executive KMP (referred to in this report as Executives) will comprise the Group CEO and those of his or her direct reports who:

- manage a business unit; or
- have accountability for the risk or financial control of the organisation; or
- have accountability to deliver a strategic priority.

The Board considers that this application of the definition of KMP more accurately identifies those in the Group who have ultimate accountability for planning, directing and controlling IAG's activities.

Applying this definition, not all members of the Group Leadership Team are KMP. The following executives who appeared in the Remuneration Report for the year ended 30 June 2017 are no longer KMP:

- Chris Bertuch, Group General Counsel and Company Secretary;
- Duncan Brain, Chief Executive, Asia; and
- David Harrington, Group Executive Strategy and Corporate Development.

These executives will not appear in this Remuneration Report. The full list of KMP for the year ended 30 June 2018 is presented below.

NAME	POSITION	TERM AS KMP(1)
EXECUTIVES		
Peter Harmer	Managing Director and Chief Executive Officer	Full year
Julie Batch	Chief Customer Officer	Full year
Tim Clark	Acting Chief Risk Officer	From 27 February 2018
Nicholas Hawkins	Chief Financial Officer	Full year
Jacki Johnson	Group Executive, People, Performance and Reputation	Full year
Mark Milliner(2)	Chief Executive Officer, Australia	Full year
Craig Olsen	Chief Executive, New Zealand	Full year
EXECUTIVES WHO CEASED AS KMP		
Ben Bessell(2)	Chief Executive, Australian Business Division	Ceased 19 July 2017
Anthony Justice(2)	Chief Executive, Australian Consumer Division	Ceased 18 November 2017
Clayton Whipp(3)	Chief Risk Officer	Ceased 1 December 2017
NON-EXECUTIVE DIRECTORS		
Elizabeth Bryan	Chairman, Independent Non-Executive Director	Full year
Duncan Boyle	Independent Non-Executive Director	Full year
Hugh Fletcher	Independent Non-Executive Director	Full year
Sheila McGregor	Independent Non-Executive Director	From 13 March 2018
Jon Nicholson	Independent Non-Executive Director	Full year
Helen Nugent	Independent Non-Executive Director	Full year
Tom Pockett	Independent Non-Executive Director	Full year
Michelle Tredenick	Independent Non-Executive Director	From 13 March 2018
Philip Twyman	Independent Non-Executive Director	Full year
NON-EXECUTIVE DIRECTOR WHO CEASED AS KMP		
Alison Deans	Independent Non-Executive Director	Ceased 20 October 2017

(1) If an individual did not serve as a KMP for the full financial year, all remuneration is disclosed from the date the individual was appointed as a KMP to the date they ceased as a KMP.

(2) Following the implementation of the new IAG Australian operating model, effective 19 July 2017, Mark Milliner commenced in the role of Chief Executive Officer, Australia. From this date, Ben Bessell reported to Mr Milliner and no longer met the criteria of a KMP. Anthony Justice remained a KMP until he ceased employment with IAG.

(3) Clayton Whipp retired from IAG effective 1 December 2017.

Key terms that are used throughout the report are defined in detail in Appendix 5.

B. EXECUTIVE REMUNERATION STRUCTURE

I. Remuneration guiding principles

IAG's remuneration practices have been designed to achieve the following objectives:

- align remuneration with the interests of IAG's shareholders;
- support the best interests of IAG's customers;
- maintain market competitiveness to attract and retain high quality people; and
- encourage constructive, collaborative behaviours that support:
  - IAG's long-term financial soundness; and
  - IAG's risk management framework.

II. Summary of remuneration components

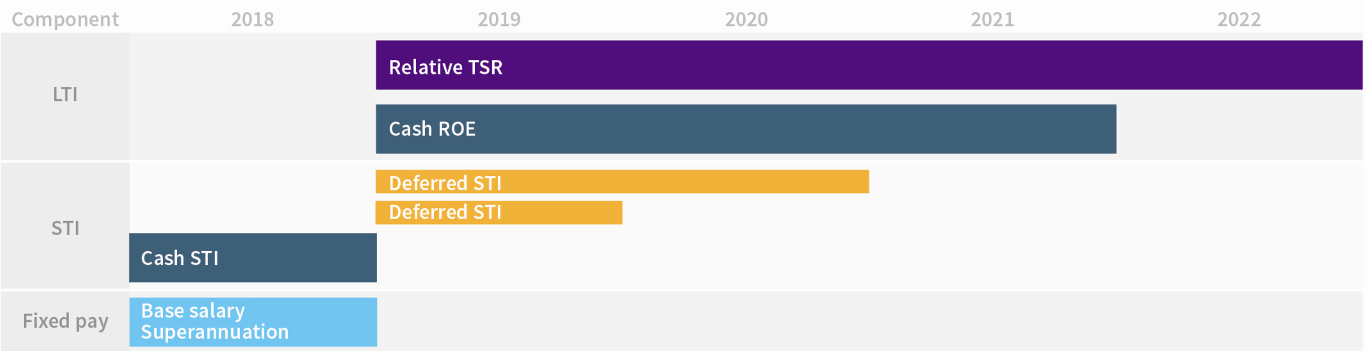
The Executive remuneration approach consists of the following components: fixed pay, cash STI, deferred STI and LTI. The table below describes the structure and purpose of each component for Executives during the year ended 30 June 2018.

TABLE 1 – REMUNERATION COMPONENTS

COMPONENT	STRUCTURE	PURPOSE
Fixed pay	Fixed pay comprises base salary and superannuation. Fixed pay for an Executive is determined by reference to the experience and skills an individual brings to the role, the internal relativities between Executives and market pay levels for similar external roles. Further details relating to fixed pay are presented in Table 2.	Fixed pay is provided to remunerate IAG employees for performing their ongoing work.
STI	STI is provided on an annual basis subject to the achievement of short-term goals agreed by the Board, outlined in the Group Balanced Scorecard. Two thirds of the total STI is delivered in cash in the remuneration review following the financial year end; and the remaining one third is deferred over the subsequent two years based on continued service. The deferred portion is subject to downward adjustment (also referred to as malus) if determined appropriate by the Board. Further details relating to the STI plan, including changes being introduced for the 2019 financial year, are presented in Table 3.	STI plays a key role in aligning superior operational outcomes for shareholders with remuneration outcomes for management. Deferral of incentives encourages ongoing employment of senior management and allows the Board to apply downward adjustment (malus) when appropriate. Share-based remuneration also reinforces the link between shareholder value creation and rewarding employees.
LTI	LTI rewards Executives for achieving long-term financial performance based on two hurdles: cash ROE over a three-year period and relative TSR over a four-year period. Further details relating to the LTI plan, including changes being introduced for the 2019 financial year, are presented in Table 4.	LTI creates a direct link between Executive reward and the return experienced by shareholders. LTI awards are subject to the two hurdles below: ■ cash ROE provides evidence of IAG's return on total shareholders' equity. The ROE hurdle utilises cash earnings, which is the measure used to determine the dividend paid to shareholders; and ■ relative TSR reflects the value created for shareholders through the movement of the share price and the value of dividends.

Remuneration received by Executives is based on IAG's performance over a number of different time periods, as illustrated in the following graph. The timeframe of potential payments to Executives is staggered progressively from one to four years to encourage decision-making which supports long-term, sustainable performance.

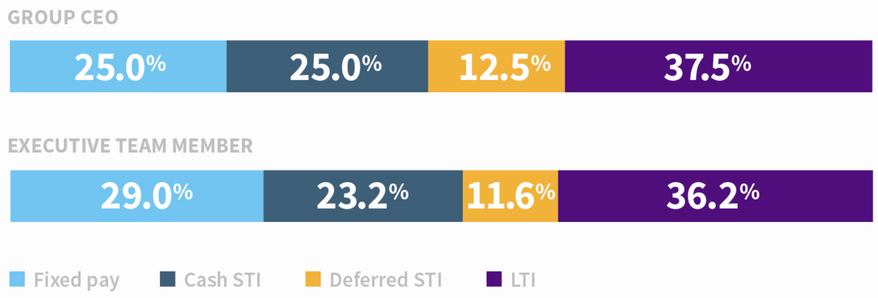
REMUNERATION COMPONENT TIMEFRAMES



III. Remuneration mix

The mix of remuneration components in IAG's remuneration framework is outlined in the following graph. This represents the structure based on the maximum potential earnings for the Group CEO and the ongoing members of the current Executive Team. The remuneration mix is current as at 30 June 2018.

REMUNERATION MIX BASED ON MAXIMUM INCENTIVE OPPORTUNITY



Each remuneration component is described in more detail below.

IV. Fixed pay

TABLE 2 – FIXED PAY

Overview	Fixed pay at IAG is set with reference to the median of the external market for comparable roles, with the flexibility to adjust based on the size and complexity of the role, and the skills and experience of the Executive. Fixed pay for Australian-based Executives is compared to the market using 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. Increases to an Executive's fixed pay are generally only provided in situations where either their pay is below market levels, or where there has been a material change in the responsibilities of their role. During the 2018 financial year, Craig Olsen was the only Executive to receive a fixed pay increase, to meet market pay levels.

V. Short-term incentive

TABLE 3 – STI AND DEFERRED STI

Behavioural gateway	All employees are required to demonstrate appropriate behaviours in the achievement of performance outcomes. The behavioural gateway only determines STI eligibility. Those who have not behaved in line with expected standards will not receive any STI in that year, regardless of their performance. If the behavioural gateway requirements are met, the size of the STI award is subsequently determined based on individual and company performance. For Executives, their behaviours during the year are assessed by the Group CEO who subsequently recommends to the Board whether they are eligible for an STI. For the Group CEO, an assessment of his or her behaviour is made by the Board.
STI opportunity	For the 2018 performance year, the maximum value of STI that could be granted to the Group CEO was 150% of fixed pay. The maximum value of STI for the Acting Chief Risk Officer was 80% of fixed pay, while for the other Executive Team members (Chief Executive Officer, Australia; Chief Executive, New Zealand; Chief Financial Officer; Chief Customer Officer; and Group Executive, People, Performance and Reputation) the maximum was 120% of fixed pay. For the 2019 performance year, the Board determined that the maximum value of STI that can be granted to the Chief Financial Officer and Chief Executive Officer, Australia will increase to 130% of fixed pay. The STI opportunities for all other Executives will remain unchanged.

Performance measures and evaluation	STI is the at-risk remuneration component designed to motivate and reward Executives for superior performance in the financial year. Performance is measured against the Group Balanced Scorecard using both financial and non-financial goals (the Group Balanced Scorecard is discussed in more detail in Table 5a). In determining STI awards, consideration is also given to the effectiveness of risk management during the year. The People and Remuneration Committee (PARC) reviews the Group CEO's performance based on Group Balanced Scorecard outcomes and the effectiveness of risk management during the year and recommends an STI award for approval by the Board. The STI awards for members of the Executive Team are recommended by the Group CEO to PARC based on an assessment of their contribution to Group Balanced Scorecard outcomes and the effectiveness of risk management during the year. These remuneration outcomes are subsequently recommended by PARC for approval by the Board. For all individuals, the Board may apply discretion in determining the STI outcomes to ensure they appropriately reflect performance.
Instrument	An Executive's STI award is comprised of a cash component and a deferred component. The cash component is two thirds of the total STI and is paid in September following the end of the performance year. The deferred component is one third of the total STI award, with half vesting after one year and the balance vesting after two years. The deferred component is typically paid in the form of Deferred Award Rights (DARs), unless it is not possible to do so, in which case cash equivalent payments are made according to the same vesting schedule. Effective the year ending 30 June 2019, the proportion of STI deferred will increase from one third to one half of the total STI awarded to an Executive.
Key terms of the deferred STI	DARs are rights over the Company's ordinary shares. DARs are granted at no cost to the Executives and IAG's policy is that no dividend is paid or payable for any unvested, or vested and unexercised, DARs. The Board has determined to make an exception to this approach for holders of DARs due to vest in 2018 and 2019 to ensure they are not disadvantaged as a result of the decision to bring forward the record date for final dividends. The record date to be eligible for final dividend payments has been brought forward to avoid a delay in distributing profits to shareholders. A consequence of the change in dates is that the DARs due to vest in 2018 and 2019 will no longer be eligible for the final dividend as the vesting dates will now be shortly after the relevant record dates. In recognition of this adverse consequence for DARs holders, the Board has determined to make a cash payment to employees who hold DARs at the 2018 and 2019 vesting dates, equivalent in value to the dividends they would have otherwise received had the record date not been moved. These payments will be disclosed in the 2019 and 2020 Remuneration Reports. The number of DARs issued is calculated based on the volume-weighted average share price (VWAP) of the Company's ordinary shares over the 30 days up to and including 30 June before the grant date. Executives who participate in the STI plan become eligible to receive one ordinary share of the Company per DAR by paying an exercise price of $1 per tranche of DARs exercised. Vesting of DARs is subject to an Executive's continuing employment with IAG at the vesting date, or meeting the conditions to retain unvested DARs upon cessation, as outlined in the 'Forfeiture Conditions' section below. Executives may not enter into transactions or arrangements which operate to limit the economic risk of unvested entitlements to IAG securities (termed hedging).
Forfeiture conditions	The Board retains the discretion to adjust downwards the unvested portion of any deferred STI awards, including to zero. DARs will be forfeited if the Executive resigns before the vesting date, except in special circumstances as outlined below. When an Executive ceases employment in special circumstances, any unvested rights may be retained on cessation of employment up to the point they vest, subject to Board discretion. Special circumstances include: redundancy, retirement, death or total and permanent disability. Any rights retained under these circumstances will remain subject to the original vesting period unless the Board determines an alternative vesting date, which would only be done in exceptional circumstances.

VI. Long-term incentive

TABLE 4 – LTI

Overview	LTI grants are determined annually by the Board. The grants are in the form of Executive Performance Rights (EPRs) that have performance hurdles which align to IAG's strategic financial targets.
LTI opportunity	For the 2018 performance year, the maximum value of LTI that could be granted to the Group CEO was 150% of fixed pay. The maximum value of LTI that could be granted to the acting Chief Risk Officer was 40% of fixed pay, while the maximum for other Executive Team members was 125% of fixed pay. For the 2019 performance year, the Board has determined that the maximum value of the LTI that can be granted to the Group CEO will increase to 165% of fixed pay, while the maximum value of LTI that can be granted to the Chief Financial Officer and Chief Executive Officer, Australia will be 140% of fixed pay. The maximum LTI opportunities for all other ongoing Executives will remain unchanged at 125%.
Instrument	If performance hurdles are achieved, rights can be settled with either the Company's ordinary shares or an equivalent cash payment. The Board may choose to exercise discretion to settle rights on vesting in cash in circumstances where it is restrictive to settle rights with shares, including in jurisdictions where legislative requirements prohibit share ownership in a foreign entity. Where rights are settled in cash, the value of the cash payment is determined based on the VWAP for the five trading days up to and including the vesting date. Rights granted prior to 1 July 2013 are only settled with the Company's ordinary shares.
Key terms of the LTI	The number of EPRs issued is calculated based on the VWAP over the 30 days up to and including 30 June before the grant date. EPRs granted during the year will not vest and have no value to the Executive unless the performance hurdles are achieved. The cash ROE performance hurdle is measured over three years, while the relative TSR hurdle is measured over four years. No dividend is paid or payable for any unvested, or vested and unexercised, EPRs. There are no opportunities to retest these performance hurdles. For awards made in the year ending 30 June 2019 onwards, the Board has approved an increase to the performance period of the ROE hurdle from three years to four years. Executives may not enter into transactions or arrangements which operate to limit the economic risk of unvested entitlements to IAG securities.
Forfeiture conditions	The Board retains the discretion to adjust downwards the unvested portion of any LTI awards, including to zero. Under the terms of the LTI, if an Executive resigns before the performance hurdles are tested, the unvested EPRs will generally lapse. In cases where the Executive acts fraudulently or dishonestly or is in breach of his or her obligations to IAG, the unvested EPRs will lapse. When an Executive ceases employment in special circumstances, any unvested rights may be retained on cessation of employment up to the point they vest, subject to Board discretion. Special circumstances include: redundancy, retirement, death or total and permanent disability. Any rights retained under these circumstances will remain subject to the original performance conditions.

PERFORMANCE HURDLES	CASH ROE	RELATIVE TSR
Description	50% weighting Cash ROE is measured relative to IAG's weighted average cost of capital (WACC).	50% weighting Relative TSR is measured against that of the top 50 industrial companies within the S&P/ASX 100 Index. Industrial companies are defined by Standard & Poor's as being all companies excluding those defined as being in the Energy sector (GICS Tier 1) and the Metals & Mining industry (GICS Tier 3). Companies which are no longer part of the index at the end of the performance period (e.g. due to acquisition or delisting), may be removed from the peer group.
Testing	The cash ROE portion of the LTI is tested from 1 July of the grant year to 30 June three years later. The cash ROE/WACC ratio is calculated for each half year. The average of the six half years in the three-year performance period is used to determine the final vesting outcome. For grants to be made in November 2018 onwards, the performance period for the cash ROE hurdle will increase from three to four years.	The relative TSR portion of the LTI is tested four years after 30 September of the grant year, with no opportunity for retesting. TSR performance is measured between 30 September of the base year, and 30 September of the test year. The opening and closing share prices used for the TSR calculation are both based on the three-month VWAP to 30 September. IAG removed retesting from LTI grants from July 2013 onwards. For LTI awards granted prior to July 2013, the TSR portion is tested after three years and then again at four years and five years. The final retest of these legacy awards occurred in the year ended 30 June 2018 and there will be no further retesting of any LTI awards in future years.
Vesting	0% vesting <1.2 x WACC 20% vesting at 1.2 x WACC 100% vesting at 1.6 x WACC with straight-line vesting in between.	0% vesting if <50th percentile of peer group 50% vesting if aligned to 50th percentile of peer group 100% vesting if aligned to 75th percentile of peer group with straight-line vesting in between.

C. LINKING IAG'S PERFORMANCE AND REWARD

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

IAG's strategy focuses Executives to achieve a successful, sustainable company that can deliver on IAG's Purpose of 'making your world a safer place'. The initiatives that enable IAG to deliver on these objectives are grouped under three broad strategic priorities: 'customer', 'simplification' and 'agility'. In working to achieve these priorities, IAG is mindful of its social and environmental responsibilities.

The 'customer' priority is to deliver world-leading customer experiences. To achieve this, IAG is pursuing a program of work that is transforming IAG from a product-led organisation to one that is orientated around the customer and informed by a deeper data-driven understanding of customers and their behaviours.

The 'simplification' priority is focused on developing a simplified, modular and lower cost operating model. The organisational capabilities that are helping to achieve the simplification priority are technology transformation, operational partnering and supply chain improvements.

The 'agility' priority defines the work to become an agile organisation distinguished by innovation, speed and importantly, execution skills.

The tables below provide a summary of key balanced scorecard objectives and outcomes for IAG for the year ended 30 June 2018. The objectives were agreed with the Board at the beginning of the financial year and are designed to focus Executives on delivering superior performance outcomes against the agreed priorities. In determining these priorities, the Board has also considered what they believe will support IAG's long-term financial soundness and ensured the risks undertaken are appropriately managed within the risk appetite. Each Executive's performance is also assessed based on their contribution to the objectives outlined below.

TABLE 5a – BALANCED SCORECARD OBJECTIVES

CATEGORY	OBJECTIVE	RATIONALE
Financial measures (60% of scorecard)	Earnings	Net profit after tax shows IAG's overall earnings after all expenses and taxation attributable to shareholders of the Company.
	Controllable operating expense	IAG's continued focus on optimisation of its operating model and related cost-out initiatives improve the efficiency with which IAG deploys its resources.
	Profitability	Underlying profit has been used as the measure of profitability for the 2018 financial year. In previous years, IAG has used underlying insurance margin to present a view of normalised performance. IAG has adopted underlying profit as the measure as it provides a more holistic view of the absolute earnings power of IAG's core insurance-related businesses. It provides a view of the underlying profitability (in dollars) of the underwriting, fee-based and associate businesses and is an important measure of how IAG generates value for shareholders.
	Growth	IAG continues to expand its product and service offerings to its markets, measured through Gross Written Premium growth, creating value for its shareholders, customers and partners.
Non-financial measures (40% of scorecard)	Customer advocacy	IAG's strategy is designed to 'put the customer at the centre of everything we do'. IAG considers this essential to driving the ability to grow profitably over the longer term. IAG is focused on designing compelling product offerings by developing a deeper understanding of customers' needs and the changing environment, then delivering world-leading customer experiences, including through digital channels. IAG uses the Customer Net Promoter Scores to measure the impact of these initiatives for its customers.
	Employee advocacy	IAG seeks to motivate and engage its employees around its Purpose of 'making your world a safer place'. Creating a strong organisational culture helps IAG deliver strong business results. IAG uses the Employee Net Promoter Score to measure its effectiveness in fostering a strong organisational culture.
	Risk appetite	Management of risk is integral to delivering IAG's strategy to meet short-term objectives and achieve long-term sustainability. IAG seeks to optimise the evaluation and pricing of risk. IAG has a clear articulation of its risk appetite, which the Board approves to uphold the expectations of IAG's stakeholders for how IAG employees conduct themselves. Due to the importance of risk management to IAG, it is included as an explicit measure on the scorecard.

TABLE 5b – BALANCED SCORECARD RESULTS FOR THE YEAR ENDED 30 JUNE 2018

OBJECTIVE AND WEIGHTING	MEASURE AND OUTCOME	COMMENT
Earnings 20%	Exceeded The Group's earnings exceeded target, with a net profit after tax of $923 million.	The strong net profit after tax result was driven largely by an improvement in the underlying profitability of the business, significantly higher than anticipated reserve releases and relatively benign natural perils experience.
Controllable operating expense 15%	Partially met The Group remains on track to achieve its targeted run-rate reduction of 10% of controllable operating expenses at the end of the 2019 financial year.	Controllable operating expenses in the period were influenced by higher costs primarily associated with the restructure of the Australian division announced in July 2017, additional investment in relation to a number of optimisation initiatives and incremental costs related to the Royal Commission.
Profitability 15%	Partially exceeded IAG's underlying result was ahead of target. This was achieved whilst also lowering the Group's risk exposure via a new whole-of-account quota share arrangement mid-way through the year.	IAG has partially exceeded its underlying result target for the year. The underlying performance of the core general insurance business improved over the prior year, reflecting rate-driven growth in short-tail personal and commercial classes in Australia and New Zealand, lower large loss experience in Australian commercial property and improved NSW CTP profitability.
Growth 10%	Exceeded IAG achieved Gross Written Premium growth from continuing operations of 1.8% (or 2.4% after adjusting for currency movements), which exceeded the target.	IAG's reported growth for the year was adversely impacted by a combination of lower premium attributable to reform of the NSW CTP Scheme, and ceasing participation in Swann's motorcycle and motor distribution channels. Normalising for these effects and the impact of foreign currency movements (particularly the NZD), IAG's underlying growth was over 4%. This underlying growth has been predominantly driven by rate increases.
Customer advocacy 20%	Met IAG sets a Customer Net Promoter Score (NPS) target relative to its peers. IAG's NPS for the 2018 financial year was 4 points above the competitive market average. This met the target range of +4 to +6 NPS points above the competitor average.	IAG continued to perform above its competitors during the 2018 financial year. The stable overall performance was driven by NRMA achieving an NPS of +19, with improvements seen for the SGIO, SGIC and New Zealand-based brands. However, a decline has been recorded for CGU, with an NPS of -3. IAG continues to invest in its customer advocacy programs to drive improvements across the customer journey.

