



26 February 2010

The Manager
Company Announcements
ASX Limited
Level 6
Exchange Centre
20 Bridge Street
SYDNEY NSW 2000

QBE Insurance Group Limited
ABN 28 008 485 014

Head Office
82 Pitt Street
SYDNEY NSW 2000
Australia

Postal Address
Box 82 GPO SYDNEY 2001
Telephone: +61 (2) 9375 4444
Facsimile: +61 (2) 9231 6104
DX 10171, Sydney Stock Exchange

Dear Sir/Madam,

**re: Report on results and financial statements
for the year ended 31 December 2009**

The Directors of QBE Insurance Group Limited announce the financial results for the year ended 31 December 2009.

The following documents are attached:

1. Appendix 4E – Preliminary Final Report
2. QBE's 2009 Annual Report including financial statements for the year ended 31 December 2009
3. Market announcement

Yours faithfully,

A handwritten signature in blue ink that reads 'D Ramsay'.

Duncan Ramsay
Company Secretary

Enc.

QBE Insurance Group Limited
ABN 28 008 485 014
Appendix 4E - Preliminary final report
31 December 2009

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QBE Insurance Group Limited

Results for announcement to the market

				A\$M
Revenue from ordinary activities	Up	4%	to	16,615
Profit from ordinary activities after tax attributable to members	Up	6%	to	1,970
Net profit for the period attributable to members	Up	6%	to	1,970
Dividends		Amount per security (cents)		Franked amount per security (cents)
Interim dividend		62.0		12.4
Final dividend		66.0		13.2
Record date for determining entitlements to the dividend	10 March 2010			
<p>The final dividend will be paid on 30 March 2010.</p> <p>The last date for receipt of election notices applicable to the Bonus Share Plan and to the Dividend Reinvestment Plan will be 10 March 2010.</p>				

QBE Insurance Group Limited

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N/A – not applicable

Attachment A

QBE Insurance Group Limited

Annual report for the year ended 31 December 2009

One team.
One culture.
47 countries.
All moving together
in one direction.



QBE Insurance Group
Annual Report December 2009

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With operations in 47 countries, QBE has achieved considerable growth over the past 10 years and is recognised as one of the top 25 global insurers and reinsurers as measured by net earned premium. Over the past five years, our underwriting results and return on equity have consistently been in the top five of the world's 50 largest insurers and reinsurers.

The culture at QBE is one of coordinated team work and always striving for excellence and higher levels of performance. The QBE culture is underpinned by nine essential behaviours which are embedded in our daily work life and continue to evolve as the organisation grows. Our culture is the framework which holds our diverse operations together.

In the words of QBE's chief executive officer, Frank O'Halloran: "You cannot run a successful organisation in 47 countries if you don't have a culture. I always use the analogy with sporting teams, that you can only be consistently successful as a sporting team if you have a strong culture where everyone knows the direction they are heading and what is expected of them."

In recognition of the common elements of high-level performance demanded in sport and QBE's businesses, this year's annual report includes images of exceptional performance in sport and details of industry and peer group acknowledgment of QBE's corporate and staff achievements during the year.

2009 in review

PROFIT AND DIVIDEND		2009	2008	% CHANGE
Net profit after income tax	\$M	1,970	1,859	6
Return on average shareholders' funds	%	18.4	20.9	
Basic earnings per share ⁽¹⁾	cents	195.6	207.7	(6)
Diluted earnings per share ⁽²⁾	cents	192.8	205.9	(6)
Dividend per share	cents	128.0	126.0	2
Dividend payout	\$M	1,306	1,187	10

GROUP OPERATING PERFORMANCE		2009	2008	% CHANGE
Gross written premium	\$M	14,455	13,142	10
Net earned premium	\$M	12,149	11,087	10
Combined operating ratio	%	89.6	88.5	
Underwriting profit	\$M	1,262	1,275	(1)
Insurance profit	\$M	2,064	2,183	(5)
Insurance profit to net earned premium	%	17.0	19.7	
Cash flow from operations	\$M	1,908	2,251	(15)

AMOUNTS IN THIS REPORT ARE DENOMINATED IN AUSTRALIAN DOLLARS UNLESS OTHERWISE SPECIFIED.

(1) Reflects shares notified to the Australian Securities Exchange. Refer to note 25(A) to the financial statements.

(2) Assumes that all hybrid securities are fully dilutive.