OBJECTIVE AND WEIGHTING	MEASURE AND OUTCOME	COMMENT
Employee advocacy 10%	Partially exceeded IAG measures employee advocacy using an Employee Net Promoter Score (eNPS). The eNPS target was to increase IAG's eNPS by between 8 and 16 points compared to the year ended 30 June 2017. IAG's eNPS result for June 2018 saw an 18-point improvement, partially exceeding the target.	IAG has experienced a significant improvement in IAG's employee advocacy scores, which employees attribute to IAG's leadership effectiveness, approach to workplace flexibility, employment benefits, work life balance and a positive work environment. IAG is implementing a system of work to support the shift towards an agile culture. The positive improvements in eNPS suggest the implementation of this system of work is generating positive outcomes for IAG's employees.
Risk appetite 10%	Met IAG measures risk-taking within the Board approved risk appetite. IAG targets 95% of operations to be within the risk appetite statements, with formal risk acceptance in place for areas operating outside of this risk appetite statement and appropriate actions to mitigate being in place.	There has been a significant level of improvement in relation to risk management and governance across IAG during the 2018 financial year. This work has resulted in an effective risk management framework and improved progress in risk maturity in both Australia and New Zealand. IAG will continue to invest in improving its risk management framework to be sufficiently robust when applied to IAG future strategy.

II. STI outcomes for the year ended 30 June 2018

The following table sets out the STI outcomes for Executives for the year ended 30 June 2018. Reflecting the desire to encourage collaboration among Executives, STI outcomes are based on each Executive's contribution to the Group Balanced Scorecard objectives described in Table 5a. The Board has the ability to adjust each Executive's STI up or down by 20%, based on their performance against individual goals and how they have fulfilled the accountabilities of their role.

Prior to determining the final incentive outcome, the Board assesses the risk management performance of the Executives, to ensure that incentives provided to Executives are appropriate. The assessment of risk by the Group CEO was informed by the Chair of the Risk Committee and acting Chief Risk Officer, who also subsequently provided their assessment directly to the Board. The Board considered whether any risk issue required the adjustment of an STI outcome for the year ended 30 June 2018, or to deferred STI awards from prior years due to vest on 1 September 2018, and determined that no adjustments were necessary. The Board will continue to consider risk-based adjustments when determining future STI awards. The Board also exercised its discretion to ensure that the final Balanced Scorecard outcomes appropriately reflected performance. The average STI for all Executives was 71% of the maximum achievable, with payments ranging from 50% to 84% of the maximum achievable.

TABLE 6 – ACTUAL STI OUTCOMES FOR THE YEAR ENDED 30 JUNE 2018

	MAXIMUM STI OPPORTUNITY	ACTUAL STI OUTCOME		CASH STI OUTCOME (2/3 OF OUTCOME)	DEFERRED STI OUTCOME (1/3 OF OUTCOME)
	(% of fixed pay)	(% of maximum)(1)	(% of fixed pay)	(% of fixed pay)	(% of fixed pay)
Peter Harmer	150 %	74 %	111 %	74 %	37 %
Julie Batch	120 %	72 %	86 %	57 %	29 %
Ben Bessell	120 %	60 %	72 %	48 %	24 %
Tim Clark	80 %	70 %	56 %	37 %	19 %
Nicholas Hawkins	120 %	80 %	96 %	64 %	32 %
Jacki Johnson	120 %	76 %	91 %	61 %	30 %
Mark Milliner	120 %	72 %	86 %	57 %	29 %
Craig Olsen	120 %	84 %	101 %	67 %	34 %
Clayton Whipp	120 %	50 %	60 %	40 %	20 %

(1) The proportion of STI forfeited is derived by subtracting the actual percentage of maximum received from 100% and was 29% on average for the year ended 30 June 2018 (compared to 36% in 2017).

Anthony Justice was not eligible for an STI for the year ended 30 June 2018.

III. Linking IAG's long-term performance and long-term reward

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

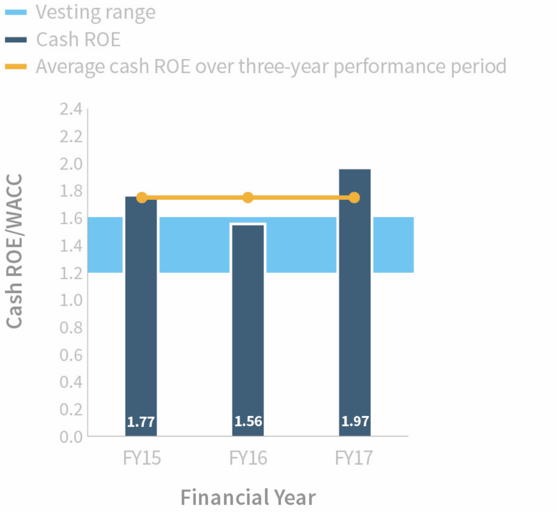
Cash ROE – 100% vesting

Cash ROE is calculated after each half year by dividing the cash earnings of IAG by the average equity balance for that period. This cash ROE figure is then expressed as a multiple of IAG's WACC over the same timeframe. The cash ROE vesting outcome is based on the average cash ROE to WACC multiple over each of the six half years during the performance period.

Cash earnings is IAG's net profit after tax attributable to owners of the Company, adjusted for the post-tax effect of any amortisation and impairment of acquired identifiable intangible assets and unusual items. The Board considers the difference between the statutory profit and cash earnings. Any adjustments to statutory profit are assessed to determine whether they should be considered in determining the cash ROE outcome. The Board can reduce the cash ROE vesting outcomes in order to ensure that reward outcomes appropriately reflect performance.

For the performance period from 1 July 2014 to 30 June 2017, the average cash ROE was 1.76 times WACC. In considering the differences between statutory profit and cash ROE over this period, the Board reduced the cash ROE outcome by the value of the software impairments announced to the market on 19 August 2016. The Board made no other adjustments to cash ROE in determining the vesting outcome. After making the adjustment for the software impairment, the notional cash ROE outcome was 1.68 times WACC. The award still vested in full as this was still above the maximum of the vesting range. The strong cash ROE performance has similarly been reflected in the dividend provided to shareholders.

IAG HISTORICAL CASH ROE OVER WACC FOR THE LTI PLAN



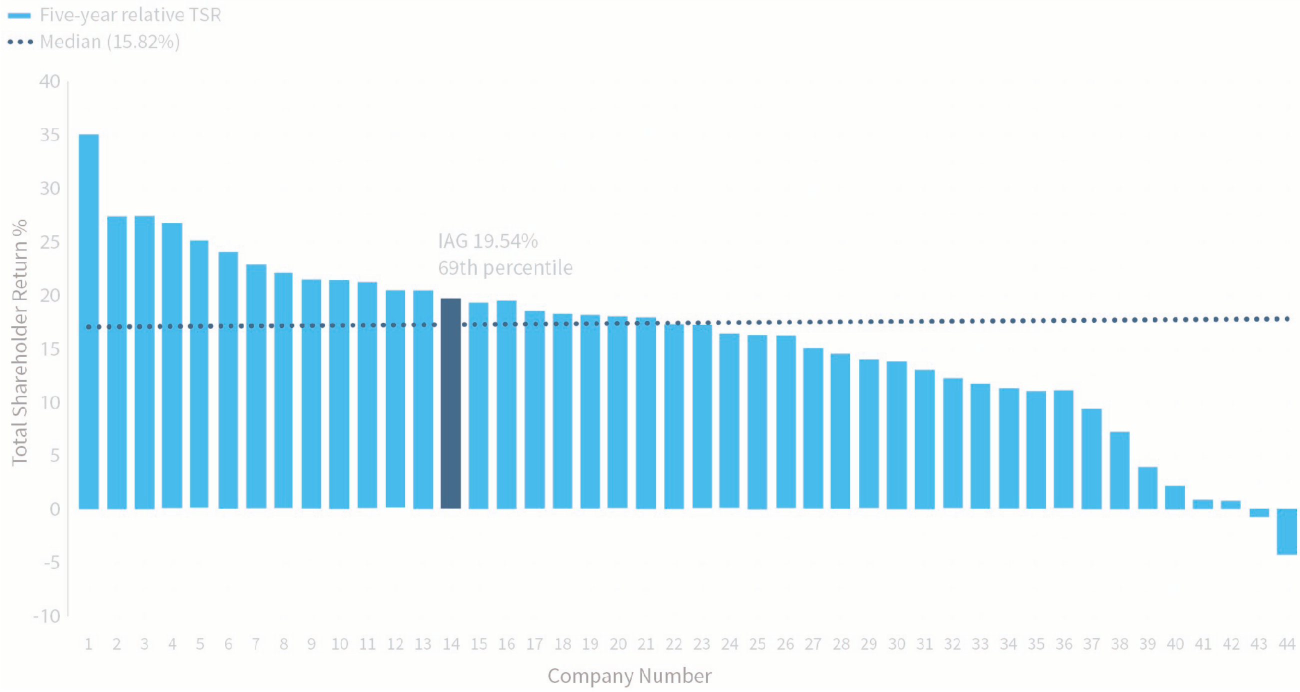
Relative TSR – additional 32% vesting

On 30 September 2017, two grants of the TSR portion of the LTI were tested: the test of the 2013/2014 LTI award and a legacy retest of the 2012/2013 LTI award.

- 2013/2014 LTI award: IAG's TSR was ranked at the 42nd percentile of its peer group and subsequently none of this award vested. There will be no retests for this award.
- 2012/2013 LTI award: IAG's TSR was ranked at the 69th percentile of its peer group, resulting in an overall vesting outcome of 88%. This result translated to an additional 32% vesting above the 56% that had already vested following the retest on 30 September 2016. This was the final test for this grant.

The following graph illustrates IAG's relative TSR against the top 50 industrial companies in the S&P/ASX 100 for the 2012/2013 LTI award:

IAG'S RELATIVE TSR AGAINST TOP 50 INDUSTRIAL COMPANIES IN S&P/ASX 100



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

TABLE 7 – HISTORICAL ANALYSIS OF SHAREHOLDER RETURN

	YEAR ENDED 30 JUNE 2014	YEAR ENDED 30 JUNE 2015	YEAR ENDED 30 JUNE 2016	YEAR ENDED 30 JUNE 2017	**YEAR ENDED 30 JUNE 2018**
Closing share price ($)	5.84	5.58	5.45	6.78	**8.53**
Dividends per ordinary share (cents)	39.00	29.00	36.00(1)	33.00	**34.00**
Basic earnings per share (cents)	56.09	31.22	25.79	39.03	**39.06**
Cash ROE (%)	23.0	15.3	13.0	15.2	**15.6**
Three-year average cash ROE to WACC outcome for EPR Plan	2.34	2.47	2.00(2)	1.76(2)	**1.83**(2)

(1) This includes the 10.00 cents (per ordinary share) 2016 special dividend.

(2) Outcomes in Table 7 reflect IAG's average cash ROE to WACC prior to the Board considering the impact of the software impairments announced to the market on 19 August 2016. The impact of the software impairments was to reduce average cash ROE to WACC by 0.09 times WACC in the three years to 30 June 2016, 0.08 times WACC in the three years to 30 June 2017 and 0.09 times WACC in the three years to 30 June 2018.

IV. Actual remuneration received by Executives

Table 8 below provides details of the remuneration received by Executives during the financial year. The table displays fixed pay and other benefits paid during the financial year, the value of cash STI awards earned in the financial year, and the value of prior years' deferred STI and LTI awards that vested during the financial year. For remuneration details provided in accordance with the Accounting Standards, refer to Appendix 1.

TABLE 8 – ACTUAL REMUNERATION RECEIVED IN 2018 AND 2017

	FINANCIAL YEAR	FIXED PAY $000 (1)	OTHER BENEFITS AND LEAVE ACCRUALS $000 (2)	TERMINATION BENEFITS $000 (3)	CASH STI $000 (4)	DEFERRED STI VESTED $000 (5)	LTI VESTED $000 (6)	TOTAL ACTUAL REMUNERATION RECEIVED $000
EXECUTIVES								
Peter Harmer	**2018**	**1,700**	**88**	**-**	**1,258**	**398**	**1,058**	**4,502**
	2017	1,700	17	-	1,139	288	697	3,841
Julie Batch(7)	**2018**	**700**	**(7)**	**-**	**403**	**141**	**169**	**1,406**
	2017	662	(11)	-	353	110	111	1,225
Tim Clark(8)	**2018**	**206**	**12**	**-**	**76**	**-**	**-**	**294**
Nicholas Hawkins(7)	**2018**	**1,200**	**37**	**-**	**768**	**344**	**1,058**	**3,407**
	2017	1,173	25	-	643	327	697	2,865
Jacki Johnson	**2018**	**1,091**	**12**	**-**	**663**	**289**	**1,054**	**3,109**
	2017	1,091	(40)	-	524	240	644	2,459
Mark Milliner	**2018**	**1,000**	**76**	**-**	**576**	**-**	**-**	**1,652**
	2017	1,000	22	-	536	-	-	1,558
Craig Olsen(9)	**2018**	**728**	**58**	**-**	**496**	**119**	**122**	**1,523**
	2017	711	33	-	381	74	79	1,278
EXECUTIVES WHO CEASED AS KMP								
Ben Bessell(8)	**2018**	**35**	**(21)**	**-**	**17**	**131**	**141**	**303**
	2017	700	33	-	308	82	91	1,214
Anthony Justice(10)	**2018**	**269**	**(2)**	**555**	**-**	**130**	**90**	**1,042**
	2017	690	(6)	-	375	71	-	1,130
Clayton Whipp(10)	**2018**	**329**	**26**	**255**	**130**	**218**	**309**	**1,267**
	2017	775	11	-	310	153	127	1,376

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

(2) Further details are provided in Table 12 in Appendix 1.

(3) Payment in lieu of notice, which incorporates statutory notice and severance entitlements.

(4) Cash STI earned within the year ended 30 June 2018 and to be paid in September 2018.

(5) The deferred STI vesting on 1 September 2017 was valued using the five-day VWAP of $6.34 (1 September 2016: $5.60).

(6) The LTI vested was valued using the five-day VWAP at vesting date which was $6.43 for awards vested on 24 August 2017 and $6.39 for awards vested on 30 September 2017 (22 August 2016: $5.90 and 30 September 2016: $5.46).

(7) The reported fixed pay for Nicholas Hawkins and Julie Batch is higher in 2018 than 2017 as their fixed pay was increased part-way through the 2017 year.

(8) Remuneration for Tim Clark and Ben Bessell is presented for the period for which they served as a KMP. As Tim Clark was not a KMP in the prior year, no information is shown for the year ended 30 June 2017.

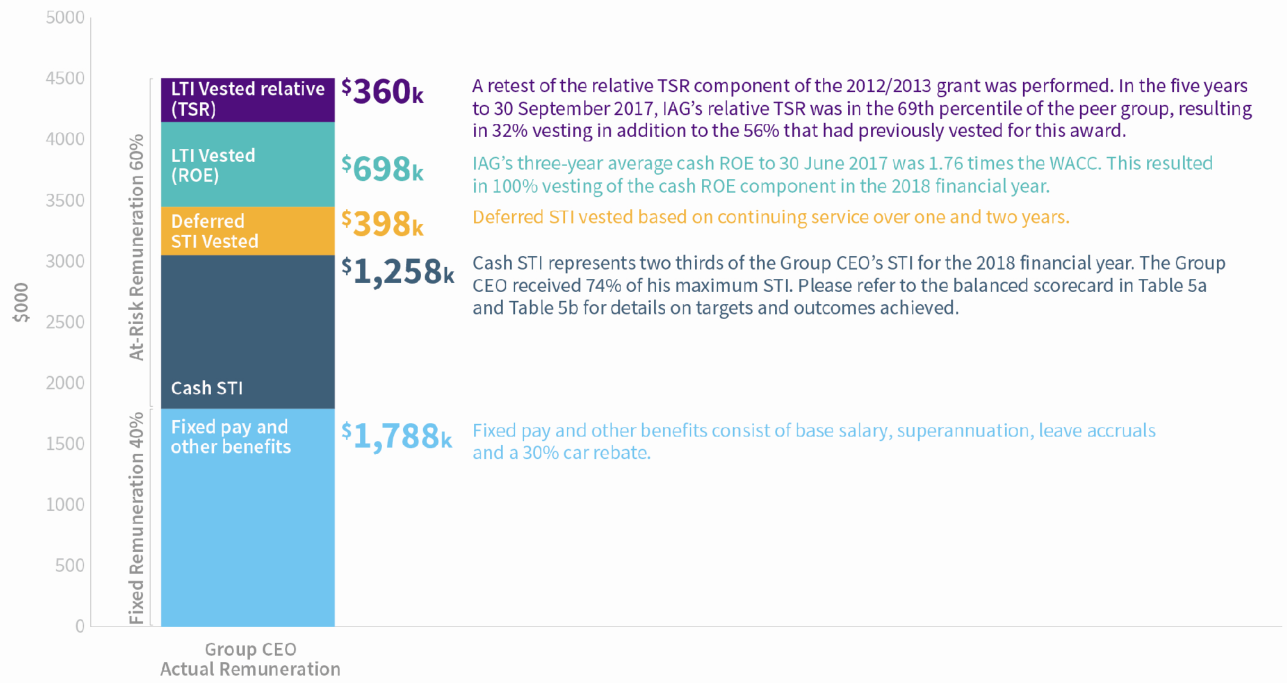
(9) Remuneration for Craig Olsen was determined in New Zealand dollars and reported in Australian dollars using the average exchange rate for the year ended 30 June 2018 which was 1 NZD = 0.922 AUD.

(10) Refer to Appendix 2, section IV for details on termination benefits.

V. Group CEO remuneration

Below are further details on drivers of the actual remuneration received by the Group CEO that are outlined in Table 8. His remuneration has been broken down into the components of the remuneration mix, with commentary on how performance has translated into remuneration outcomes.

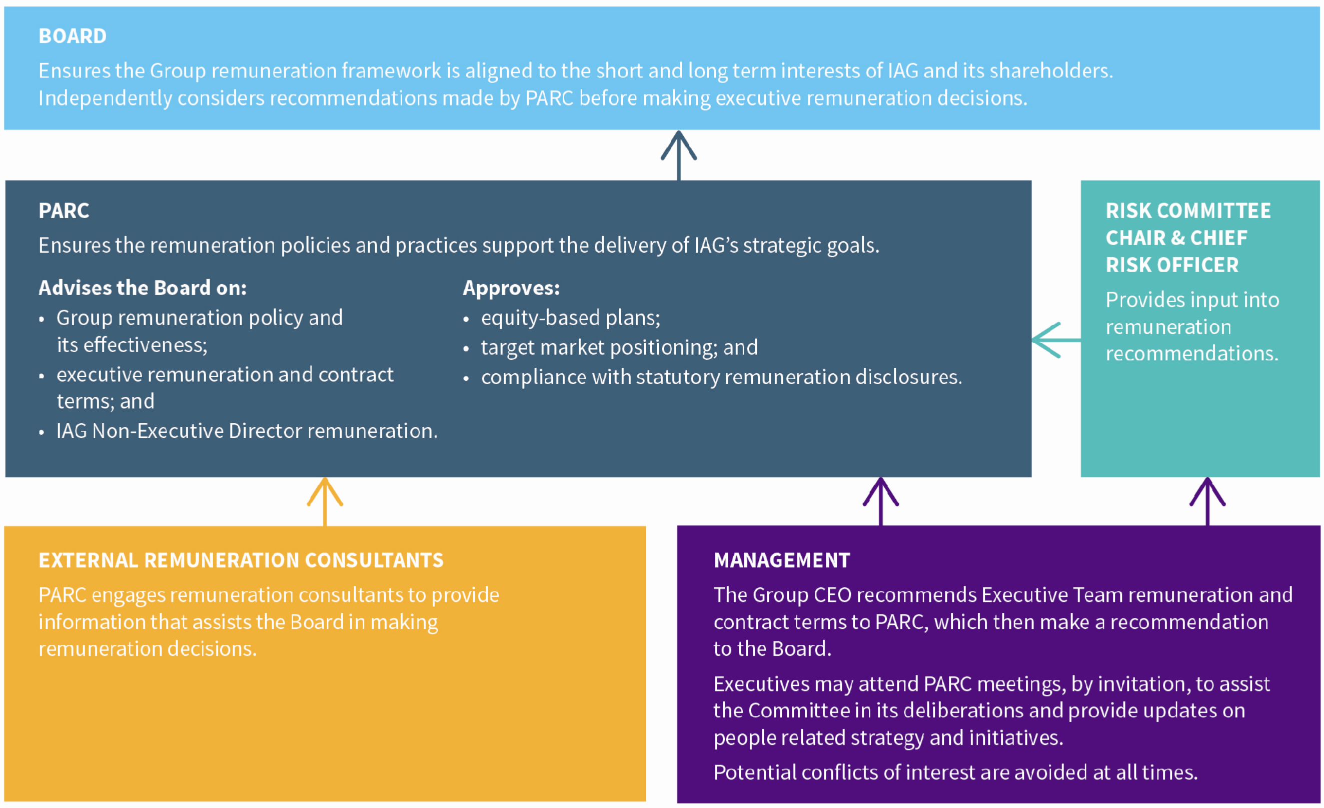
GROUP CEO FY18 PERFORMANCE AND ACTUAL REMUNERATION OUTCOMES



D. EXECUTIVE REMUNERATION GOVERNANCE

I. IAG's approach to remuneration governance

IAG governs its remuneration through the Board and PARC. These governance arrangements are illustrated in the following chart.



II. Use of remuneration consultants

PARC engaged Pay Governance as external remuneration consultants to assist with the review of IAG's approach to executive remuneration. Pay Governance was engaged during the year to provide a review of global market practices and to facilitate a workshop for the Board in reviewing IAG's executive remuneration strategy. The remuneration information provided was used as an input to the remuneration decisions by the Board only. EY was separately engaged to provide remuneration benchmarking of the Non-Executive Directors and the Executive Team. No remuneration recommendations, as defined by the *Corporations Act 2001*, were provided by Pay Governance or EY.

III. Adjustment policy

Each year, the Board assesses whether variable remuneration 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.

Each year PARC makes a recommendation to the Board on whether to adjust variable reward. The Group CEO initially assesses material financial and non-financial risks across the Group as well as the risk management performance of each member of the Executive Team. This assessment is supported by a detailed review of risk and audit reporting across the year by the acting Chief Risk Officer. The Chair of the Risk Committee independently provides input to the Group CEO. The Group CEO makes a recommendation to PARC on whether an adjustment is necessary to the remuneration of any individual or group of employees. PARC and the Board separately consider the Group CEO's recommendation, together with input from both the acting Chief Risk Officer and the Chair of the Risk Committee, in conducting their own assessment of whether an adjustment of variable remuneration is required. In the year ended 30 June 2018, this assessment did not reveal any requirement for the Board to adjust remuneration.

IV. Mandatory shareholding requirement for Executives

The Group CEO is required to accumulate and hold ordinary shares of the Company or other IAG securities with a value of two times his or her base salary, and the Executive Team one times their respective base salaries. Executives have four 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 2014 met the mandatory shareholding requirement at 30 June 2018.

E. 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. Mandatory shareholding requirement for Non-Executive Directors

Non-Executive Directors are required to hold ordinary shares of the Company or other IAG securities with a value equal to their annual Board fee. The mandatory shareholding requirement for Non-Executive Directors is based on either the value of shares at acquisition or the market value at the testing date, whichever is higher. This allows Non-Executive Directors to build a long-term shareholding in IAG without being impacted by short-term share price volatility. The Non-Executive Directors have three years from the date of their appointment to the Board to meet their required holding. Compliance with this requirement is assessed at the end of each financial year.

For the test conducted at 30 June 2018, compliance with the mandatory shareholding requirement was assessed using the closing share price as at that date and the Non-Executive Directors' Board fee from three years prior. All Non-Executive Directors appointed prior to 30 June 2015 met the mandatory shareholding requirement at 30 June 2018.

III. Board performance

The Board conducts a review of its performance, composition, size and succession annually and it conducts an independent review of these matters at least every two years with the assistance of 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 April 2018. The Formal Review led by the Chairman involves the completion of questionnaires by Non-Executive Directors and Executives; interviews with the independent expert; the collation of results; and discussion with individual Non-Executive Directors and the Board as well as the Group CEO and Executive Team. PARC is responsible for coordinating the Board's review of the Chairman's performance in those years where a Formal Review is not conducted.

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. Remuneration structure

Non-Executive Director remuneration is comprised of:

- board fees (paid as cash, superannuation and Non-Executive Director Award Rights);
- committee fees; and
- subsidiary board fees.

a. CHANGES TO NON-EXECUTIVE DIRECTOR REMUNERATION DURING THE YEAR ENDED 30 JUNE 2018

In the year ended 30 June 2018, there were no changes to the fees for service as Chairman or a Director on the Insurance Australia Group Limited Board. All Committee fees also remain unchanged. Similarly, in August 2018 the Board reviewed fees for the 2019 financial year and determined that no increase to fees would be made. 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 9 – BOARD AND COMMITTEE FEES

		ROLE	
BOARD/COMMITTEE	YEAR	CHAIRMAN	DIRECTOR
Board	**2018**	**$577,166**	**$192,372**
	2017	$577,166	$192,372
Audit Committee	**2018**	**$50,000**	**$25,000**
	2017	$50,000	$25,000
Risk Committee	**2018**	**$50,000**	**$25,000**
	2017	$50,000	$25,000
People and Remuneration Committee	**2018**	**$50,000**	**$25,000**
	2017	$50,000	$25,000
Nomination Committee	**2018**	**N/A**	**N/A**
	2017	N/A	N/A

b. SUBSIDIARY BOARD FEES

A summary of Non-Executive Directors' service on subsidiary boards and the fees paid is set out below:

TABLE 10 – FEES FOR NON-EXECUTIVE DIRECTORS' SERVICE ON SUBSIDIARY BOARDS

DIRECTOR	SUBSIDIARY	CAPACITY	ANNUAL FEE
Elizabeth Bryan	Insurance Manufacturers of Australia Pty Limited	Chairman	$184,800
Hugh Fletcher*	IAG New Zealand Limited	Chairman	$138,300

* This amount was paid to Hugh Fletcher in New Zealand dollars and reported in Australian dollars using the average exchange rate for the year ended 30 June 2018 which was 1 NZD = 0.922 AUD.

TABLE 11 – NON-EXECUTIVE DIRECTOR AWARD RIGHT (NAR) PLAN

Overview	PARC has determined that the annual remuneration paid by IAG to Non-Executive Directors for their services may be delivered partially in cash and partially in rights over IAG shares. Participation in the NAR Plan is voluntary. Structuring Non-Executive Director remuneration in this way supports Non-Executive Directors in building their shareholdings in IAG, which enhances the alignment of interests between Non-Executive Directors and shareholders.
Performance measures	There are no performance conditions attached to the NAR Plan, which reflects good governance practices by ensuring that the structure of Non-Executive Director remuneration does not act to bias decision-making or compromise objectivity. A service condition is attached to the vesting of the NARs. The full annual allocation of unvested NARs are issued at the grant date, with tranches vesting each month to align the vesting of NARs with the payment of Non-Executive Director fees. As the grant date for NARs is part way through a financial year, a proportion of the NARs granted is immediately vested.
Instrument	Grants under the NAR Plan are in the form of NARs over IAG shares. Each NAR entitles the Non-Executive Director to acquire one ordinary share in IAG subject to satisfaction of a service condition.
Key terms of the NAR Plan	The Non-Executive Director and IAG agree a proportion of the base Board fee to be provided as NARs. The number of NARs offered is determined by dividing this value by the five-day VWAP up to and including the grant date, rounded to the nearest NAR. Non-Executive Directors have no voting rights until the NARs are exercised and the Non-Executive Director holds shares in IAG. Non-Executive Directors do not have to pay any amount to exercise NARs. NARs expire on the date that is 15 years from the grant date, or any other date determined by the Board (Expiry Date). NARs that are not exercised before the Expiry Date will lapse. Non-Executive Directors may not enter into transactions or arrangements which operate to limit the economic risk of unvested entitlements to IAG securities.
Forfeiture conditions	In the event a Non-Executive Director ceases service with the Board, any vested NARs may be exercised for shares in IAG in the subsequent trading window. Any unvested NARs will lapse. Under certain circumstances (e.g. change of control), the Board also has sole and absolute discretion to deal with the rights, including waiving any applicable vesting conditions and/or exercise conditions by giving notice or allowing a Non-Executive Director affected by the relevant event to transfer their rights.

APPENDIX 1. 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 12 – 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											
2018	**1,675**	**1,258**	**63**	**25**	**25**	**-**	**3,046**	**424**	**1,419**	**4,889**	**63**
2017	1,665	1,139	(8)	35	25	-	2,856	307	1,139	4,302	60
Julie Batch											
2018	**671**	**403**	**(17)**	**29**	**10**	**-**	**1,096**	**135**	**410**	**1,641**	**58**
2017	632	353	(21)	30	10	-	1,004	111	267	1,382	53
Tim Clark(9)											
2018	**197**	**76**	**11**	**9**	**1**	**-**	**294**	**28**	**44**	**366**	**40**
Nicholas Hawkins											
2018	**1,171**	**768**	**19**	**29**	**18**	**-**	**2,005**	**285**	**922**	**3,212**	**61**
2017	1,143	643	8	30	17	-	1,841	293	853	2,987	60
Jacki Johnson											
2018	**1,066**	**663**	**(4)**	**25**	**16**	**-**	**1,766**	**249**	**901**	**2,916**	**62**
2017	1,056	524	(56)	35	16	-	1,575	234	857	2,666	61
Mark Milliner											
2018	**980**	**576**	**61**	**20**	**15**	**-**	**1,652**	**443**	**693**	**2,788**	**61**
2017	965	536	7	35	15	-	1,558	235	232	2,025	50
Craig Olsen(10)											
2018	**728**	**496**	**58**	**-**	**-**	**-**	**1,282**	**131**	**418**	**1,831**	**57**
2017	711	381	33	-	-	-	1,125	87	261	1,473	49
EXECUTIVES WHO CEASED AS KMP											
Ben Bessell(11)											
2018	**34**	**17**	**(21)**	**1**	**-**	**-**	**31**	**7**	**22**	**60**	**77**
2017	670	308	23	30	10	-	1,041	96	285	1,422	48
Anthony Justice(12)											
2018	**259**	**-**	**(4)**	**10**	**2**	**555**	**822**	**281**	**653**	**1,756**	**53**
2017	660	375	(16)	30	10	-	1,059	92	249	1,400	51
Clayton Whipp(13)											
2018	**318**	**130**	**24**	**11**	**2**	**255**	**740**	**354**	**860**	**1,954**	**69**
2017	740	310	-	35	11	-	1,096	187	437	1,720	54

(1) Base salary includes amounts paid in cash plus the portion of IAG's superannuation contribution that is paid as cash instead of being paid into superannuation, and salary sacrifice items such as cars and parking, as determined in accordance with *AASB 119 Employee Benefits*. Base salary for Nicholas Hawkins and Julie Batch has increased between the 2017 and 2018 financial years as their remuneration in the 2017 financial year was increased part-way through the year.

(2) Cash STI represents the amount to be settled in cash in relation to the financial year from 1 July 2017 to 30 June 2018.

(3) This column includes annual and mid-service 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 are limited to Craig Olsen for salary continuance insurance.

(4) Superannuation represents the employer's contributions.

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

(6) Payment in lieu of notice which incorporates statutory notice and severance entitlements.

(7) The deferred STI is granted as DARs and is valued using the Black-Scholes valuation model. An allocated portion of unvested DARs is included in the total remuneration disclosure above. The deferred STI for the year ended 30 June 2018 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 EPRs. To determine the value of EPRs, a Monte Carlo simulation (for the relative TSR performance hurdle) and Black-Scholes valuation (for the cash ROE performance hurdle) have been applied. The valuation takes into account the exercise price of the EPR, life of the EPR, price of ordinary shares of the Company as at the grant date, expected volatility of the Company's 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) Tim Clark was appointed to the role of acting Chief Risk Officer on 27 February 2018. Remuneration has been disclosed for the period he acted in a KMP role.

(10) Remuneration for Craig Olsen was determined in New Zealand dollars and reported in Australian dollars using the average exchange rate for the year ended 30 June 2018 which was 1 NZD = 0.922 AUD.

(11) Ben Bessell ceased being a KMP on 19 July 2017 as a result of the implementation of the new IAG Australian operating model.

(12) Anthony Justice ceased being a KMP on 18 November 2017 when he ceased employment with IAG.

(13) Clayton Whipp retired from the role of Chief Risk Officer on 1 December 2017.

II. Total remuneration details for Non-Executive Directors

Details of total remuneration for Non-Executive Directors for the year ended 30 June 2018 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 board and committee fees	Superannuation	Retirement benefits				
	$000	$000	$000	$000	$000	$000	$000	$000
NON-EXECUTIVE DIRECTORS								
Elizabeth Bryan								
2018	**481**	**197**	**20**	**-**	**-**	**-**	**90**	**788**
2017	474	226	19	-	-	-	97	816
Duncan Boyle								
2018	**176**	**63**	**23**	**-**	**-**	**-**	**-**	**262**
2017	92	18	10	-	-	-	-	120
Hugh Fletcher								
2018	**176**	**184**	**21**	**-**	**-**	**-**	**-**	**381**
2017	176	187	21	-	-	-	-	384
Sheila McGregor(1)								
2018	**53**	**7**	**6**	**-**	**-**	**-**	**-**	**66**
Jon Nicholson								
2018	**176**	**55**	**22**	**-**	**-**	**-**	**-**	**253**
2017	177	46	20	-	-	-	-	243
Helen Nugent								
2018	**176**	**59**	**22**	**-**	**-**	**-**	**-**	**257**
2017	69	26	11	-	-	-	24	130
Tom Pockett								
2018	**179**	**68**	**20**	**-**	**-**	**-**	**-**	**267**
2017	180	68	19	-	-	-	-	267
Michelle Tredenick(1)								
2018	**53**	**7**	**6**	**-**	**-**	**-**	**-**	**66**
Philip Twyman								
2018	**178**	**60**	**20**	**-**	**-**	**-**	**-**	**258**
2017	180	70	19	-	-	-	-	269
NON-EXECUTIVE DIRECTOR WHO CEASED AS KMP								
Alison Deans								
2018	**59**	**15**	**7**	**-**	**-**	**-**	**-**	**81**
2017	149	32	20	-	-	-	24	225

(1) Non-Executive Directors appointed part way through the year ended 30 June 2018.

APPENDIX 2. EXECUTIVE EMPLOYMENT AGREEMENTS

Details are provided below of contractual elements for the Group CEO and Executive Team. 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. 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 12-month notice period, or payment in lieu of notice, as provided in their employment agreement; and
- the retrenchment benefits due under the company retrenchment policy.

For Executives based in Australia, the maximum benefit under the retrenchment policy is 87 weeks of base salary, 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 would 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 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.

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. Executives who ceased employment in the financial year

All termination benefits provided to Executives did not exceed the level that would require shareholder approval under the *Corporations Act 2001*.

On ceasing employment, Anthony Justice received a contractual payment in lieu of notice of $525,000. In addition, Mr Justice received outplacement support to the value of $30,000. No other payments were provided to Mr Justice upon termination.

On ceasing employment, Clayton Whipp received a contractual payment in lieu of notice of $255,000. No other payments were provided to Mr Whipp upon termination.

Ben Bessell did not receive any termination benefits upon ceasing as KMP as Mr Bessell has continued employment with IAG.

APPENDIX 3. MOVEMENT IN EQUITY PLANS WITHIN THE FINANCIAL YEAR

Changes in each Executive's holding of DARs and EPRs and each Non-Executive Director's holdings of NARs during the financial year are set out below. The DARs granted during the year reflect the deferred portion of the STI outcome for the year ended 30 June 2017. The EPRs granted during the year ended 30 June 2018 were in relation to the LTI plan. The NARs granted during the year represent the total number of rights a Non-Executive Director has agreed to receive as part of the payment of their base Board fees.

TABLE 14 – MOVEMENT IN POTENTIAL VALUE OF DARS, EPRS AND NARS FOR THE YEAR ENDED 30 JUNE 2018

		RIGHTS ON ISSUE AT 1 JULY (1)	RIGHTS GRANTED (2)		RIGHTS EXERCISED (3)		RIGHTS LAPSED		RIGHTS ON ISSUE AT 30 JUNE	RIGHTS VESTED DURING THE YEAR	RIGHTS VESTED AND EXERCIS-ABLE AT 30 JUNE
		Number	Number	Value $000	Number	Value $000	Number	Value $000	Number	Number	Number
EXECUTIVES											
Peter Harmer	DAR	104,350	88,100	558	(62,800)	456	-	-	129,650	62,800	-
	EPR	1,247,762	394,200	1,736	(164,986)	1,197	(136,026)	987	1,340,950	164,986	-
Julie Batch	DAR	34,750	27,300	173	(22,300)	162	-	-	39,750	22,300	-
	EPR	309,206	135,300	596	(26,368)	191	(21,538)	156	396,600	26,368	-
Tim Clark	DAR	21,300	-	-	-	-	-	-	21,300	-	-
	EPR	117,100	-	-	-	-	-	-	117,100	-	-
Nicholas Hawkins	DAR	81,400	49,800	316	(54,200)	393	-	-	77,000	54,200	-
	EPR	912,362	231,900	1,021	(164,986)	1,197	(136,026)	987	843,250	164,986	-
Jacki Johnson	DAR	72,450	40,500	257	(45,600)	331	-	-	67,350	45,600	-
	EPR	901,083	210,800	928	(167,457)	1,215	(125,276)	909	819,150	164,286	-
Mark Milliner	DAR	150,000	41,500	263	-	-	-	-	191,500	-	-
	EPR	453,500	193,200	851	-	-	-	-	646,700	-	-
Craig Olsen	DAR	30,400	29,500	187	(18,800)	136	-	-	41,100	18,800	-
	EPR	300,268	146,100	644	(19,004)	138	(14,864)	108	412,500	19,004	-
EXECUTIVES WHO CEASED AS KMP											
Ben Bessell(4)	DAR	33,150	-	-	-	-	-	-	33,150	-	-
	EPR	324,184	-	-	-	-	-	-	324,184	-	-
Anthony Justice(4)	DAR	33,150	29,000	184	(20,500)	149	-	-	41,650	20,500	-
	EPR	283,400	-	-	(14,050)	102	-	-	269,350	14,050	-
Clayton Whipp(4)	DAR	76,100	24,000	152	(34,400)	250	-	-	65,700	34,400	-
	EPR	463,354	-	-	(48,716)	354	(24,588)	178	390,050	48,118	-
NON-EXECUTIVE DIRECTORS											
Elizabeth Bryan	NAR	18,877	14,611	90	(28,621)	208	-	-	4,867	14,611	4,867
Helen Nugent	NAR	4,112	-	-	(4,112)	30	-	-	-	-	-
NON-EXECUTIVE DIRECTOR WHO CEASED AS KMP											
Alison Deans	NAR	4,720	-	-	(4,720)	34	-	-	-	-	-

(1) Opening number of rights on issue represents the balance as at the date of appointment as KMP or 1 July 2017.

(2) The value of the DARs granted during the year is the fair value at grant date calculated using the Black-Scholes valuation model. The value of the DARs granted on 3 November 2017 was $6.34. This amount is allocated to remuneration over years ending 30 June 2018 to 30 June 2020. The value of the cash ROE portion of the EPRs granted on 3 November 2017 is the fair value at grant date, calculated using the Black-Scholes valuation model, which was $5.95. The cash ROE portion of the EPR grants is first exercisable after the performance period concludes on 30 June 2020. The value of the relative TSR portion of the EPRs granted on 3 November 2017 is the fair value at grant date, calculated using the Monte Carlo simulation, which was $2.86. The relative TSR portion of the EPRs is first exercisable on 30 September 2021. The amount is allocated to remuneration over the years ending 30 June 2018 to 30 June 2022. The value of the NARs granted during the year is the fair value at grant date calculated using the Black-Scholes valuation model. The value of the annual NARs granted on 15 September 2017 was $6.14. This amount is allocated to remuneration over the year ended 30 June 2018.

(3) Rights vested and exercised during the financial year. The value of the rights exercised is based on the VWAP for the year ended 30 June 2018, which was $7.26.

(4) The rights on issue at 30 June for former KMP represents the rights held at the date they ceased to be a KMP.

I. LTI awards outstanding during the year ended 30 June 2018
Details of outstanding LTI awards made to Executives in the year ended 30 June 2018 are shown in the table below:

TABLE 15 – LTI AWARDS OUTSTANDING DURING THE YEAR ENDED 30 JUNE 2018

AWARD	GRANT DATE	BASE DATE	TEST DATE	PERFORMANCE HURDLE ACHIEVEMENT	LAST EXERCISE DATE
2017/2018 Series 6 – TSR(1)	03/11/2017	30/09/2017	30/09/2021	N/A	03/11/2024
2017/2018 Series 6 – ROE(1)	03/11/2017	01/07/2017	30/06/2020	N/A	03/11/2024
2016/2017 Series 6 – TSR(1)	24/03/2017	30/09/2016	30/09/2020	N/A	24/03/2024
2016/2017 Series 6 – ROE(1)	24/03/2017	01/07/2016	30/06/2019	N/A	24/03/2024
2016/2017 Series 6 – TSR(1)	02/11/2016	30/09/2016	30/09/2020	N/A	02/11/2023
2016/2017 Series 6 – ROE(1)	02/11/2016	01/07/2016	30/06/2019	N/A	02/11/2023
2015/2016 Series 6 – TSR(1)	31/03/2016	30/09/2015	30/09/2019	N/A	31/03/2023
2015/2016 Series 6 – ROE(1),(2)	31/03/2016	01/07/2015	30/06/2018	N/A	31/03/2023
2015/2016 Series 6 – TSR(1)	02/11/2015	30/09/2015	30/09/2019	N/A	02/11/2022
2015/2016 Series 6 – ROE(1),(2)	02/11/2015	01/07/2015	30/06/2018	N/A	02/11/2022
2014/2015 Series 6 – TSR(1)	03/11/2014	30/09/2014	30/09/2018	N/A	03/11/2021
2014/2015 Series 6 – ROE(1)	03/11/2014	01/07/2014	30/06/2017	100%	03/11/2021
2013/2014 Series 6 – TSR(1)	01/11/2013	30/09/2013	30/09/2017	0%	01/11/2020
2012/2013 Series 5 – TSR(3)	26/10/2012	30/09/2012	30/09/2015	88%	26/10/2019

(1) Terms and conditions for EPR Plans from 2013/2014 to 2017/2018 relating to relative TSR and cash ROE are the same; therefore, they are all referred to as Series 6.
(2) The cash ROE portion of EPR Plan 2015/2016 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 2019.
(3) The TSR portion of the EPR Plan 2012/2013 is the final award that is subject to retesting. The final test was performed on 30 September 2017.

APPENDIX 4. RELATED PARTY INTERESTS
In accordance with the *Corporations Act Regulation 2M.3.03*, the Remuneration Report includes disclosure of related parties' interests.

I. Movements in total number of ordinary shares held
The relevant interests of each KMP and their related parties in ordinary shares of the Company are disclosed in the table below:

TABLE 16 – 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	SHARES RECEIVED ON EXERCISE OF NAR	NET MOVEMENT OF SHARES DUE TO OTHER CHANGES(1)	TOTAL SHARES HELD AT 30 JUNE	SHARES HELD NOMINALLY AT 30 JUNE(2)
	Number	Number	Number	Number	Number	Number	Number
2018							
NON-EXECUTIVE DIRECTORS AND EXECUTIVES							
Elizabeth Bryan	34,234	-	-	28,621	-	62,855	62,855
Duncan Boyle	32,679	-	-	-	-	32,679	32,679
Hugh Fletcher	83,552	-	-	-	1,704	85,256	48,695
Sheila McGregor(3)	-	-	-	-	-	-	-
Jon Nicholson	34,589	-	-	-	-	34,589	24,162
Helen Nugent	540	-	-	4,112	15,460	20,112	20,112
Tom Pockett	32,428	-	-	-	199	32,627	-
Michelle Tredenick(3)	-	-	-	-	-	-	-
Philip Twyman	15,522	-	-	-	-	15,522	12,780
Peter Harmer	825,788	62,800	164,986	-	(120,000)	933,574	172,800
Julie Batch	98,930	22,300	26,368	-	(70,645)	76,953	-
Tim Clark	521	-	-	-	-	521	521
Nicholas Hawkins	220,000	54,200	164,986	-	(269,186)	170,000	-
Jacki Johnson	741,960	45,600	167,457	-	(149,200)	805,817	592,760
Mark Milliner	-	-	-	-	-	-	-
Craig Olsen	149,947	18,800	19,004	-	-	187,751	14,800

	SHARES HELD AT 1 JULY	SHARES RECEIVED ON EXERCISE OF DAR	SHARES RECEIVED ON EXERCISE OF EPR	SHARES RECEIVED ON EXERCISE OF NAR	NET MOVEMENT OF SHARES DUE TO OTHER CHANGES(1)	TOTAL SHARES HELD AT 30 JUNE	SHARES HELD NOMINALLY AT 30 JUNE(2)
	Number	Number	Number	Number	Number	Number	Number
NON-EXECUTIVE DIRECTOR AND EXECUTIVES WHO CEASED AS KMP(4)							
Alison Deans	37,742	-	-	4,720	-	42,462	37,742
Ben Bessell	42,780	-	-	-	-	42,780	277
Anthony Justice	12,750	20,500	14,050	-	-	47,300	-
Clayton Whipp	125,957	34,400	48,716	-	(89,962)	119,111	509

(1) Net movement of shares relates to acquisition and disposal transactions by the KMP and their related parties during the year.

(2) 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.

(3) Opening number of shares held represents the balance as at the date of appointment.

(4) Information on shares held is disclosed up to the date of cessation.

II. Movements in total number of capital notes held

During the year ended 30 June 2018, Philip Twyman indirectly held 5,109 capital notes (2017: 5,109 capital notes). No other KMP had any interest directly or nominally in capital notes during the financial year (2017: nil).

III. Movements in total number of reset exchangeable securities held

No KMP had any interest directly or nominally in reset exchangeable securities of IAG Finance (New Zealand) Limited at any time during the financial year (2017: nil).

IV. Relevant interest of each Director and their related parties in listed securities of the Group in accordance with the *Corporations Act 2001*

TABLE 17 – HOLDINGS OF SHARES, CAPITAL NOTES AND RESET EXCHANGEABLE SECURITIES

	ORDINARY SHARES		CAPITAL NOTES		RESET EXCHANGEABLE SECURITIES	
	Held directly(1)	Held indirectly(2)	Held directly	Held indirectly	Held directly	Held indirectly
Elizabeth Bryan	-	62,855	-	-	-	-
Duncan Boyle	-	32,679	-	-	-	-
Hugh Fletcher	36,561	48,695	-	-	-	-
Sheila McGregor	-	-	-	-	-	-
Jon Nicholson	10,427	24,162	-	-	-	-
Helen Nugent	-	20,112	-	-	-	-
Tom Pockett	32,627	-	-	-	-	-
Michelle Tredenick	-	-	-	-	-	-
Philip Twyman	2,742	12,780	-	5,109	-	-
Peter Harmer	760,774	172,800	-	-	-	-

(1) 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 was signed. Trading in ordinary shares of the Company 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.

(2) These ordinary shares of the Company 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*.

APPENDIX 5. 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 STI earned in the reported financial year plus the value of DARs vested during the financial year plus the value of EPRs vested during the year.
At-risk remuneration	Remuneration that is dependent on a combination of the financial performance of IAG, 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.
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 owners of the Company 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 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	The portion of an Executive's STI that is deferred over a period of two years and typically awarded in the form of DARs.
Executive Team	The Executives who report directly to the Group CEO and: ▪ manage a business unit; or ▪ have accountability for the risk or financial control of the organisation; or ▪ have accountability to deliver a strategic priority. The Executive Team comprises the following members of IAG's Group Leadership Team: Chief Executive Officer, Australia; Chief Executive, New Zealand; Chief Financial Officer; Chief Risk Officer; Chief Customer Officer; and Group Executive, People, Performance and Reputation.
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 Balanced Scorecard	The Group Balanced Scorecard sets out the objectives that have to be achieved to meet key strategic priorities of the organisation. The Group Balanced Scorecard uses goals set against financial and non-financial objectives. Achievement against these objectives is measured and this informs the Board's determination of STI outcomes.
Group CEO	IAG's Managing Director and Chief Executive Officer.
Key management personnel (KMP)	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.
Long-term incentive (LTI)/Executive Performance Rights (EPRs)	A grant of rights in the form of EPRs that are exercisable for ordinary shares of the Company or cash as determined by the Board. Vesting occurs between three and four years after the grant date if performance hurdles are achieved.
Malus	The Board has the ability to reduce the value of deferred remuneration before it has vested, including down to zero.
Non-Executive Director Award Right (NAR)	The NAR Plan provides Directors with the opportunity to build their shareholding in IAG. Under the Plan, Directors agree to receive a portion of their base Board fee in the form of rights over ordinary IAG shares. Participation in the plan is voluntary.
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 Executives in the 2018 financial year, one third of STI is deferred for a period of two years and two thirds is paid in cash in September following the end of the performance year.
Total shareholder return (TSR)	TSR combines share price movements and dividends paid to reflect total return to shareholders. IAG uses relative TSR performance against other companies in the peer group to calculate one half of the LTI outcome.
Weighted average cost of capital (WACC)	This is the rate that a company is expected to pay on average to all its securityholders to finance its assets.

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 and 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 15th day of August 2018 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 of Insurance Australia Group Limited for the financial year ended 30 June 2018 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

Andrew Yates
Partner

Sydney
15 August 2018

CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

FOR THE YEAR ENDED 30 JUNE 2018

	NOTE	2018 $m	2017* $m
Gross earned premium	2.1	**11,522**	11,321
Outwards reinsurance premium expense		**(3,851)**	(3,122)
Net earned premium (i)		**7,671**	8,199
Claims expense		**(8,005)**	(8,358)
Reinsurance and other recoveries revenue	2.1	**3,388**	3,276
Net claims expense (ii)	2.2	**(4,617)**	(5,082)
Commission expense		**(970)**	(985)
Underwriting expense		**(1,787)**	(1,781)
Reinsurance commission revenue	2.1	**880**	687
Net underwriting expense (iii)		**(1,877)**	(2,079)
Underwriting profit (i) + (ii) + (iii)		**1,177**	1,038
Investment income on assets backing insurance liabilities	2.3	**249**	248
Investment expenses on assets backing insurance liabilities		**(19)**	(16)
Insurance profit		**1,407**	1,270
Investment income on shareholders' funds	2.3	**177**	261
Fee and other income		**164**	180
Share of net profit of associates		**31**	19
Finance costs		**(82)**	(93)
Fee-based, corporate and other expenses		**(284)**	(290)
Net loss attributable to non-controlling interests in unitholders' funds		**(3)**	(4)
Profit before income tax from continuing operations		**1,410**	1,343
Income tax expense	5.2	**(384)**	(328)
Profit after income tax from continuing operations		**1,026**	1,015
Loss after income tax from discontinued operations	6.5	**(25)**	(10)
Profit for the year		**1,001**	1,005
OTHER COMPREHENSIVE INCOME/(EXPENSE)			
Items that may be reclassified subsequently to profit or loss:			
Net movement in foreign currency translation reserve, net of tax		**(15)**	(17)
Items that will not be reclassified to profit or loss:			
Remeasurements of defined benefit plans, net of tax		**2**	25
Other comprehensive (expense)/income from continuing operations, net of tax		**(13)**	8
Other comprehensive income from discontinued operations, net of tax	6.5	**1**	1
Total comprehensive income for the year, net of tax		**989**	1,014
PROFIT/(LOSS) FOR THE YEAR ATTRIBUTABLE TO			
Shareholders of the Parent – continuing operations		**947**	938
Shareholders of the Parent – discontinued operations	6.5	**(24)**	(9)
Non-controlling interests – continuing operations		**79**	77
Non-controlling interests – discontinued operations	6.5	**(1)**	(1)
Profit for the year		**1,001**	1,005
TOTAL COMPREHENSIVE INCOME/(LOSS) FOR THE YEAR ATTRIBUTABLE TO			
Shareholders of the Parent – continuing operations		**934**	946
Shareholders of the Parent – discontinued operations	6.5	**(23)**	(8)
Non-controlling interests – continuing operations		**79**	77
Non-controlling interests – discontinued operations	6.5	**(1)**	(1)
Total comprehensive income for the year, net of tax		**989**	1,014

* Prior year comparatives have been re-presented due to the discontinued operations. Refer to Note 6.5.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (CONTINUED)

	NOTE	2018 cents	2017* cents
EARNINGS PER SHARE – CONTINUING AND DISCONTINUED OPERATIONS			
Basic earnings per ordinary share	4.3	**39.06**	39.03
Diluted earnings per ordinary share	4.3	**38.30**	37.72
EARNINGS PER SHARE – CONTINUING OPERATIONS			
Basic earnings per ordinary share	4.3	**40.08**	39.41
Diluted earnings per ordinary share	4.3	**39.26**	38.07

* Prior year comparatives have been re-presented due to the discontinued operations. Refer to Note 6.5.

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 2018

	NOTE	2018 $m	2017 $m
ASSETS			
Cash held for operational purposes	8.1	**448**	424
Investments	2.3	**11,007**	12,136
Trade and other receivables	2.6	**4,085**	4,153
Current tax assets		**17**	66
Assets held for sale	6.5	**655**	-
Reinsurance and other recoveries on outstanding claims	2.2	**5,422**	5,258
Deferred insurance expenses	2.5	**3,443**	2,770
Deferred levies and charges		**136**	105
Deferred tax assets	5.2	**544**	545
Property and equipment		**180**	182
Other assets		**89**	121
Investment in joint venture and associates	6.3	**557**	505
Goodwill and intangible assets	5.1	**3,183**	3,332
Total assets		**29,766**	29,597
LIABILITIES			
Trade and other payables	2.7	**2,592**	2,434
Current tax liabilities		**120**	169
Liabilities held for sale	6.5	**444**	-
Unearned premium liability	2.4	**6,217**	6,331
Outstanding claims liability	2.2	**10,410**	11,371
Non-controlling interests in unitholders' funds		**239**	219
Provisions	5.3	**327**	329
Other liabilities		**516**	328
Interest-bearing liabilities	4.1	**1,960**	1,624
Total liabilities		**22,825**	22,805
Net assets		**6,941**	6,792
EQUITY			
Share capital	4.2	**7,082**	7,082
Treasury shares held in trust		**(27)**	(38)
Reserves		**(4)**	17
Retained earnings		**(382)**	(499)
Parent interest		**6,669**	6,562
Non-controlling interests		**272**	230
Total equity		**6,941**	6,792

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 2018

	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
2018							
Balance at the beginning of the financial year	**7,082**	**(38)**	**(19)**	**36**	**(499)**	**230**	**6,792**
Profit for the year	**-**	**-**	**-**	**-**	**923**	**78**	**1,001**
Other comprehensive income/(expense)	**-**	**-**	**(14)**	**-**	**2**	**-**	**(12)**
Total comprehensive income/(loss) for the year	**-**	**-**	**(14)**	**-**	**925**	**78**	**989**
Transactions with owners in their capacity as owners							
Share-based remuneration	**-**	**11**	**-**	**(7)**	**(5)**	**-**	**(1)**
Dividends determined and paid	**-**	**-**	**-**	**-**	**(803)**	**(36)**	**(839)**
Balance at the end of the financial year	**7,082**	**(27)**	**(33)**	**29**	**(382)**	**272**	**6,941**
2017							
Balance at the beginning of the financial year	7,275	(43)	(3)	35	(701)	222	6,785
Profit for the year	-	-	-	-	929	76	1,005
Other comprehensive income/(expense)	-	-	(16)	-	25	-	9
Total comprehensive income/(loss) for the year	-	-	(16)	-	954	76	1,014
Transactions with owners in their capacity as owners							
Off-market share buy-back, including transaction costs	(193)	-	-	-	(123)	-	(316)
Share-based remuneration	-	5	-	1	(3)	-	3
Purchase of non-controlling interest	-	-	-	-	(3)	-	(3)
Dividends determined and paid	-	-	-	-	(623)	(68)	(691)
Balance at the end of the financial year	7,082	(38)	(19)	36	(499)	230	6,792

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 2018

	NOTE	2018 $m	2017 $m
CASH FLOWS FROM OPERATING ACTIVITIES			
Premium received		**11,779**	11,793
Reinsurance and other recoveries received		**3,195**	3,129
Claims costs paid		**(9,006)**	(8,995)
Outwards reinsurance premium expense paid		**(4,016)**	(3,329)
Dividends, interest and trust distributions received		**416**	458
Finance costs paid		**(87)**	(86)
Income taxes paid		**(379)**	(137)
Other operating receipts		**1,802**	1,566
Other operating payments		**(3,757)**	(3,763)
Net cash flows from operating activities	8.1	**(53)**	636
CASH FLOWS FROM INVESTING ACTIVITIES			
Net cash flows on disposal/(acquisition) of subsidiaries and associates		**4**	37
Net cash flows from sale/(purchase) of investments and plant and equipment		**387**	1,081
Net cash flows from investing activities		**391**	1,118
CASH FLOWS FROM FINANCING ACTIVITIES			
Outlays for repurchase of shares, including transaction costs		**-**	(316)
Proceeds from borrowings, net of transaction costs		**348**	394
Repayment of borrowings		**(2)**	(727)
Net cash flow from issue and redemption of trust units		**18**	(38)
Dividends paid to shareholders of the Parent		**(803)**	(623)
Dividends paid to non-controlling interests		**(36)**	(68)
Net cash flows from financing activities		**(475)**	(1,378)
Net movement in cash held		**(137)**	376
Effects of exchange rate changes on balances of cash held in foreign currencies		**2**	-
Cash and cash equivalents at the beginning of the financial year		**1,480**	1,104
Cash and cash equivalents at the end of the financial year	8.1	**1,345**	1,480

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

NOTES TO THE FINANCIAL STATEMENTS

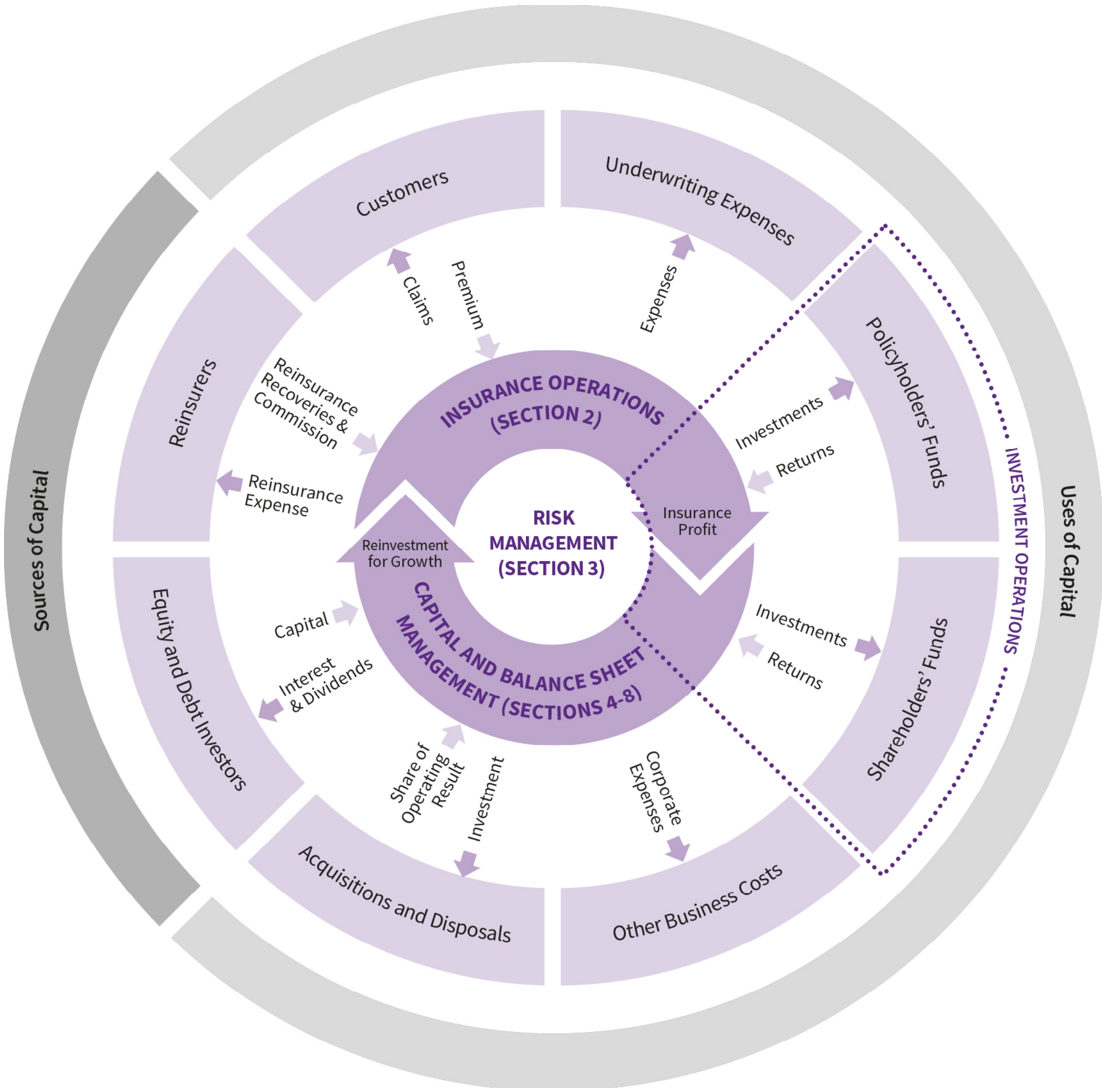
1. OVERVIEW

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 IAG.

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 IAG's exposure to various risks, explains how these affect IAG's financial position and performance and how IAG seeks to manage and mitigate these risks.
4. Capital structure – provides information about the capital management practices of IAG 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 IAG's tax balances.
6. Group structure – provides a summary of IAG's controlled entities and includes acquisition and divestment disclosure.
7. Unrecognised items – disclosure of items not recognised in the financial statements at the balance date but which could potentially have a significant impact on IAG'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 (Company or Parent), the ultimate parent entity in the Group, 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 13, Tower Two, Darling Park, 201 Sussex Street, Sydney, NSW 2000, Australia. This financial report covers the consolidated financial statements for the Company and its subsidiaries (IAG or Group) for the year ended 30 June 2018.

A description of the nature of IAG'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 15 August 2018 and complies with International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB), 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 has issued a new standard (*IFRS 17 Insurance Contracts* – adopted as *AASB 17 Insurance Contracts* in an Australian context) that does include such criteria, however this standard will not come into effect until 1 January 2021. Until this standard takes effect, 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 statements incorporates the assets and liabilities of all entities controlled by the Company as at 30 June 2018. A list of significant controlled entities is set out in Note 6.1. 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. Reclassification of comparatives

Certain items have been reclassified from IAG's prior year financial report due to IAG'S consolidated Asian businesses now meeting the classification of discontinued operations. For further details, refer to Note 6.5.

D. SIGNIFICANT ACCOUNTING POLICIES ADOPTED
The accounting policies adopted in the preparation of this financial report have been applied consistently by all entities in IAG 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 IAG. 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 IAG on adoption. Refer to Note 8.5 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 within 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
Investment in joint venture and associates impairment testing	Note 6.3

NOTE 1.3 SEGMENT REPORTING
IAG 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.

A. REPORTABLE SEGMENTS
IAG has general insurance operations in Australia and New Zealand. Following the classification of IAG's consolidated businesses in Thailand, Vietnam and Indonesia as discontinued operations at 30 June 2018, Asia is no longer disclosed as a distinct operating segment. For further details refer to Note 6.5. IAG's ongoing interests in Malaysia and India continue to be treated as associates, but have been reclassified to Corporate and other within IAG's segment reporting.

The reportable segments for the period ended 30 June 2018 comprise the following business divisions:

I. Australia
The Australian division comprises two segments:

Consumer
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).

Business
This segment provides commercial insurance to businesses throughout Australia, predominantly under the CGU and WFI brands through intermediaries including brokers, authorised representatives and distribution partners

II. New Zealand
This segment provides general insurance products 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.

III. Corporate and other
This segment comprises other activities, including corporate services, capital management activity, shareholders' funds investment activities, inward reinsurance from associates, and investment in associates in Malaysia and India. IAG's captive reinsurance operation (captive) is a corporate function that acts as the interface between the external providers of reinsurance capital and the operating business divisions. IAG does not manage or view the captive as a separate business. Consequently, the operating results of the captive are systematically allocated to the operating business segments.

B. FINANCIAL INFORMATION

	AUSTRALIA			NEW ZEALAND	CORPORATE AND OTHER	TOTAL
	CONSUMER	BUSINESS	TOTAL			
	$m	$m	$m	$m	$m	$m
2018						
I. Financial performance						
Total external revenue(1)	**8,434**	**4,473**	**12,907**	**3,267**	**237**	**16,411**
Underwriting profit/(loss)	**833**	**142**	**975**	**209**	**(7)**	**1,177**
Net investment income on assets backing insurance liabilities	**138**	**77**	**215**	**9**	**6**	**230**
Insurance profit/(loss)	**971**	**219**	**1,190**	**218**	**(1)**	**1,407**
Net investment income on shareholders' funds	**-**	**-**	**-**	**-**	**165**	**165**
Share of net profit of associates	**-**	**2**	**2**	**-**	**29**	**31**
Finance costs	**-**	**-**	**-**	**-**	**(82)**	**(82)**
Other net operating result	**-**	**(5)**	**(5)**	**-**	**(106)**	**(111)**
Total segment result from continuing operations	**971**	**216**	**1,187**	**218**	**5**	**1,410**
Income tax expense						**(384)**
Profit for the year from continuing operations						**1,026**
II. Other segment information						
Capital expenditure(2)	**-**	**-**	**-**	**-**	**155**	**155**
Depreciation and amortisation expense	**50**	**64**	**114**	**51**	**-**	**165**
2017(3)						
I. Financial performance						
Total external revenue(1)	8,162	4,241	12,403	3,276	313	15,992
Underwriting profit	816	141	957	80	1	1,038
Net investment income/(expense) on assets backing insurance liabilities	125	63	188	45	(1)	232
Insurance profit	941	204	1,145	125	-	1,270
Net investment income on shareholders' funds	-	-	-	-	246	246
Share of net profit/(loss) of associates	-	(1)	(1)	-	20	19
Finance costs	-	-	-	-	(93)	(93)
Other net operating result	-	(28)	(28)	-	(71)	(99)
Total segment result from continuing operations	941	175	1,116	125	102	1,343
Income tax expense						(328)
Profit for the year from continuing operations						1,015
II. Other segment information						
Capital expenditure(2)	-	-	-	-	109	109
Depreciation and amortisation expense	53	54	107	52	1	160

(1) Total external revenue comprises gross earned premium, 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.

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

(3) Prior year comparatives have been re-presented due to the discontinued operations. Refer to Note 6.5.

2. INSURANCE DISCLOSURES

SECTION INTRODUCTION

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

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

To mitigate IAG's overall risk and optimise its return profile, IAG passes some of its underwriting exposure to third parties (primarily reinsurance companies). The premiums paid to reinsurers are an expense to IAG, 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 IAG under a sound investment philosophy. IAG 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

	2018	2017*
	$m	$m
A. COMPOSITION		
Gross written premium	**11,647**	11,439
Movement in unearned premium liability	**(125)**	(118)
Gross earned premium	**11,522**	11,321
Reinsurance and other recoveries revenue	**3,388**	3,276
Reinsurance commission revenue	**880**	687
Total general insurance revenue	**15,790**	15,284

* Prior year comparatives have been re-presented due to the discontinued operations. Refer to Note 6.5.

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.

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. The final value of the variable commission revenue recognised is subject to the achievement of a specified underlying profitability hurdle rate over time. This variable revenue is recognised over the term of the reinsurance contract on a straight-line, or other systematic basis, in accordance with the terms of the contract, and is reassessed at each reporting date.

NOTE 2.2 CLAIMS AND REINSURANCE AND OTHER RECOVERIES ON OUTSTANDING CLAIMS

A. NET CLAIMS EXPENSE

			2018			2017*
	Current year	Prior years	Total	Current year	Prior years	Total
	$m	$m	$m	$m	$m	$m
Gross claims – undiscounted	**8,585**	**(675)**	**7,910**	9,364	(1,019)	8,345
Discount	**(114)**	**209**	**95**	(135)	148	13
Gross claims – discounted	**8,471**	**(466)**	**8,005**	9,229	(871)	8,358
Reinsurance and other recoveries – undiscounted	**(3,304)**	**(18)**	**(3,322)**	(3,355)	30	(3,325)
Discount	**57**	**(123)**	**(66)**	66	(17)	49
Reinsurance and other recoveries – discounted	**(3,247)**	**(141)**	**(3,388)**	(3,289)	13	(3,276)
Net claims expense	**5,224**	**(607)**	**4,617**	5,940	(858)	5,082

* Prior year comparatives have been re-presented due to the discontinued operations. Refer to Note 6.5

B. NET OUTSTANDING CLAIMS LIABILITY

I. Composition of net outstanding claims liability

	2018	2017
	$m	$m
Gross central estimate – discounted	**8,267**	9,224
Reinsurance and other recoveries – discounted	**(4,377)**	(4,358)
Net central estimate – discounted	**3,890**	4,866
Claims handling costs – discounted	**364**	362
Risk margin	**734**	885
Net outstanding claims liability – discounted	**4,988**	6,113

The gross outstanding claims liability includes $5,756 million (2017: $6,488 million) which is expected to be settled more than 12 months from the reporting date.

The carrying value of reinsurance and other recoveries includes $3,214 million (2017: $3,151 million) which is expected to be settled more than 12 months from the reporting date.

II. Reconciliation of movements in net discounted outstanding claims liability

	2018	2017*
	$m	$m
Net outstanding claims liability at the beginning of the financial year	**6,113**	7,052
Movement in the prior year central estimate	**(244)**	(391)
Current year claims incurred, net of reinsurance and other recoveries	**4,979**	5,689
Claims paid, net of reinsurance and other recoveries received	**(5,644)**	(6,033)
Movement in discounting	**67**	40
Movement in risk margin	**(143)**	(247)
Transfers to liabilities held for sale	**(105)**	-
Net movement of discontinued operations	**(8)**	12
Net foreign currency movements	**(27)**	(9)
Net outstanding claims liability at the end of the financial year	**4,988**	6,113
Reinsurance and other recoveries on outstanding claims liability	**5,422**	5,258
Gross outstanding claims liability at the end of the financial year	**10,410**	11,371

* Prior year comparatives have been re-presented due to the discontinued operations. Refer to Note 6.5.

III. Maturity analysis

Refer to Note 3.1 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 estimate 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 IAG'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 claims 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.

During the financial year, IAG announced the sale of its consolidated businesses in Thailand, Vietnam and Indonesia. The development table below includes claims related to these operations up to the 2018 accident year. Any outstanding claims relating to these businesses have been treated as paid in the table below within item (1).

	ACCIDENT YEAR											
	2008 and prior $m	2009 $m	2010 $m	2011 $m	2012 $m	2013 $m	2014 $m	2015 $m	2016 $m	2017 $m	2018 $m	Total $m
NET ULTIMATE CLAIM PAYMENTS												
Development												
At end of accident year		4,708	4,663	5,010	5,216	5,167	5,602	6,293	4,965	5,267	4,495	
One year later		4,746	4,637	5,123	5,290	5,090	5,606	6,219	4,917	5,211		
Two years later		4,680	4,535	5,162	5,231	5,010	5,519	6,156	4,858			
Three years later		4,673	4,485	5,193	5,142	4,930	5,378	6,040				
Four years later		4,587	4,432	5,390	5,090	4,850	5,309					
Five years later		4,534	4,379	5,457	5,027	4,831						
Six years later		4,489	4,344	5,475	5,020							
Seven years later		4,451	4,315	5,562								
Eight years later		4,447	4,306									
Nine years later		4,441										
Current estimate of net ultimate claim payments		4,441	4,306	5,562	5,020	4,831	5,309	6,040	4,858	5,211	4,495	
Cumulative payments made to date(1)		4,400	4,260	5,357	4,911	4,653	5,036	5,632	4,375	4,604	2,896	
Net undiscounted outstanding claims liability	104	41	46	205	109	178	273	408	483	607	1,599	4,053
Discount to present value	(6)	(2)	(3)	(7)	(6)	(9)	(13)	(19)	(21)	(34)	(43)	(163)
Net discounted outstanding claims liability	98	39	43	198	103	169	260	389	462	573	1,556	3,890
Reconciliation												
Claims handling costs												364
Risk margin												734
Net outstanding claims liability												4,988

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 prior to the reporting date including direct and indirect claims 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 claim payments, both gross and net of reinsurance and other recoveries and associated claims 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 claim 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.

IAG 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:

	2018	2017
	%	%
The percentage risk margin applied to the net outstanding claims liability	**17**	17
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 at 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 goods and services tax (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 IAG'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 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		NEW ZEALAND	ASIA
	CONSUMER	BUSINESS		
2018				
Discounted average term to settlement	**1.9 years**	**2.0 years**	**1.0 year**	**n/a**
Inflation rate	**2.2%-3.9%**	**0.0%-4.3%**	**1.9%**	**n/a**
Superimposed inflation rate	**0.0%-5.0%**	**0.0%-5.0%**	**0.0%**	**n/a**
Discount rate	**1.5%-4.2%**	**1.5%-4.1%**	**1.8%-3.6%**	**n/a**
Claims handling costs ratio	**4.6%**	**4.3%**	**3.9%**	**n/a**
2017				
Discounted average term to settlement	2.1 years	2.0 years	1.0 year	0.4 year
Inflation rate	2.4%-4.1%	0.0%-4.3%	2.0%	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%	1.5%-4.4%	1.8%-3.5%	0.0%
Claims handling costs ratio	4.1%	4.4%	4.1%	1.6%

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 divisional 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 or average term.

ASSUMPTION	MOVEMENT IN ASSUMPTION	AUSTRALIA		NEW ZEALAND	ASIA
		CONSUMER	BUSINESS		
		$m	$m	$m	$m
2018					
Discounted average term to settlement	**+10%**	**(11)**	**(9)**	**(1)**	**n/a**
	-10%	**11**	**9**	**1**	**n/a**
Inflation rate	**+1%**	**46**	**35**	**5**	**n/a**
	-1%	**(45)**	**(34)**	**(4)**	**n/a**
Discount rate	**+1%**	**(46)**	**(35)**	**(4)**	**n/a**
	-1%	**48**	**37**	**4**	**n/a**
Claims handling costs ratio	**+1%**	**48**	**41**	**9**	**n/a**
	-1%	**(48)**	**(41)**	**(9)**	**n/a**
2017					
Discounted average term to settlement	+10%	(14)	(9)	(1)	-
	-10%	14	9	1	-
Inflation rate	+1%	61	40	5	-
	-1%	(59)	(39)	(5)	-
Discount rate	+1%	(61)	(39)	(5)	-
	-1%	65	42	5	-
Claims handling costs ratio	+1%	53	41	7	2
	-1%	(53)	(41)	(7)	(2)

NOTE 2.3 INVESTMENTS

	2018	2017*
	$m	$m
A. INVESTMENT INCOME		
Dividend revenue	**42**	45
Interest revenue	**320**	373
Trust revenue	**37**	18
Realised net (losses)/gains	**(33)**	74
Unrealised net gains/(losses)	**60**	(1)
Total investment income	**426**	509
Represented by		
Investment income on assets backing insurance liabilities	**249**	248
Investment income on shareholders' funds	**177**	261
	426	509

* Prior year comparatives have been re-presented due to the discontinued operations. Refer to Note 6.5.

	2018	2017
	$m	$m
B. INVESTMENT COMPOSITION		
I. Interest-bearing investments		
Cash and short-term money	**753**	1,056
Government and semi-government bonds	**933**	1,034
Corporate bonds and notes	**5,896**	6,311
Subordinated securities	**1,333**	1,768
Other	**253**	199
	9,168	10,368
II. Equity investments (includes exposure to convertible securities)		
Listed	**1,049**	1,099
Unlisted	**683**	479
	1,732	1,578
III. Other investments		
Other trusts	**107**	158
Derivatives	**-**	32
	107	190
Total investments	**11,007**	12,136

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, IAG's investment funds under management are compared to the technical provisions of IAG, 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. IAG 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 supported by comparable transaction multiples observed in the local market.

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

	LEVEL 1 $m	LEVEL 2 $m	LEVEL 3 $m	TOTAL $m
2018				
Interest-bearing investments	**2,169**	**6,998**	**1**	**9,168**
Equity investments	**1,049**	**341**	**342**	**1,732**
Other investments	**-**	**107**	**-**	**107**
	3,218	**7,446**	**343**	**11,007**
2017				
Interest-bearing investments	2,085	8,282	1	10,368
Equity investments	1,076	340	162	1,578
Other investments	4	185	1	190
	3,165	8,807	164	12,136

NOTE 2.4 UNEARNED PREMIUM LIABILITY

	2018 $m	2017* $m
A. RECONCILIATION OF MOVEMENTS		
Unearned premium liability at the beginning of the financial year	**6,331**	6,220
Deferral of premiums written during the financial year	**5,915**	5,748
Earning of premiums written in previous financial years	**(5,790)**	(5,630)
Net premiums earned and written on discontinued operations	**(3)**	(4)
Transfers to liabilities held for sale	**(206)**	-
Net foreign exchange movements	**(30)**	(3)
Unearned premium liability at the end of the financial year	**6,217**	6,331

* Prior year comparatives have been re-presented due to the discontinued operations. Refer to Note 6.5.

The carrying value of unearned premium liability includes $133 million (2017: $172 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. IAG 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. IAG 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.

The LAT at reporting date resulted in a surplus for IAG (2017: surplus for IAG), with the table below providing details of the net premium liabilities (net of reinsurance and adjusted for appropriate risk margin) used in the LAT:

	2018 $m	2017 $m
Net central estimate of present value of expected cash flows on future claims	**2,718**	3,416
Risk margin of the present value of expected future cash flows	**66**	77
	2,784	3,493
Risk margin percentage	**2.4%**	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.

NOTE 2.5 DEFERRED INSURANCE EXPENSES

	DEFERRED ACQUISITION COSTS(1)		DEFERRED OUTWARDS REINSURANCE EXPENSE(2)		TOTAL DEFERRED INSURANCE EXPENSES	
	2018	2017(3)	**2018**	2017(3)	**2018**	2017(3)
	$m	$m	**$m**	$m	**$m**	$m
A. RECONCILIATION OF MOVEMENTS						
At the beginning of the financial year	**1,020**	1,051	**1,750**	1,727	**2,770**	2,778
Costs deferred	**1,809**	1,787	**4,662**	3,134	**6,471**	4,921
Amortisation charged to profit	**(1,835)**	(1,819)	**(3,851)**	(3,122)	**(5,686)**	(4,941)
Transfers to assets held for sale	**(37)**	-	**(74)**	-	**(111)**	-
Net costs earned and written on discontinued operations	**(2)**	2	**25**	12	**23**	14
Net foreign exchange movements	**(6)**	(1)	**(18)**	(1)	**(24)**	(2)
Deferred costs at the end of the financial year	**949**	1,020	**2,494**	1,750	**3,443**	2,770

(1) The carrying value of deferred acquisition costs includes $27 million (2017: $54 million) which is expected to be amortised more than 12 months from reporting date.

(2) The carrying value of deferred outwards reinsurance expense includes $101 million (2017: $42 million) which is expected to be amortised more than 12 months from reporting date.

(3) Prior year comparatives have been re-presented due to the discontinued operations. Refer to Note 6.5.

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

	2018	2017
	$m	$m
A. COMPOSITION		
I. Premium receivable		
Gross premium receivable	**3,622**	3,402
Provision for impairment	**(33)**	(39)
Net premium receivable	**3,589**	3,363
II. Trade and other receivables(1)		
Reinsurance recoveries on paid claims	**92**	242
Loan to associates(2)	**99**	90
Investment-related receivables	**124**	280
Trade and other debtors	**181**	178
Trade and other receivables	**496**	790
	4,085	4,153

(1) 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.

(2) 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 IAG'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

	2018 $m	2017 $m
A. COMPOSITION		
I. Reinsurance premium payable(1)	**1,157**	712
II. Trade creditors(2)		
Commissions payable	**275**	268
Stamp duty payable	**130**	123
GST payable on premium receivable	**175**	157
Corporate treasury derivatives payable	**14**	-
Other(3)	**321**	472
	915	1,020
III. Other payables(2)		
Other creditors and accruals	**403**	378
Investment creditors	**113**	310
Interest payable on interest-bearing liabilities	**4**	14
	520	702
	2,592	2,434

(1) IAG has a right of offset and settles on a net basis under the agreement with National Indemnity Company (NICO), a Berkshire Hathaway (BH) company, and under the combined 12.5% quota share agreements. This balance includes reinsurance premium payable to BH of $1,166 million (2017: $1,166 million) and the combined 12.5% quota share agreements of $727 million (2017: nil), which have been offset with receivables due from BH of $650 million (2017: $677 million) and the combined 12.5% quota share agreements of $294 million (2017: nil), respectively. The relevant cash flows pertaining to the contracts have been presented on a gross basis within the cash flow statement.

(2) 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.

(3) Other trade creditors include $4 million (2017: $6 million) of 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 IAG's approach to risk and capital management.

IAG 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 IAG's strategy, decision-making and 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 six risk categories:

- Strategic
- Insurance
- Reinsurance
- Financial
- Operational
- Regulatory Risk and Compliance

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 six 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 IAG and is supported by a risk function. IAG's CRO and the risk function provide 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 IAG that identify, assess, treat, monitor, report and/or communicate all internal and external sources of risk that could have a material impact on IAG'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 documented 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 the 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 IAG, and provide context to implement the 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 IAG'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 IAG'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.

The RMS is supported by risk culture and behaviours that are the foundation for appropriate risk management and business sustainability. IAG is committed to conducting businesses in a manner aligned with IAG's purpose which is supported by principles developed in conjunction with the Ethics and Consumer Advisory Board which includes external representation.

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 IAG'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. Strategic risk mitigation is further enhanced by the accountabilities of the Customer Labs function operated under the Chief Customer Officer. This function ensures IAG is accessing data-driven customer insights and reacting to such through the innovation of products, services and adjacencies.

C. INSURANCE RISK

Insurance risk is defined as the risk that IAG 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 unforeseen, 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 IAG'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 are issued to each operating division. 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 supporting 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, regulators and shareholders. IAG's significant underwriting and pricing expertise, coupled with its data and analytics capability, allow IAG 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 IAG.

As referenced above, business divisions underwrite within 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 IAG's intention to respond to and settle all valid 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 for further details.

III. Concentrations of insurance risk

Each year IAG sets its tolerance for concentration risk through the use of various models to estimate IAG's maximum exposure to potential natural disasters and other catastrophes. IAG 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 IAG'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 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 policyholders being impacted by the same event. This aggregation of multiple claims arising from a single event creates the most material financial loss potential in the Group. IAG 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. IAG actively monitors the aggregate exposure to catastrophe losses in all regions and limits exposure 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 per risk 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 from continuing operations by both region and product, which demonstrates the diversity of IAG'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):

	2018	2017*
	%	%
a. REGION		
Australia	**79**	80
New Zealand	**21**	20
	100	100
b. PRODUCT		
Motor	**32**	31
Home	**29**	28
Short-tail commercial	**22**	22
CTP (motor liability)	**7**	8
Liability	**6**	6
Other short-tail	**1**	2
Workers' compensation	**3**	3
	100	100

* Prior year comparatives have been re-presented due to the discontinued operations. Refer to Note 6.5.

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;
- inadequate or inappropriate reinsurance recovery management;
- reinsurance arrangements not being 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 IAG'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 IAG's reinsurance retention for catastrophe must not exceed 4% of net earned premium.

IAG purchases catastrophe reinsurance protection to the greater of:

- a 1-in-250 year return period for earthquake loss calculated on a whole-of-portfolio basis for Australia;
- a 1-in-1000 year return period for earthquake loss calculated on a whole-of-portfolio basis for New Zealand.

This is a more conservative view than APRA's prescribed minimum approach of 1-in-200 year return period loss calculated on a whole-of-portfolio, all perils basis.

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.

The amount of reinsurance purchased is determined by reference to the modelled probable maximum loss (PML). Natural perils are inherently uncertain, which presents model risk. As a result, the loss from an actual event could exceed the modelled PML.

To facilitate the reinsurance process, manage counterparty exposure and create economies of scale, IAG has established a centralised reinsurance model across its operations. This is via captive reinsurance entities in Singapore and Labuan and a reinsurance department or virtual captive in Australia, collectively referred to as IAG Reinsurance. IAG Reinsurance acts as the interface between the external providers of reinsurance capital and the operating business divisions.

The use of reinsurance introduces credit risk. The management of credit risk includes the monitoring of reinsurers' credit ratings and controlling total exposures to limit counterparty default risk which is further explained in the financial risk section. IAG adopts a sound underwriting approach to the reinsurance program through the expertise provided by IAG Reinsurance. 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 arrangements:

- a 32.5% whole-of-account quota share arrangements;
- a Group catastrophe cover which is placed in line with the strategy of buying to the level of a 1-in-250 year event on a whole-of-portfolio basis. IAG's catastrophe reinsurance protection runs to a calendar year and operates on an excess of loss basis, with IAG retaining the first $250 million ($169 million post-quota share) of each loss. It covers all territories in which IAG operates. The limit of catastrophe cover purchased effective 1 January 2018 was $8 billion placed to 67.5%. Should a loss event occur that is greater than $8 billion, IAG could potentially incur a net loss greater than the retention. IAG 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;
- crop quota share and stop loss;
- adverse development cover (ADC) and quota share protection on the CTP portfolio;
- ADC for the February 2011 Canterbury earthquake event; and
- ADC for policies issued prior to 31 December 2015 covering IAG's exposure to asbestos relating to legacy general liability and/or workers' compensation policies.

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 investment 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;
- 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.

I. Market risk

a. FOREIGN EXCHANGE RISK

IAG 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	**2018** **$m** **Impact directly to equity**	2017 $m Impact directly to equity
Net investments in foreign operations and related hedge arrangements		
New Zealand dollar	**63**	66
Malaysian ringgit	**18**	18
Other currencies where considered significant	**5**	13
	86	97

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

IAG 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		**2018** **$m** **Impact to profit**	2017 $m Impact to profit
Investments – equity and trust securities and related equity derivatives	+10%	**108**	108
	-10%	**(105)**	(107)

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.

IAG'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 IAG'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		**2018**	2017
		$m	$m
		Impact to profit	Impact to profit
Investments – interest-bearing securities and related interest rate derivatives	+1%	**(159)**	(200)
	-1%	**167**	213

Refer to Note 2.2 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. IAG's credit risk arises predominantly from investment activities, reinsurance activities, premium debtors and dealings with other intermediaries. IAG 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 IAG with the Group Treasury function responsible for implementation. IAG 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

IAG 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 include predominantly high credit quality investments, such as 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 very strong overall credit quality of IAG's investment book:

CREDIT RATING OF INTEREST-BEARING INVESTMENTS	**2018**	2017
	$m	$m
AAA	**3,520**	3,794
AA	**3,514**	3,776
A	**482**	433
BBB and below	**1,652**	2,365
	9,168	10,368

b. REINSURANCE RECOVERIES ON PAID CLAIMS

Reinsurance arrangements mitigate insurance risk but expose IAG 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. IAG has clearly defined policies for the approval and management of credit risk in relation to reinsurers. IAG 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 the jurisdictions in which IAG operates and so there is the potential for additional risk such as country risk and transfer risk.

It is IAG 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 IAG'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	**2018**		2017	
	$m	**% of total**	$m	% of total
AA	**3,667**	**89**	3,367	86
A	**456**	**11**	526	14
BBB and below	**11**	**-**	12	-
Total	**4,134**	**100**	3,905	100

Of these, approximately $1,025 million (2017: $1,001 million) is secured directly as follows, reducing the credit risk:

- deposits held in trust: $23 million (2017: $144 million);
- letters of credit: $1,000 million (2017: $854 million); and
- loss deposits: $2 million (2017: $3 million).

An ageing analysis for reinsurance recoveries on paid claims is provided below:

	NOT OVERDUE		OVERDUE		TOTAL
		<30 days	30-120 days	>120 days	
	$m	$m	$m	$m	$m
2018					
Reinsurance recoveries on paid claims	**70**	**8**	**3**	**11**	**92**
2017					
Reinsurance recoveries on paid claims	128	11	44	59	242

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. IAG is also exposed to the credit risk associated with brokers and other intermediaries when premium is collected via these intermediaries. IAG'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 IAG's limited exposure:

	NOT OVERDUE		OVERDUE		TOTAL
		<30 days	30-120 days	>120 days	
	$m	$m	$m	$m	$m
2018					
Premium receivable	**2,981**	**315**	**278**	**48**	**3,622**
Provision for impairment	**(3)**	**(3)**	**(7)**	**(20)**	**(33)**
	2,978	**312**	**271**	**28**	**3,589**
2017					
Premium receivable	2,771	308	273	50	3,402
Provision for impairment	(5)	(3)	(7)	(24)	(39)
	2,766	305	266	26	3,363

III. Liquidity risk

IAG'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). IAG 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.

a. OUTSTANDING CLAIMS LIABILITY AND INVESTMENTS

Underwriting insurance contracts expose IAG 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 claim 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	
	2018	2017	**2018**	2017
	$m	$m	**$m**	$m
Floating interest rate (at call)	**-**	-	**755**	944
Within 1 year or less	**2,446**	2,776	**1,607**	2,255
Within 1 to 2 years	**920**	1,182	**773**	880
Within 2 to 5 years	**1,200**	1,601	**2,656**	2,550
Over 5 years	**422**	554	**3,377**	3,739
Total	**4,988**	6,113	**9,168**	10,368

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
2018							
Principal repayments(1)	**1,974**	**-**	**-**	**-**	**1,020**	**954**	**1,974**
Contractual interest payments(1)		**91**	**91**	**274**	**-**	**-**	**456**
Total contractual undiscounted payments		**91**	**91**	**274**	**1,020**	**954**	**2,430**
2017							
Principal repayments(1)	1,638	-	-	-	684	954	1,638
Contractual interest payments(1)		73	73	220	-	-	366
Total contractual undiscounted payments		73	73	220	684	954	2,004

(1) 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 Note 4.1. 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

IAG's 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.

IAG has a documented description of the capital management process (ICAAP) and reports annually on the operation of the ICAAP to the Board, together with a forward-looking estimate of expected capital utilisation (as represented in IAG's Capital Plan) and capital resilience (ICAAP Annual Report). Adequacy of IAG'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 IAG 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 IAG that carry on insurance business in Australia are registered with APRA and are subject to APRA's Prudential Standards. It is IAG's policy to ensure that each of the licenced insurers maintains an adequate capital position.

IAG's long-term target capital ranges set out below remain unchanged:

- a total regulatory capital position equivalent to 1.4 to 1.6 times the PCA, compared to a regulatory requirement of 1.0 times; and
- Common Equity Tier 1 capital of 0.9 to 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	**2018**	2017
	$m	$m
Common Equity Tier 1 capital (CET1 capital)	**3,114**	2,888
Additional Tier 1 capital	**624**	679
Total Tier 1 capital	**3,738**	3,567
Tier 2 capital	**1,280**	959
Total regulatory capital	**5,018**	4,526
Total PCA	**2,468**	2,661
PCA multiple	**2.03**	1.70
CET1 multiple	**1.26**	1.09

At 30 June 2018, IAG's Insurance Concentration Risk Charge (ICRC) from a catastrophe event was $169 million (2017: $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 the ongoing strength and security of IAG, 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 design, catastrophe exposure, investment strategy, profit margins and capital structure, are all assessed using dynamic financial analysis modelling.

An important influence on IAG's capital level is the payment of dividends. IAG targets a dividend payout ratio, measured as a proportion of cash earnings, within a range approved by the Board (refer to Note 4.4).

b. CAPITAL COMPOSITION

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

CAPITAL MIX	**Target**	**2018**	2017
	%	%	%
Ordinary equity less goodwill and intangible assets	**60-70**	**65.7**	68.1
Interest-bearing liabilities – hybrid securities and debt	**30-40**	**34.3**	31.9
Total capitalisation		**100.0**	100.0

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. IAG 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, Fraud and Business Continuity Frameworks and policies are in place as are various other operational risk policies.

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

G. REGULATORY RISK AND COMPLIANCE

Regulatory Risk and Compliance is defined as failure or inability to comply with applicable laws, regulations or codes excluding failure of staff to adhere to internal policies/procedures and meeting contractual obligations. IAG 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.

IAG acknowledges that a Royal Commission is the highest level of public inquiry in Australia. The Board, together with Management, is committed to cooperating fully with the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (the Royal Commission). IAG has provided submissions to the Royal Commission, and resources and expertise have been allocated to ensure any request arising from the Royal Commission is addressed with the appropriate consideration and importance. While it is likely the Royal Commission will make recommendations that could impact the broader financial services landscape in Australia, it remains too early to predict the nature and extent of these changes and any consequential impact these may have for IAG's businesses.

4. CAPITAL STRUCTURE

SECTION INTRODUCTION

This section provides disclosures on the capital structure of IAG, 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 IAG – 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. IAG 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. IAG 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

			2018		2017	
Final Maturity Date	**Principal Amount**	Section	**Carrying Value $m**	**Fair Value $m**	Carrying Value $m	Fair Value $m
A. COMPOSITION						
I. Capital nature(1)						
a. ADDITIONAL TIER 1 REGULATORY CAPITAL(2)						
Reset exchangeable securities						
No fixed date	$550 million	B. I	**550**	**565**	550	569
Capital notes						
No fixed date	$404 million	B. II	**404**	**423**	404	431
b. TIER 2 REGULATORY CAPITAL						
AUD subordinated convertible term notes						
19 March 2040	$350 million	B. III	**350**	**354**	350	356
15 June 2044	$350 million	B. IV	**350**	**353**	-	-
			700		350	
NZD subordinated convertible term notes(3)						
15 June 2043	NZ$350 million	B. V	**320**	**332**	334	337
II. Operational nature						
Other interest-bearing liabilities			**-**	**-**	2	2
Less: capitalised transaction costs			**(14)**		(16)	
			1,960		1,624	

(1) Capital instruments above cannot be reconciled to the regulatory capital section of Note 3.1 due to APRA transitional arrangements.

(2) 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.

(3) At the reporting date, the Company recognised accrued interest of $1 million (2017: $1 million) which is presented within trade and other payables.

B. SIGNIFICANT TERMS AND CONDITIONS

I. 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;
- all remain outstanding as at the reporting date;
- non-cumulative floating rate distribution payable quarterly;
- distribution rate equals the sum of the three-month bank bill swap rate (BBSW) plus a margin of 4.00% per annum multiplied by (1-tax rate);
- if the distributions are not fully franked, the distribution rate is increased to compensate holders for the unfranked portion of the distribution, subject to no payment conditions existing;
- 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).

II. Capital notes

- face value of $404 million and issued by the Company on 22 December 2016;
- all remain outstanding as at the reporting date;
- non-cumulative floating rate distribution payable quarterly;
- distribution rate equals the sum of three-month bank bill swap rate (BBSW) plus a margin of 4.70% per annum multiplied by (1-tax rate);
- if the distributions are not fully franked, the distribution rate is increased to compensate holders for the unfranked portion of the distribution, subject to no payment conditions existing;
- 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 distribution payment date;
- IAG may convert, redeem or resell capital notes on 15 June 2023, or upon occurrence of certain events, subject to APRA approval;
- the capital notes are scheduled for conversion into a variable number of ordinary shares of the Company (subject to a maximum number of 140.6 million shares) on 16 June 2025 and at each subsequent distribution payment date provided the mandatory conversion conditions are satisfied; and
- the capital notes must be converted into a variable number of IAG ordinary shares (subject to a maximum of 351.1 million shares) or written-off if APRA determines the Company to be non-viable.

III. AUD subordinated convertible term notes due 2040

- face value of $350 million and issued by Insurance Australia Limited (IAL), a wholly-owned subsidiary of the Company on 19 March 2014;
- all remain outstanding as at the reporting date;
- 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 notes at face value between 19 March 2019 and 19 March 2020 and for certain tax and regulatory events (in each case subject to APRA's prior written approval);
- the notes can be converted into a variable number of ordinary shares of the Company (subject to a maximum of 128.0 million shares) at the option of holders from and including 19 March 2022 and at each subsequent interest payment date and the maturity date of 19 March 2040; and
- the notes must be converted into a variable number of ordinary shares of the Company (subject to a maximum of 319.9 million shares) or written-off if APRA determines the Company to be non-viable.

IV. AUD subordinated convertible term notes due 2044

- face value of $350 million and issued by the Company on 29 March 2018;
- all remain outstanding as at the reporting date;
- floating interest rate equal to the three-month bank bill swap rate (BBSW) plus a margin of 2.10% per annum is payable quarterly;
- the notes mature on 15 June 2044 unless converted or redeemed earlier, subject to rights of conversion or redemption;
- IAG has an option to redeem the notes at face value between 15 June 2024 and 15 June 2025 and for certain tax and regulatory events (in each case subject to APRA's prior written approval);
- the notes can be converted into a variable number of ordinary shares of the Company (subject to a maximum of 88.7 million shares) at the option of holders from and including 15 June 2027 and at each subsequent interest payment date and the maturity date of 15 June 2044; and
- the notes must be converted into a variable number of ordinary shares of the Company (subject to a maximum of 221.8 million shares) or written-off if APRA determines the Company to be non-viable.

V. 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 unless converted or redeemed earlier, subject to rights of conversion or redemption;
- IAG has an option to redeem the notes at face value between 15 June 2022 and 15 June 2023, and for certain tax and regulatory events (in each case subject to APRA's prior written approval);
- if the notes are not redeemed on 15 June 2022, the interest rate will become the applicable three-month bank bill benchmark rate (BKBM) plus a margin of 2.60% per annum;
- the notes can be converted into a variable number of ordinary shares of the Company (subject to a maximum of 114.0 million 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 ordinary shares of the Company (subject to a maximum of 284.9 million 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

	2018 Number of shares in millions	2017 Number of shares in millions	**2018** $m	2017 $m
A. SHARE CAPITAL				
Balance at the beginning of the financial year	**2,367**	2,431	**7,082**	7,275
Off-market share buy-back, including transaction costs	**-**	(64)	**-**	(193)
Balance at the end of the financial year	**2,367**	2,367	**7,082**	7,082

B. STRATEGIC RELATIONSHIP WITH BERKSHIRE HATHAWAY (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 terms of the Subscription Agreement were released to the ASX on 16 June 2015 (attached to the Appendix 3B on that date).

I. 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 IAG. 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 3 million (2017: 3 million) at an average price per share of $6.20 (2017: $5.47).

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 and Monte Carlo simulation. 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). 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 ordinary shares of the Company 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

	2018 cents	2017[3] cents
A. REPORTING PERIOD VALUES		
Continuing and discontinued operations		
Basic earnings per ordinary share[1]	**39.06**	39.03
Diluted earnings per ordinary share[2]	**38.30**	37.72
Continuing operations		
Basic earnings per ordinary share[1]	**40.08**	39.41
Diluted earnings per ordinary share[2]	**39.26**	38.07

(1) 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.

(2) 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.

(3) Prior year comparatives have been re-presented due to the discontinued operations. Refer to Note 6.5.

	2018 $m	2017 $m
B. RECONCILIATION OF EARNINGS USED IN CALCULATING EARNINGS PER SHARE		
Profit attributable to shareholders of the Parent which is used in calculating basic and diluted earnings per share	**923**	929
Finance costs of convertible securities, net of tax	**38**	37
Profit attributable to shareholders of the Parent which is used in calculating diluted earnings per share	**961**	966
Profit from continuing operations attributable to shareholders of the Parent	**947**	938
Loss from discontinued operations attributable to shareholders of the Parent	**(24)**	(9)

	2018 Number of shares in millions	2017 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	**2,363**	2,380
Weighted average number of dilutive potential ordinary shares relating to:		
Convertible securities	**142**	175
Unvested share-based remuneration rights supported by treasury shares held in trust	**4**	6
	2,509	2,561

NOTE 4.4 DIVIDENDS

	2018		2017	
	Cents per share	**$m**	Cents per share	$m
A. ORDINARY SHARES				
2018 interim dividend paid on 29 March 2018 (2017: 2017 interim dividend) fully franked at 30%[1]	**14.0**	**330**	13.0	307
Dividend component of off-market share buy-back fully franked at 30%	**-**	**-**	192.0	123
2017 final dividend paid on 9 October 2017 (2017: 2016 final dividend) fully franked at 30%[2]	**20.0**	**473**	13.0	316
		803		746
B. DIVIDEND NOT RECOGNISED AT REPORTING DATE				
2018 final dividend (2017: 2017 final dividend) fully franked at 30% to be paid on 27 September 2018[2]	**20.0**	**474**	20.0	474

(1) Of the total 2018 interim dividend declared of $331 million, right and entitlement of $1 million (2017 interim dividend: $1 million) to dividends on unallocated treasury shares was waived during the year by the trustee of the IAG Share and Rights Plans Trust.

(2) Of the total 2017 final dividend declared of $474 million, right and entitlement of $1 million (2016 final dividend: nil) to dividends on unallocated treasury shares was waived during the year by the trustee of the IAG Share and Rights Plans Trust.

	2018	2017
	$m	$m
C. DIVIDEND FRANKING AMOUNT		
Franking credits available for subsequent financial periods based on a tax rate of 30%	**100**	115

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, immediately after payment of the final dividend, will have no further franking credits available for distribution.

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 ordinary shares of the Company. The price of DRP shares is the VWAP, 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 2018 interim dividend paid on 29 March 2018 was settled with the on-market purchase of 6.6 million shares priced at $8.09 per share (based on a VWAP for 10 trading days from 26 February 2018 to 9 March 2018 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 capital notes or reset exchangeable securities, unless certain actions are taken by IAG. For further details, refer to Note 4.1.

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

	2018			2017		
	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	**1,223**	**11**	**(15)**	922	14	(3)
II. Investment-related derivatives (derivatives without hedge accounting applied)						
Bond futures	**2,559**	**-**	**-**	2,913	-	-
Share price index futures	**(28)**	**-**	**-**	(44)	-	-
Forward foreign exchange contracts	**3,394**	**-**	**(53)**	2,827	29	-
Options	**-**	**-**	**-**	(48)	3	(1)
III. Treasury-related derivatives (derivatives without hedge accounting applied)						
Forward foreign exchange contracts	**754**	**6**	**(8)**	1,160	11	(4)
Interest rate swaps	**320**	**1**	**-**	334	-	(5)

All derivative contracts are expected to be settled within 12 months, except for interest rate swaps which mature in more than three 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 IAG'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, with finite useful life intangible assets also subject to amortisation. 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 prima facie 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, IAG recognises a deferred tax asset in relation to the earthquake losses incurred by its New Zealand operations since the 2011 financial year. This asset is expected to 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
2018						
A. COMPOSITION						
Cost	**2,870**	**872**	**157**	**192**	**125**	**4,216**
Accumulated amortisation and impairment	**-**	**(743)**	**(122)**	**(131)**	**(42)**	**(1,038)**
Net foreign exchange movements	**5**	**(8)**	**1**	**4**	**3**	**5**
Balance at the end of the financial year	**2,875**	**121**	**36**	**65**	**86**	**3,183**
B. RECONCILIATION OF MOVEMENTS						
Balance at the beginning of the financial year	**2,974**	**99**	**66**	**90**	**103**	**3,332**
Additions acquired and developed	**-**	**81**	**-**	**3**	**-**	**84**
Disposal through sale of businesses	**(15)**	**-**	**-**	**(1)**	**-**	**(16)**
Net movement in discontinued operations	**-**	**2**	**-**	**-**	**(1)**	**1**
Transfers to assets held for sale	**(62)**	**(3)**	**-**	**-**	**-**	**(65)**
Amortisation	**-**	**(58)**	**(29)**	**(25)**	**-**	**(112)**
Amortisation and impairment charged to discontinued operations	**-**	**(1)**	**-**	**-**	**(14)**	**(15)**
Net foreign exchange movements	**(22)**	**1**	**(1)**	**(2)**	**(2)**	**(26)**
Balance at the end of the financial year	**2,875**	**121**	**36**	**65**	**86**	**3,183**
2017						
C. COMPOSITION						
Cost	2,947	798	157	190	125	4,217
Accumulated amortisation and impairment	-	(690)	(93)	(105)	(29)	(917)
Net foreign exchange movements	27	(9)	2	5	7	32
Balance at the end of the financial year	2,974	99	66	90	103	3,332
D. RECONCILIATION OF MOVEMENTS						
Balance at the beginning of the financial year	2,982	132	96	93	107	3,410
Additions acquired and developed	20	22	-	21	-	63
Disposal through sale of businesses	(26)	-	(1)	-	-	(27)
Amortisation	-	(54)	(29)	(24)	(4)	(111)
Net foreign exchange movements	(2)	(1)	-	-	-	(3)
Balance at the end of the financial year	2,974	99	66	90	103	3,332

E. IMPAIRMENT

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 amounts of intangible assets with finite useful lives are reviewed at each reporting date by determining whether there is an indication that the carrying values 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:

	2018	2017
	$m	$m
Australian Consumer division	**756**	771
Australian Business division	**1,479**	1,479
New Zealand	**640**	667
Asia	**-**	57
	2,875	2,974

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. The forecast durations reflect the insurance business life cycle and the growth trajectories of portfolios within each of the established and emerging markets.
- Terminal value is calculated using a perpetuity growth formula based on the cash flow forecast at the end of the relevant valuation forecast period, 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 IAG's impairment assessment for significant CGUs as at 30 June 2018 are: Australian Consumer division 4.8% (2017: 4.5%), Australian Business division 4.0% (2017: 4.5%) and New Zealand 3.7% (2017: 3.5%).
- Discount rates reflect a beta and equity risk premium appropriate to IAG, with risk adjustments for individual segments and countries where applicable. The post-tax discount rates used for significant CGUs as at 30 June 2018 are: Australian Consumer division 9.5% (2017: 9.7%), Australian Business division 9.5% (2017: 9.7%) and New Zealand 10.1% (2017: 10.3%).

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 represent 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

	2018 $m	2017* $m
A. INCOME TAX EXPENSE		
Current tax	393	350
Deferred tax	(11)	14
Under/(over) provided in prior year	2	(36)
Income tax expense	384	328
Deferred income tax expense/(credit) included in income tax comprises		
Decrease in deferred tax assets	5	55
Decrease in deferred tax liabilities	(16)	(41)
	(11)	14
B. RECONCILIATION OF PRIMA FACIE TAX TO INCOME TAX EXPENSE		
Profit for the year before income tax	1,410	1,343
Income tax calculated at 30% (2017: 30%)	423	403
Amounts which are not deductible/(taxable) in calculating taxable income		
Difference in tax rate	(48)	(31)
Impairment not subject to income tax	11	-
Rebatable dividends	(4)	(5)
Interest on capital notes and convertible preference shares	6	6
Other	(6)	(9)
Income tax expense applicable to current year	382	364
Adjustment relating to prior year	2	(36)
Income tax expense attributable to profit for the year from continuing operations after impact of tax consolidation	384	328
C. DEFERRED TAX ASSETS		
I. Composition		
a. AMOUNTS RECOGNISED IN PROFIT		
Property and equipment	106	88
Employee benefits	78	85
Insurance provisions	113	119
Investments	30	31
Provisions	6	4
Tax losses	396	433
	729	760
b. AMOUNTS RECOGNISED DIRECTLY IN OTHER COMPREHENSIVE INCOME		
Defined benefit superannuation plans	11	12
	740	772
c. AMOUNTS SET-OFF AGAINST DEFERRED TAX LIABILITIES	(196)	(227)
	544	545
II. Reconciliation of movements		
Balance at the beginning of the financial year	772	861
Charged to profit or loss	(5)	(55)
Charged to equity	(1)	(11)
Adjustments relating to prior year	11	(23)
Transfers to assets held for sale	(25)	-
Charged to discontinued operations	2	1
Foreign exchange differences	(14)	(1)
Balance at the end of the financial year prior to set-off	740	772

* Prior year comparatives have been re-presented due to the discontinued operations. Refer to Note 6.5.

III. Tax losses

The deferred tax assets from tax losses primarily relate to those incurred in IAG's New Zealand business as a result of the Christchurch earthquake events that occurred in 2010 and 2011 and the 2016 Kaikoura earthquake. In the context of the New Zealand Income Tax Act, tax losses carried forward do not expire after a particular period and remain available to offset against future income tax liabilities, provided the 49% continuity of shareholding requirement is met at the listed holding company level.

	2018 $m	2017* $m
D. DEFERRED TAX LIABILITIES		
I. Composition		
a. AMOUNTS RECOGNISED IN PROFIT		
Investments	**67**	80
Intangible assets	**18**	26
Other	**108**	114
	193	220
b. AMOUNTS RECOGNISED DIRECTLY IN OTHER COMPREHENSIVE INCOME		
Hedges	**3**	7
	196	227
c. AMOUNTS SET-OFF AGAINST DEFERRED TAX ASSETS	**(196)**	(227)
	-	-
II. Reconciliation of movements		
Balance at the beginning of the financial year	**227**	258
Credited to profit or loss	**(16)**	(41)
(Credited)/charged to equity	**(4)**	2
Adjustments relating to prior year	**-**	8
Transfers to liabilities held for sale	**(12)**	-
Charged to discontinued operations	**1**	-
Balance at the end of the financial year prior to set-off	**196**	227

* Prior year comparatives have been re-presented due to the discontinued operations. Refer to Note 6.5.

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

The Company 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. The Company is the head entity within the tax-consolidated group.

NOTE 5.3 PROVISIONS

	2018	2017*
	$m	$m
A. EMPLOYEE BENEFITS		
I. Expense recognised in the consolidated statement of comprehensive income		
Defined contribution superannuation plans	**106**	111
Defined benefit superannuation plans	**6**	1
Share-based remuneration	**32**	22
Salaries and other employee benefits expense	**1,472**	1,464
	1,616	1,598
II. Provision recognised on the consolidated balance sheet		
Annual leave	**87**	92
Long service leave	**88**	91
Cash-based incentive arrangements	**97**	98
Defined benefit superannuation plans	**17**	18
Executive performance rights	**16**	-
Other employee benefits	**4**	7
	309	306

* Prior year comparatives have been re-presented due to the discontinued operations. Refer to Note 6.5.

The employee benefits provision includes $80 million (2017: $76 million) which is expected to be settled after more than 12 months from reporting date.

	2018	2017
	$m	$m
B. RESTRUCTURING PROVISION		
Balance at the beginning of the financial year	**23**	26
Additions	**29**	25
Amounts settled	**(34)**	(28)
Balance at the end of the financial year	**18**	23

The provision primarily comprises restructuring costs in respect of the operating model changes in Australia. All provision outstanding at the reporting date is expected to be settled within 12 months (2017: 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. Under the plan, eligible employees have the capacity to earn an incentive, calculated as a proportion of their base salary, which is paid in cash each year. 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 Group, 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. Executive performance rights

Executive performance rights (EPRs) issued after July 2013 are indeterminate rights in that they can be cash-settled or equity-settled. The choice of settlement is with the Board. Liabilities for the EPRs that are cash-settled are recognised as employee benefit expense over the relevant service period. The liabilities are remeasured to fair value at each reporting date and are presented as employee benefit obligations in the balance sheet.

VI. 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 DETAILS OF SUBSIDIARIES

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

	COUNTRY OF INCORPORATION/ FORMATION	EXTENT OF BENEFICIAL INTEREST IF NOT 100%	
		2018	2017
		%	%
A. ULTIMATE PARENT			
Insurance Australia Group Limited	Australia		
B. SUBSIDIARIES			
I. Australian general insurance operations			
CGU Insurance Limited(1),(3)	Australia		
CGU-VACC Insurance Limited(1),(2)	Australia		
HBF Insurance Pty Ltd(1),(2)	Australia		
IAG Re Australia Limited(1),(2)	Australia		
Insurance Australia Limited	Australia		
Insurance Manufacturers of Australia Pty Limited	Australia	**70.00**	70.00
Mutual Community General Insurance Proprietary Limited(1),(2)	Australia	**-**	
Swann Insurance (Aust) Pty Ltd(1),(3)	Australia		
WFI Insurance Limited(1),(3)	Australia		
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 insurance operations			
AAA Assurance Corporation(4)	Vietnam	**73.07**	63.17
IAG Re Labuan (L) Berhad	Malaysia		
IAG Re Singapore Pte Ltd	Singapore		
PT Asuransi Parolamas(4)	Indonesia	**80.00**	80.00
Safety Insurance Public Company Limited(4)	Thailand	**98.61**	98.61
IV. Corporate operations			
IAG Finance (New Zealand) Limited	Australia		

(1) On 1 August 2017, all the insurance assets and liabilities of these entities were transferred into a related business, Insurance Australia Limited.

(2) Mutual Community General Insurance Propriety Limited was deregistered in April 2018, and CGU-VACC Insurance Limited, HBF Insurance Pty Ltd and IAG Re Australia Limited were deregistered in July 2018.

(3) These entities are targeted for deregistration.

(4) On 19 June 2018, IAG announced the sale of its businesses in Thailand, Vietnam and Indonesia. Refer to Note 6.5.

NOTE 6.2 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 IAG's beneficial interest is 70%.

	INSURANCE MANUFACTURERS OF AUSTRALIA PTY LIMITED	
	2018	2017
	$m	$m
I. Summarised statement of comprehensive income		
Net premium revenue	**3,085**	2,935
Profit after tax attributable to the Parent entity	**186**	179
Profit after tax attributable to non-controlling interest	**79**	77
Other comprehensive income	**1**	3
Total comprehensive income	**266**	259
II. Summarised balance sheet		
Total assets	**4,136**	3,791
Total liabilities	**(3,237)**	(3,039)
Net assets	**899**	752
Carrying amount of non-controlling interest	**270**	226
III. Summarised cash flow		
Net cash flows from operating and investing activities	**34**	217
Dividends paid to other IAG entities	**(83)**	(163)
Dividends paid to non-controlling interest	**(36)**	(68)
Total net cash flows	**(85)**	(14)

NOTE 6.3 INVESTMENT IN JOINT VENTURE AND ASSOCIATES

A. INTERESTS IN JOINT VENTURE AND ASSOCIATES

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

	COUNTRY OF INCORPORATION/ FORMATION	PRINCIPAL ACTIVITY	CARRYING VALUE		OWNERSHIP INTEREST	
			2018	2017	**2018**	2017
			$m	$m	**%**	%
AmGeneral Holdings Berhad (AmGeneral)	Malaysia	Insurance underwriting	**392**	353	**49.00**	49.00
SBI General Insurance Company Limited (SBI General)	India	Insurance underwriting	**139**	138	**26.00**	26.00
Other			**26**	14		
			557	505		

During the reporting period, IAG has undertaken an assessment of the recoverable amount of its Asian assets. In aggregate, this has given rise to a write-down totalling $50 million. The write-down reflects updated assumptions and forecasts in relation to the current operating landscape affecting both the investment in associates and select identifiable intangibles. The related expense has been presented within 'Fee-based, corporate and other expenses' and 'Loss after income tax from discontinued operations' in the statement of comprehensive income. Where applicable, in addition to the impact of the write-down, the movement in carrying values shown above also includes the net impact of current period earnings and changes in exchange rates. The post-tax discount rates applied for valuation purposes have remained unchanged since 30 June 2017.

B. SUMMARISED FINANCIAL INFORMATION

Summarised financial information of material 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 2018.

	2018		2017	
	AmGeneral Holdings Berhad $m	**SBI General Insurance Company Limited $m**	AmGeneral Holdings Berhad $m	SBI General Insurance Company Limited $m
I. Summarised statement of comprehensive income				
Revenue	**519**	**784**	543	580
Profit after tax	**74**	**79**	53	30
Other comprehensive (expense)/income	**(1)**	**-**	1	-
Total comprehensive income	**73**	**79**	54	30
II. Summarised balance sheet				
Total assets	**1,982**	**1,185**	1,643	957
Total liabilities	**(1,198)**	**(887)**	(1,024)	(736)
Net assets as at reporting date	**784**	**298**	619	221
IAG's ownership interest	**384**	**77**	303	58
Other adjustments*	**8**	**62**	50	80
Carrying value as at 30 June	**392**	**139**	353	138

* 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

IAG'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 IAG 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 IAG. 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 IAG 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 IAG.

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 6.4 PARENT ENTITY DISCLOSURES

The ultimate Parent entity in the Group 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	
	2018	2017
	$m	$m
A. FINANCIAL RESULTS		
Profit for the year	**1,428**	467
Total comprehensive income for the year, net of tax	**1,428**	467
B. FINANCIAL POSITION		
Current assets	**12**	16
Total assets	**10,789**	12,221
Current liabilities	**159**	171
Total liabilities	**1,563**	3,619
C. SHAREHOLDERS' EQUITY		
Share capital	**7,082**	7,082
Retained earnings	**2,144**	1,520
Total shareholders' equity	**9,226**	8,602

The Group's consolidation of its nine Australian insurance licences into two, which occurred on 1 August 2017, had the combined effect on the Parent entity of a reduction in both non-current assets and non-current liabilities resulting from the return of capital from its seven subsidiary entities whose operations ceased on completion of the transfer of their insurance assets and liabilities to a related entity, Insurance Australia Limited. The restructure has also caused the upstreaming of material dividends, which largely explains the increase in the profit for the Parent entity during the year. The consolidation of insurance licences had no impact to the Group's consolidated financial performance or position.

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 (2017: nil).

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 (2017: nil).

NOTE 6.5 DISCONTINUED OPERATIONS

On 19 June 2018, IAG announced it had entered into a sale agreement with Tokio Marine & Nichido Fire Insurance Co., Ltd (Tokio Marine) for IAG's operations in Thailand and Indonesia. Separate to the transactions with Tokio Marine, IAG has reached an agreement to sell its interest in AAA Assurance Corporation, based in Vietnam. All transactions are expected to conclude in the financial year ending 30 June 2019, subject to regulatory approvals or notifications. As a result of the sale agreements, these consolidated Asian businesses have been identified as discontinued operations in the current financial year and comparative figures have been re-presented accordingly.

	2018	2017
	$m	$m
A. RESULTS OF DISCONTINUED OPERATIONS		
Revenue	**493**	510
Expenses	**(516)**	(519)
Loss before income tax	**(23)**	(9)
Income tax expense	**(2)**	(1)
Loss for the year from discontinued operations	**(25)**	(10)
Other comprehensive income, net of tax	**1**	1
Total comprehensive loss from discontinued operations	**(24)**	(9)
Loss for the year attributable to shareholders of the Parent	**(24)**	(9)
Loss for the year attributable to non-controlling interests	**(1)**	(1)
Loss for the year from discontinued operations	**(25)**	(10)
Total comprehensive loss for the year attributable shareholders of the Parent	**(23)**	(8)
Total comprehensive loss for the year attributable non-controlling interests	**(1)**	(1)
Total comprehensive loss from discontinued operations	**(24)**	(9)
B. EARNINGS PER SHARE FROM DISCONTINUED OPERATIONS		
Basic earnings per share, from discontinued operations – cents per share	**(1.02)**	(0.38)
Diluted earnings per share, from discontinued operations – cents per share	**(0.96)**	(0.35)
C. CASH FLOW FROM DISCONTINUED OPERATIONS		
Net cash flows from operating activities	**(47)**	7
Net cash flows from investing activities	**34**	16
Net cash flows from financing activities	**(4)**	(4)
Net cash flows for the year from discontinued operations	**(17)**	19

D. ASSETS AND LIABILITIES HELD FOR SALE

Assets and liabilities related to the Group's consolidated businesses in Thailand, Vietnam and Indonesia, that have been classified as held for sale are included in the table below:

	2018
	$m
Cash held for operational purposes	32
Investments	282
Trade and other receivables	72
Reinsurance and other recoveries on outstanding claims	52
Deferred insurance expenses	111
Other assets	41
Goodwill and intangible assets	65
Total assets held for sale	655
Trade and other payables	65
Outstanding claims liability	157
Unearned premium liability	206
Other liabilities	16
Total liabilities held for sale	444

7. UNRECOGNISED ITEMS

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 IAG's performance or financial position and are 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 IAG'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 IAG'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.

IAG 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 IAG's balance sheet had a fair value as at the reporting date of $335 million (2017: $335 million).

NOTE 7.2 COMMITMENTS

	2018	2017
	$m	$m
A. OPERATING LEASE COMMITMENTS		
I. Property		
Due within 1 year	**84**	120
Due within 1 to 2 years	**89**	104
Due within 2 to 5 years	**237**	257
Due after 5 years	**559**	642
	969	1,123
II. Equipment		
Due within 1 year	**25**	31
Due within 1 to 2 years	**13**	22
Due within 2 to 5 years	**32**	6
	70	59
	1,039	1,182

B. RECOGNITION AND MEASUREMENT

Certain properties, motor vehicles and computer equipment are leased under non-cancellable operating leases. Most leases are subject to annual review 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 events 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 2018. These include:

- On 15 August 2018, the Board determined to pay a final dividend of 20.0 cents per share, 100% franked. The dividend will be paid on 27 September 2018. The DRP will operate by acquiring shares on-market for participants with no discount applied.
- On 15 August 2018, IAG announced a capital management initiative amounting to 25.0 cents per ordinary share, or $592 million, expected to comprise a 19.5 cents capital return and a 5.5 cents fully franked special dividend, with a share consolidation which would reduce IAG's ordinary issued shares by approximately 2.4% and preserve consistency of EPS calculation. The capital return and share consolidation are subject to shareholder approval at the AGM, and IAG has made payment of the special dividend conditional on approval being obtained. If approved, the capital management initiative is expected to occur on or around 26 November 2018.

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 IAG's performance or financial position.

NOTE 8.1 NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT

	2018 $m	2017 $m
A. COMPOSITION OF CASH AND CASH EQUIVALENTS		
Cash held for operational purposes	**448**	424
Cash and short-term money held in investments	**753**	1,056
Cash and cash equivalents in discontinued operations	**144**	-
Cash and cash equivalents	**1,345**	1,480
B. RECONCILIATION OF PROFIT FOR THE YEAR TO NET CASH FLOWS FROM OPERATING ACTIVITIES		
Profit for the year	**1,001**	1,005
I. Non-cash items		
Net gains on investments	**(31)**	(76)
Amortisation of intangible assets and impairment	**161**	111
Depreciation of property and equipment	**58**	52
Other non-cash items	**(1)**	11
II. Movement in operating assets and liabilities		
Insurance assets	**(1,335)**	(577)
Insurance liabilities	**(70)**	(411)
Net movement in other operating assets and liabilities	**174**	352
Net movement in tax assets and liabilities	**(9)**	210
Provisions	**(1)**	(41)
Net cash flows from operating activities	**(53)**	636

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 IAG in relation to their involvement in the activities within the Group.

	2018 $000	2017 $000
Short-term employee benefits	**14,098**	19,074
Post-employment benefits	**326**	533
Other long-term benefits	**89**	145
Termination benefits	**810**	600
Share-based payments	**8,769**	8,974
	24,092	29,326

The reduction in KMP compensation compared to the prior financial year reflects the lower number of individuals that met the refined KMP definition, as outlined in the Remuneration Report.

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 on behalf of specific individual Non-Executive Directors and Executives and the terms of the contract specifically prohibit the disclosure of the premium paid. Insurance products provided by IAG 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

	2018	2017
	$000	$000
A. KPMG		
Audit of the financial statements prepared for the Parent and subsidiaries	**7,762**	8,098
Audit of statutory returns in accordance with regulatory requirements	**585**	1,059
Other assurance services	**121**	126
Advisory services	**2,620**	1,233
Total remuneration of auditors	**11,088**	10,516

In relation to the Royal Commission, IAG has engaged external legal advisors. As part of this engagement, the legal advisors have appointed IAG's auditors, KPMG, to provide project administration, documentation and preparation assistance, process and control review and testing and general assistance. During the 2018 financial year, the costs incurred for this engagement relating to KPMG totalled $1,503 thousand, which have been presented within advisory services costs above.

NOTE 8.4 NET TANGIBLE ASSETS

	2018	2017
	$	$
Net tangible assets per ordinary share	**1.47**	1.36

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 new Australian Accounting Standards and Interpretations applicable for the current reporting year are given below. The adoption of these standards did not have a material financial impact:

TITLE	DESCRIPTION
AASB 2016-1	Amendments to Australian Accounting Standards – Recognition of Deferred Tax Assets for Unrealised Losses [AASB 112]
AASB 2016-2	Amendments to Australian Accounting Standards – Disclosure Initiative: Amendments to AASB 107
AASB 2017-2	Amendments to Australian Accounting Standards – Further Annual Improvements 2014-2016 Cycle
AASB 1048	Interpretation of Standards

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	A
AASB 17	Insurance	1 January 2021	B
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 2014-7	Amendments to Australian Accounting Standards arising from AASB 9 (December 2014)	1 January 2018	A
AASB 2014-10	Amendments to Australian Accounting Standards – Sale or Contribution of Assets between an Investor and its Associate	1 January 2022	A
AASB 2015-8	Amendments to Australian Accounting Standards – Effective Date of AASB 15	1 January 2022	A
AASB 2015-10	Amendments to Australian Accounting Standards – Effective Date of Amendments to AASB 10 and AASB 128	1 January 2022	A
AASB 2016-3	Amendments to Australian Accounting Standards – Clarifications to AASB 15	1 January 2018	A

TITLE	DESCRIPTION	OPERATIVE DATE	NOTE
AASB 2016-5	Classification and Measurement of Share–based Payment Transactions	1 January 2018	A
AASB 2016-6	Applying AASB 9 Financial Instruments with AASB 4 Insurance Contracts	1 January 2018	A
AASB 2017-3	Amendments to Australian Accounting Standards – Clarifications to AASB 4	1 January 2018	A
AASB 2017-6	Amendments to Australian Accounting Standards – Prepayment Features with Negative Compensation	1 January 2019	A
AASB 2017-7	Amendments to Australian Accounting Standards – Long-term Interests in Associates and Joint Ventures	1 January 2019	A
AASB 2018-1	Amendments to Australian Accounting Standards – Annual Improvements 2015–2017 Cycle	1 January 2019	A
AASB 2018-2	Amendments to Australian Accounting Standards – Plan Amendment, Curtailment or Settlement	1 January 2019	A
AASB Interpretation 22	Foreign Currency Transactions and Advance Consideration	1 January 2018	A
AASB Interpretation 23	Uncertainty over Income Tax Treatments, and relevant amending standards	1 January 2019	A
Conceptual Framework	Amendments to standards to apply the new definition and recognition criteria in the Conceptual Framework for Financial Reporting	1 January 2020	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.

The Australian Accounting Standards and amendments detailed in the table above are not mandatory for IAG until the operative dates stated, however, early adoption is permitted. IAG currently plans to apply the standards and amendments detailed above for the reporting periods beginning on or after the operative dates set out above.

AASB 9 was issued during 2014 and will replace existing accounting requirements for financial instruments. Currently, IAG's investments are designated as at fair value through profit or loss on initial recognition and are subsequently remeasured to fair value at each reporting date, reflecting the business model applied by IAG to manage and evaluate its investment portfolio. Under this business model, the adoption of *AASB 9* is not expected to result in significant changes to accounting for investments. Other changes to the accounting for IAG's financial instruments arising from the application of *AASB 9* are expected to be minimal.

AASB 15 introduces a single model for the recognition of revenue based on when control of goods and services transfers to a customer. It does not apply to insurance contracts and financial instruments. Hence the majority of IAG's revenue is not impacted by this change.

AASB 16 was issued during 2016 and will replace existing accounting requirements for leases. Under current requirements, leases are classified based on their nature as either finance leases, which are recognised on the balance sheet, or operating leases, which are not recognised on the balance sheet. The application of *AASB 16* will result in the recognition of all leases on the balance sheet in the form of a right-of-use asset and a corresponding lease liability, except for leases of low value assets and leases with a term of 12 months or less. As a result, the new standard is expected to impact leases which are currently classified by IAG as operating leases, primarily, leases over premises and equipment. Based on preliminary assessments, the resulting amount to be recognised, in effect as a gross up to the balance sheet, is expected to be approximately $775 million. This is based on lease commitments and discount rates as at 30 June 2018.

AASB 17, a new accounting standard for insurance contracts, was adopted by the Australian Accounting Standards Board on 19 July 2017 subsequent to being issued by the International Accounting Standards Board on 18 May 2017. The standard is effective for periods beginning 1 January 2021. The first applicable reporting period for IAG will be for the year ending 30 June 2022, with the comparative period for the year ending 30 June 2021. The standard introduces a new general measurement model for accounting for insurance contracts, with the application of a simplified approach (similar to *AASB 1023*) permitted in certain circumstances. IAG is currently undertaking a detailed impact assessment of the new standard. There are changes in the presentation of the financial statements and disclosures anticipated. Due to the complexity of the requirements within the standard the final impact of certain requirements may not be determined until global interpretations and regulatory responses to the new standard are developed.

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 Group as at 30 June 2018 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 2018.

Signed at Sydney this 15th day of August 2018 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 AUDIT OF THE FINANCIAL REPORT

Opinion

We have audited the Financial Report of Insurance Australia Group Limited (the Company).

In our opinion, the accompanying Financial Report of the Company is in accordance with the *Corporations Act 2001*, including:

- giving a true and fair view of the Group's financial position as at 30 June 2018 and of its financial performance for the year ended on that date; and
- complying with *Australian Accounting Standards* and the *Corporations Regulations 2001*.

The Financial Report comprises:

- Consolidated balance sheet as at 30 June 2018;
- Consolidated statement of comprehensive income, Consolidated statement of changes in equity, and Consolidated cash flow statement for the year then ended;
- Notes including a summary of significant accounting policies; and
- Directors' Declaration.

The Group consists of the Company and the entities it controlled at the year-end or from time to time during the financial year.

Basis for opinion

We conducted our audit in accordance with *Australian Auditing Standards*. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the Financial Report* section of our report.

We are independent of the Group in accordance with the *Corporations Act 2001* and the ethical requirements of the *Accounting Professional and Ethical Standards Board's APES 110 Code of Ethics for Professional Accountants* (the Code) that are relevant to our audit of the Financial Report in Australia. We have fulfilled our other ethical responsibilities in accordance with the Code.

Key Audit Matters

The Key Audit Matters we identified are:

- Valuation of Gross outstanding claims liability
- Valuation of Reinsurance and other recoveries on outstanding claims
- Valuation of Goodwill and Investment in joint venture and associates

Key Audit Matters are those matters that, in our professional judgement, were of most significance in our audit of the Financial Report of the current period.

These matters were addressed in the context of our audit of the Financial Report as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Valuation of Gross outstanding claims liability ($10,410 million)

Refer to Note 2.2 of the Financial Report

The Key Audit Matter

Gross outstanding claims liability is a Key Audit Matter as a result of significant complexity relating to:

Valuation of gross outstanding claims liability

The valuation of gross outstanding claims liability is significant to the Key Audit Matter as:

- judgment is required by us to consider the central estimate of the gross outstanding claims liability. This is a significant estimate as the eventual outcomes of incurred but unsettled claims at the balance sheet date are inherently uncertain;
- there is limited information available and a greater level of uncertainty inherent in assessing estimations of claims which have been incurred by the balance sheet date but have not yet been reported to the Group. Examples include where there has been a recent natural catastrophe, or for the liability business;
- judgment is required when considering the application of historical experience of claims development to determine current estimates, including the greater variability between the original estimation and the ultimate settlement of claims where there is a long time delay between the claim being incurred and the ultimate settlement. Examples include claims arising from Workers' Compensation, Liability, Compulsory Third Party (CTP) and the main Canterbury earthquakes of September 2010 and February 2011;
- the claims estimation uses an actuarial modelling process which involves complex and subjective actuarial methodologies, judgments and assumptions about future events and developments, both within and external to the Group. Small changes in these methodologies, judgements and assumptions can have significant implications to the quantification of outstanding claims liabilities, as outlined in Note 2.2(E);
- the Canterbury earthquake claims require judgement and technical actuarial expertise to evaluate the attribution of claims costs between the September 2010 and the February 2011 Canterbury earthquake events;
- judgement is required to assess the estimation of the periods the claims are expected to be settled in;
- the estimation of claims at year end relies on the integrity of the underlying data, including claim payments and individual estimates of unsettled claims, which is gathered from many different systems; and
- we involve senior resources, with deep industry experience, together with our actuarial specialists in evaluating the Group's estimations of outstanding claims.

How the matter was addressed in our audit

Our audit procedures included:

Valuation of gross outstanding claims liability

We adopted a risk based approach to determine which classes of business posed higher claims estimation risks. Factors influencing the risk assessment included the level of judgement required, degree of uncertainty regarding the assumptions adopted, longer delays between claims being incurred, reported and expected settlement, greater relative magnitude in size, and significant variations over prior estimates.

For the higher risk areas identified, such as Workers' Compensation, Liability, CTP and the main Canterbury earthquakes, we:

- compared the Group's actuarial methodologies with the methodologies applied in the industry and in prior periods;
- evaluated the Group's governance processes, including Reserving Committees and actuarial control cycles for the valuation of the outstanding claims liabilities;
- evaluated the actuarial methodologies and the assumptions applied in the previous reporting period by comparing the actual claims development to the prior year claims liability estimate. We used the information to assess the adjustments made to the current year's actuarial methodologies and assumptions applied in the estimation;
- challenged key actuarial assumptions, including loss ratios, claim frequency and average size of claims, expected trends in court settlements and jury awards, and allowance for future claims inflation. Further we evaluated the attribution of losses to Canterbury earthquake events, by comparing these to our expectations based on the Group's historical experience, our industry knowledge and independently observable trends; and
- considered judgments required to estimate the period in which the claims will be settled by analysing historical payment patterns and assessing any significant changes.

For certain classes of business, we independently projected the gross outstanding claims liability by applying our own actuarial methodologies and selecting assumptions for those methodologies. We used this re-projection to compare our results to the Group's estimates and challenge any significant differences.

We were assisted by KPMG actuarial specialists in interpreting and evaluating the Group's actuarial modelling processes and methodology for determining the level of provisions for gross outstanding claims liabilities. We also considered the work and findings of external, independent actuaries, engaged by the Group.

Our procedures around the financial records and controls included, amongst others:

- testing accounting and actuarial controls such as reconciliations of key data;
- testing key controls and a sample of claims case estimates and paid claims, by comparing the Group's estimations for individual claims to third party evidence; and

- using our IT specialists we tested the general IT environment as well as a sample of reconciliations between data on the claims systems (underlying data) and data used in the actuarial modelling processes. We evaluated the Group's comparison programs which they use to assess the consistency of the data.

Risk margins and probability of adequacy

The evaluation of the risk margins and probability of adequacy is significant to the Key Audit Matter as it is complex and necessitated a significant level of judgement by us in our audit.

Outstanding claims include statistically determined risk margins developed by the Group to make allowance for the inherent uncertainty in estimating ultimate claim settlements. The risk margins are included to achieve a specified probability of adequacy for the total outstanding claims reserves.

We involved senior resources and our actuarial specialists to focus on the complex statistical processes and parameters used by the Group to establish the risk margins.

Risk margins and probability of adequacy

With the assistance of our actuarial specialists we evaluated the statistical processes to establish the Group's risk margins. In particular our procedures included:

- assessing the statistical processes' suitability by critically studying these and comparing them to known industry practices, our industry knowledge and other observable trends in industry forums and Actuaries Institute papers;
- assessing the risk margin parameters for significant portfolios by comparing these with external sources of data including published statistics (e.g. APRA-published data), prior periods and our industry knowledge;
- checking the central estimates of outstanding claims, which were tested in the valuation of gross outstanding claims liability processes, and are a key input into the risk margin model, to the underlying financial records; and
- critically evaluating the Group's judgement in the execution of the statistical processes by comparing the overall results to our expectations based on the Group's historical experience, our industry knowledge and independent observable trends (e.g. listed competitors).

Valuation of Reinsurance and other recoveries on outstanding claims ($5,422 million)

Refer to Note 2.2 of the Financial Report

The Key Audit Matter

Reinsurance and other recoveries on outstanding claims is a Key Audit Matter as:

- reinsurance and other recoveries, similar to the valuation of gross outstanding claims, are quantified from claims case estimates, paid claims data and estimates of ultimate claims settlement amounts. As such, the rationale for identifying it as a Key Audit Matter is the same as that highlighted for the valuation of gross outstanding claims;
- the Group has extensive reinsurance arrangements designed to protect its aggregate exposure to catastrophic claim events. Evaluating the reinsurance transactions accounting across the Group requires significant consideration by our senior resources with deep industry knowledge and specialised technical skills; and
- the Group also has a range of significant reinsurance contracts, including the whole-of-account quota share arrangements, the catastrophe excess of loss program, adverse development covers in the form of excess of loss contracts, and other quota share arrangements, which form part of its capital management. Our consideration of the accounting treatment and recoverability of balances owed by the reinsurer counterparties requires our senior resources, deep industry experience and specialised technical skills.

How the matter was addressed in our audit

In addition to the audit procedures undertaken to assess the valuation of gross outstanding claims liability, our procedures included:

- testing, for a sample of contracts, how the reinsurance and other recoveries on outstanding claims were accounted for. We referred to the terms of the reinsurance contracts, board meeting minutes, our expectations based on the Group's past experience, our industry knowledge, and the insurance accounting standard;
- independently evaluating a sample of reinsurance balances and other recoveries due to the Group arising from the whole-of-account quota share contracts. We referred to the terms of the reinsurance contracts, and applied them to the original underlying claims estimates and paid claims data to recalculate the reinsurance and other recoveries due. These independently generated results were compared to the amounts processed by the Group;
- evaluating a sample of the transactions processed relating to the reinsurance contracts. We tested the consistency of the contract terms to the criteria for the recognition of the transaction contained in accounting standards; and
- assessing the recoverability of balances owed by reinsurer counterparties by considering their credit worthiness and capital strength, based on external sources of information, payment history of amounts and evaluation of information for indicators of disputes.

Valuation of Goodwill ($2,875 million) and Investment in joint venture and associates ($557 million)

Refer to Notes 5.1 and 6.3 of the Financial Report

The Key Audit Matter

Valuation of goodwill and investment in joint venture and associates is a Key Audit Matter as:

- judgement is involved in assessing the cash generating units identified by the Group;
- the evaluation of potential impairment involves judgement in relation to forecast cash flows and key variables. Instances where judgement is required include interest rates, risk premium, growth rates, profit measures and terminal growth rates. We focused specifically on those cash generating units and associates where the valuation showed potential impairment indicators, or where there was a significant reduction in the valuation in the period;
- the assessment of the valuation of goodwill, and investment in joint venture and associates, requires the involvement of senior resources from the audit team together with our valuation specialists; and
- the Group uses complex models to perform their annual testing of goodwill for impairment. The models are largely internally developed, use adjusted historical performance, and a range of internal and external sources as inputs to the assumptions. Complex modelling, particularly those containing highly judgemental allocations of corporate assets and costs to cash generating units, using forward-looking assumptions tends to be prone to greater risk for potential bias, error and inconsistent application. These conditions necessitate additional scrutiny by us, in particular to address the objectivity of sources used for assumptions, and their consistent application.

How the matter was addressed in our audit

With the assistance of our valuation specialists, our procedures included:

- evaluating the Group's determination of their cash generating units based on our knowledge of the business, and understanding of the industries in which the Group operates, against the accounting standard requirements;
- evaluating the impact of the restructure of the Australian business on the determination of cash generating units;
- performing sensitivity testing, using the Group's models, to evaluate the impact of varying key assumptions. This enabled us to critically challenge the Group's quantification of assumptions and focus our testing to the most sensitive assumptions;
- challenging the Group's calculations and assumptions used in the discounted cash flow model during the year;
- assessing the Group's quantification of key variables by comparing them to external, observable metrics (e.g. GDP growth and inflation incl. forecasts provided by Oxford Economics and IBIS World), our knowledge of the markets, and current market practice;
- comparing the forecast cash flows to Board approved budgets and business plans, and examination of the accuracy of past budgets to actual cash flows in order to challenge the Group's current forecasts;
- comparing the valuations for certain joint ventures and associates to external, independent and observable valuations for broadly similar enterprises, and investigating significant outliers;
- assessing the Group's allocation of corporate costs to the forecast cash flows contained in the value in use model, based on the requirements of the accounting standard and our understanding of the business; and
- involving our specialists, we evaluated the internally prepared discounted cash flow model. This included:
  - assessing the valuation approach and methodology against market and industry practices and accounting standards; and
  - assessing the integrity of the models used, including the accuracy of the underlying formulas.

Using our IT specialists, we tested the general IT environment as well as specific system controls in relation to the underlying data used in the valuation models to assess the consistency of the data.

Other Information

Other Information is financial and non-financial information in Insurance Australia Group Limited's annual reporting which is provided in addition to the Financial Report and the Auditor's Report. The Directors are responsible for the Other Information.

Our opinion on the Financial Report does not cover the Other Information and, accordingly, we do not express an audit opinion or any form of assurance conclusion thereon, with the exception of the Remuneration Report.

In connection with our audit of the Financial Report, our responsibility is to read the Other Information. In doing so, we consider whether the Other Information is materially inconsistent with the Financial Report or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

We are required to report if we conclude that there is a material misstatement of this Other Information, and based on the work we have performed on the Other Information that we obtained prior to the date of this Auditor's Report we have nothing to report.

Responsibilities of the Directors for the Financial Report

The Directors are responsible for:

- preparing the Financial Report that gives a true and fair view in accordance with *Australian Accounting Standards* and the *Corporations Act 2001*;
- implementing necessary internal control to enable the preparation of a Financial Report that gives a true and fair view and is free from material misstatement, whether due to fraud or error; and
- assessing the Group's ability to continue as a going concern and whether the use of the going concern basis of accounting is appropriate. This includes disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless they either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the Financial Report

Our objective is:

- to obtain reasonable assurance about whether the Financial Report as a whole is free from material misstatement, whether due to fraud or error; and
- to issue an Auditor's Report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with *Australian Auditing Standards* will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error. They are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of this Financial Report.

A further description of our responsibilities for the audit of the Financial Report is located at the *Auditing and Assurance Standards Board* website at http://www.auasb.gov.au/auditors_responsibilities/ar1.pdf. This description forms part of our Auditor's Report.

REPORT ON THE REMUNERATION REPORT

Opinion

In our opinion, the Remuneration Report of Insurance Australia Group Limited for the year ended 30 June 2018, complies with *Section 300A* of the *Corporations Act 2001*.

Directors' responsibilities

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 responsibilities

We have audited the Remuneration Report included in pages 18 to 38 of the Directors' Report for the year ended 30 June 2018.

Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with *Australian Auditing Standards*.

KPMG

KPMG

Andrew Yates
Partner

Ian Moyser
Partner

Sydney
15 August 2018

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).

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 2018 annual general meeting (AGM) of Insurance Australia Group Limited will be held on 26 October 2018 commencing at 9.30am at Sofitel Sydney Wentworth, 61-101 Philip Street, Sydney NSW 2000. 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 2018 AGM at www.iag.com.au. The information required to log on and use online voting is shown on the voting form.

SHAREHOLDER QUESTIONS

If shareholders 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, shareholders should use the form supplied with the notice of meeting and return it with their completed Voting Form in the pre-addressed envelope provided or by fax to +61 (0)3 9473 2555. Questions for the auditor must be received by 5pm on 19 October 2018.

Shareholders may also submit a question after completing their voting instructions online at www.iag.com.au. Shareholders 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 the Company's Dividend Reinvestment Plan (DRP), if available, providing the option to increase their shareholding without incurring brokerage or GST.

MANAGEMENT OF HOLDING

Using their Shareholder Reference Number (SRN) or Holder Identification Number (HIN) and postcode of their registered address, shareholders can view their holding online through IAG's share registry, Computershare, by following the easy prompts on their website at www.investorcentre.com where shareholders will be able to:

- view holding balance;
- review dividend payment history;
- access shareholder forms; and
- retrieve holding statements, including recent dividend payment advices.

The share registry investor centre site also allows shareholders to update or add details to their shareholding. If shareholders wish to amend or update any of the current details, they will be asked to register by choosing a User ID and Password.

Shareholders will also be asked to enter answers to three personal questions for verification purposes should they forget their password in the future.

If shareholders have previously used the Investor Centre site, they will be asked to key in their password only.

Once shareholders have completed these steps, they are then able to update their details and submit their changes to the share register including:

- change or amend their address if they are registered with an SRN;
- nominate or amend their direct credit payment instructions;
- set up or amend their DRP instructions;
- sign up for electronic shareholder communications, including the annual report via email; and
- add/change tax file number (TFN) / Australian business number (ABN) details.

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

Shareholders are strongly advised to lodge their TFN, ABN or exemption. If they 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

Shareholders can register to receive an email alert advising of new IAG media releases, financial announcements or presentations. Shareholders 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 their email address.

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

ORDINARY SHARES INFORMATION

IMPORTANT DATES*	2018
IAG year end	30 June
Full year results and dividend announced	15 August
Annual report and notice of meeting mailout commences	10 September
Record date for final dividend	22 August
Final dividend paid	27 September
Written questions for the auditor close (5pm)	19 October
Proxy return close (10am)	24 October
Annual general meeting (9.30am)	26 October
IAG half year end	31 December

* Please note that some dates are subject to change.

TWENTY LARGEST ORDINARY SHAREHOLDERS AS AT 12 JULY 2018	NUMBER OF SHARES	% OF ISSUED SHARES
HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED	611,069,628	25.81
J P MORGAN NOMINEES AUSTRALIA LIMITED	424,649,039	17.94
CITICORP NOMINEES PTY LIMITED	115,295,018	4.87
NATIONAL INDEMNITY COMPANY	89,766,607	3.79
NATIONAL NOMINEES LIMITED	66,410,456	2.81
BNP PARIBAS NOMINEES PTY LTD <AGENCY LENDING DRP A/C>	43,656,739	1.84
CITICORP NOMINEES PTY LIMITED <COLONIAL FIRST STATE INV A/C>	34,058,949	1.44
BNP PARIBAS NOMS PTY LTD <DRP>	22,327,490	0.94
HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED <NT-COMNWLTH SUPER CORP A/C>	9,088,091	0.38
AMP LIFE LIMITED	7,825,935	0.33
MILTON CORPORATION LIMITED	5,847,282	0.25
ARGO INVESTMENTS LIMITED	5,031,075	0.21
HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED-GSCO ECA	4,882,593	0.21
AUSTRALIAN FOUNDATION INVESTMENT COMPANY LIMITED	4,129,215	0.17
BKI INVESTMENT COMPANY LIMITED	3,157,370	0.13
IAG SHARE PLAN NOMINEE PTY LIMITED (IAG DAP UNALLOCATED ACCOUNT>	3,112,983	0.13
IOOF INVESTMENT MANAGEMENT LIMITED <IPS SUPER A/C>	2,705,382	0.11
POWERWRAP LIMITED <SCHEME - IML TRADES A/C>	2,494,131	0.11
HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED - A/C 2	1,895,756	0.08
MUTUAL TRUST PTY LTD	1,869,639	0.08
Total for top 20	1,459,273,378	61.63

RANGE OF ORDINARY SHAREHOLDERS AS AT 12 JULY 2018	NUMBER OF HOLDERS	NUMBER OF SHARES	% OF ISSUED SHARES
1-1,000	394,587	209,170,795	8.84
1,001-5,000	262,858	485,507,971	20.51
5,001-10,000	13,088	89,684,102	3.79
10,001-100,000	4,459	85,424,067	3.61
100,001 and over	118	1,497,737,409	63.25
Total	675,110	2,367,524,344	100.00
Shareholders with less than a marketable parcel of 62 shares as at 12 July 2018	3,272	82,402	

DIVIDEND DETAILS

SHARE CLASS	DIVIDEND	FRANKING	AMOUNT PER SHARE	DRP ISSUE PRICE	PAYMENT DATE
Ordinary	Interim	Fully franked	14.0 cents	$8.0900	29 March 2018
Ordinary	Final	Fully franked	20.0 cents	*	27 September 2018

* The DRP issue price for the final dividend is scheduled to be announced on 10 September 2018.

SUBSTANTIAL SHAREHOLDINGS AS AT 12 JULY 2018

SUBSTANTIAL SHAREHOLDERS AS AT 12 July 2018	NUMBER OF SHARES	% OF ISSUED SHARES
Ordinary shares		
THE CAPITAL GROUP COMPANIES, INC.	118,766,781	5.02

IAGPD CAPITAL NOTES INFORMATION

TWENTY LARGEST CAPITAL NOTE HOLDERS AS AT 12 JULY 2018	NUMBER OF NOTES	% OF ISSUED NOTES
HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED	514,143	12.72
J P MORGAN NOMINEES AUSTRALIA LIMITED	204,437	5.06
NATIONAL NOMINEES LIMITED	154,570	3.82
BNP PARIBAS NOMS PTY LTD <DRP>	102,609	2.54
IOOF INVESTMENT MANAGEMENT LIMITED <IPS SUPER A/C>	88,467	2.19
NAVIGATOR AUSTRALIA LTD <JB WERE LIST FIX INT SMA A/C>	70,364	1.74
HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED - A/C 2	64,072	1.59
CITICORP NOMINEES PTY LIMITED	57,634	1.43
NAVIGATOR AUSTRALIA LTD <MLC INVESTMENT SETT A/C>	57,469	1.42
NULIS NOMINEES (AUSTRALIA) LIMITED <NAVIGATOR MAST PLAN SETT A/C>	45,312	1.12
BNP PARIBAS NOMINEES PTY LTD HUB24 CUSTODIAL SERV LTD DRP	35,402	0.88
AUSTRALIAN EXECUTOR TRUSTEES LIMITED <NO 1 ACCOUNT>	32,496	0.80
INVIA CUSTODIAN PTY LIMITED <INCOME POOL A/C>	20,000	0.49
IOOF INVESTMENT MANAGEMENT LIMITED <IPS IDPS A/C>	17,550	0.43
THE WYATT BENEVOLENT INSTITUTION INC	15,517	0.38
CITICORP NOMINEES PTY LIMITED <DPSL>	13,853	0.34
NETWEALTH INVESTMENTS LIMITED <WRAP SERVICES A/C>	13,050	0.32
TRUSTEES OF CHURCH PROPERTY FOR THE DIOCESE OF NEWCASTLE <SAVINGS & DEVELOPMENT A/C>	12,870	0.32
INVIA CUSTODIAN PTY LIMITED <RISF A/C>	12,500	0.31
ANGUS DOWNS PTY LTD	12,000	0.30
Total for top 20	1,544,315	38.20

RANGE OF CAPITAL NOTE HOLDERS AS AT 11 JULY 2018	NUMBER OF HOLDERS	NUMBER OF NOTES	% OF ISSUED NOTES
1-1,000	4,215	1,403,204	34.73
1,001-5,000	399	812,367	20.10
5,001-10,000	36	247,394	6.12
10,001-100,000	19	602,541	14.91
100,001 and over	4	975,759	24.14
Total	4,673	4,041,265	100.00
Capital note holders with less than a marketable parcel of 5 notes as at 12 July 2018	3	6	

CORPORATE DIRECTORY

SHARE REGISTRY

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FIVE-YEAR FINANCIAL SUMMARY

	2018 $m	2017[9] $m	2016 $m	2015 $m	2014 $m
Gross written premium	**11,647**	11,439	11,367	11,440	9,779
Gross earned premium	**11,522**	11,321	11,411	11,525	9,721
Outwards reinsurance premium expense	**(3,851)**	(3,122)	(3,183)	(1,196)	(1,077)
Net premium revenue	**7,671**	8,199	8,228	10,329	8,644
Net claims expense	**(4,617)**	(5,082)	(5,397)	(6,941)	(5,201)
Net underwriting expense	**(1,877)**	(2,079)	(2,116)	(2,847)	(2,303)
Underwriting profit[1]	**1,177**	1,038	715	541	1,140
Net investment income on assets backing insurance liabilities	**230**	232	463	562	439
Management reported insurance profit[1]	**1,407**	1,270	1,178	1,103	1,579
Net investment income from shareholders' funds	**165**	246	97	223	396
Other income	**164**	180	204	187	199
Share of net profit/(loss) of associates[2]	**31**	19	17	6	(8)
Finance costs	**(82)**	(93)	(99)	(107)	(98)
Corporate and administration expenses[3]	**(185)**	(222)	(423)	(383)	(255)
Acquired intangible amortisation and impairment	**(90)**	(57)	(54)	(80)	(11)
Profit before income tax	**1,410**	1,343	920	949	1,802
Income tax expense	**(384)**	(328)	(218)	(119)	(472)
Profit after tax from continuing operations	**1,026**	1,015	702	830	1,330
Loss after tax from discontinued operations	**(25)**	(10)	-	-	-
Net profit attributable to non-controlling interests	**(78)**	(76)	(77)	(102)	(97)
Net profit attributable to shareholders of the Parent	**923**	929	625	728	1,233
Ordinary shareholders' equity ($ million)	**6,669**	6,562	6,563	6,817	6,568
Total assets ($ million)[4]	**29,766**	29,597	30,030	31,402	29,748
KEY RATIOS					
Gross written premium growth	**1.8 %**	n/a	(0.6)%	17.0 %	3.0%
Loss ratio[5]	**60.2 %**	62.0 %	65.6 %	67.2 %	60.2 %
Expense ratio[6]	**24.5 %**	25.3 %	25.7 %	27.6 %	26.7 %
Combined ratio[7]	**84.7 %**	87.3 %	91.3 %	94.8 %	86.9 %
Insurance margin[8]	**18.3 %**	15.5 %	14.3 %	10.7 %	18.3 %
SHARE INFORMATION					
Dividends per ordinary share – fully franked (cents)	**34.00**	33.00	36.00	29.00	39.00
Basic earnings per ordinary share (cents)	**39.06**	39.03	25.79	31.22	56.09
Diluted earnings per ordinary share (cents)	**38.30**	37.72	25.34	30.45	53.62
Ordinary share price at 30 June ($) (ASX: IAG)	**8.53**	6.78	5.45	5.58	5.84
Convertible preference share price at 30 June ($) (ASX: IAGPC)	**-**	-	101.50	101.60	106.44
Capital notes price at 30 June ($) (ASX: IAGPD)	**104.67**	106.53	-	-	-
Reset exchangeable securities price at 30 June ($) (ASX: IANG)	**102.66**	103.40	100.00	103.10	107.00
Issued ordinary shares (million)	**2,367**	2,367	2,431	2,431	2,341
Issued convertible preference shares (million)	**-**	-	4	4	4
Issued capital notes (million)	**4**	4	-	-	-
Market capitalisation (ordinary shares) at 30 June ($ million)	**20,191**	16,048	13,249	13,565	13,671
Net tangible asset backing per ordinary share ($)[4]	**1.47**	1.36	1.30	1.34	1.27

(1) The amounts for 2016 financial year are presented on a management reported (non-IFRS) basis which is not directly comparable to the equivalent statutory (IFRS) figure. A reconciliation between the two is outlined in the Operating and Financial Review section of the Directors' Report in the 30 June 2016 Annual Report.
(2) Share of net profit/(loss) of associates includes regional support and development costs.
(3) Includes a $198 million impairment of capitalised software for 2016 and a $60 million impairment of the investment in Bohai Insurance for 2015.
(4) 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.
(5) The loss ratio refers to the net claims expense as a percentage of net premium revenue.
(6) The expense ratio refers to net underwriting expense as a percentage of net premium revenue.
(7) The combined ratio refers to the sum of the loss ratio and expense ratio.
(8) Insurance margin is a ratio of insurance profit over net premium revenue.
(9) The financial information for 2017 has been re-presented to reflect the changed treatment of the Asian businesses as discontinued operations. Financial information for 2016, 2015 and 2014 is not re-presented.

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AUSTRALIA

NEW ZEALAND

ASIA

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 Insurance Australia Limited (IAL), the underwriter of general insurance products under the Coles Insurance brand. These products are distributed by Coles under an Authorised Representative Agreement with IAL.

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

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

100%-owned unless indicated (all ownership percentages are as at 30 June 2018).