Chairman's report

On behalf of the board, I am pleased to report a 6% increase in net profit after tax to \$1,970 million following a year of continuing volatility in financial markets and a strengthening Australian dollar. We should not underestimate the significant achievement of the QBE Group in producing such outstanding financial and underwriting results in a period that history will record as being one of the most difficult and disruptive to the world's economic environment since the 1930s.



Given the difficult economic conditions and historically low interest rates, QBE produced an excellent return on equity of 18.4% compared with 20.9% last year. We continue to outperform the great majority of the top 50 global insurers and reinsurers (as measured by net earned premium) who have averaged a return on equity of around 13% over the past five years. Like 2008, the profit includes a number of significant items resulting from the global financial crisis. These are referred to on page 6.

In recognition of the strong return on equity and profit, the directors have declared a final dividend of 66.0 cents per share. The total dividend for 2009 is 128.0 cents per share, up from 126.0 cents for the year ended 31 December 2008 on an increased number of shares. The total dividend payout for 2009 is \$1,306 million, up 10% compared with \$1,187 million in 2008. With over 70% of profits generated by our foreign operations, the proportion of Australian profits and tax paid means a lower franking rate on dividends. The franking rate for the final dividend is 20%, consistent with the franking rate for the 2009 interim dividend. Books close on 10 March and the final dividend is payable on 30 March.

Including the share purchase plan issue in January 2009, dividend reinvestment and conversion of hybrid securities, the number of issued shares notified to the Australian Securities Exchange ("ASX") increased by 38 million to 1,025 million. Due to the increased number of shares, basic earnings per share reduced from 207.7 cents last year to 195.6 cents per share.

The value of QBE shares varied considerably throughout the year, affected by concerns over the impact of the stronger Australian dollar and low interest yields. Including reinvestment of dividends, shares recorded an increase in value for the year of 5.1% compared with the Australian All Ordinaries Accumulation Index which recorded an increase in 2009 of 39.6%. Over the longer term, QBE shares have outperformed the index with a compound annual average growth rate of 15.7% over five years, 18.5% over 10 years and 21.3% over 20 years compared with 8.2%, 8.7% and 9.9% respectively.

During the year we completed four acquisitions in Australia, the UK and the Americas and settled deferred consideration for earlier acquisitions. The continuing volatility in debt markets also provided the opportunity to repurchase an additional \$193 million of long-term QBE debt securities at a substantial discount, giving rise to a profit of \$70 million. Funding of acquisitions and the refinancing of approximately \$1.1 billion of borrowings which matured in 2009 was assisted by the issue of £550 million of senior notes maturing in 2015 and short-term bank finance of around \$500 million. The short-term borrowings were repaid from operating cash flow before year end. The remaining \$156 million of hybrid senior convertible securities were converted to QBE shares during the year.

QBE's ratio of borrowings to shareholders' funds was 29.1% at the end of 2009 compared with 32.9% last year end. This is the lowest level of gearing for many years and will provide increased financial flexibility to assist growth when opportunities arise and as debt markets improve.

The Group's regulatory capital and solvency levels are considered stable and strong for our various regulated insurance entities around the world and the consolidated Group at 31 December 2009. QBE calculates its minimum capital requirement using the Australian Prudential Regulation Authority's ("APRA's") risk-based capital approach for Australian insurers, taking into account the new regulations for corporate groups which commenced on 31 March 2009. On this basis, the Group capital adequacy multiple at 31 December 2009, after allowing for the final dividend, was around 1.6 times or \$2.5 billion in excess of the minimum capital requirement of \$4.1 billion. The QBE board considers the excess to be healthy given the low debt levels and the Group's proven ability to raise funds.

The directors continue to ensure that the financial strength of all QBE's operating entities is maintained at levels adequate to meet the requirements of our policyholders, business counterparties, regulatory authorities and rating agencies. The financial strength rating for our major insurance entities

NET PROFIT AFTER INCOME TAX

\$1,970M

Up 6% from last year

DIVIDEND PER SHARE

128 cents

Up 2 cents from last year

DIVIDEND PAYOUT

\$1,306M

Up 10% from last year

SHAREHOLDERS' HIGHLIGHTS

FOR THE YEAR ENDED 31 DECEMBER

		2009	2008
Net profit after income tax	\$M	1,970	1,859
Basic earnings per share ⁽¹⁾	cents	195.6	207.7
Diluted earnings per share ⁽²⁾	cents	192.8	205.9
Dividend payout	\$M	1,306	1,187
Dividend per share ⁽¹⁾	cents	128.0	126.0
Net tangible assets per share ⁽¹⁾	\$	5.16	5.73
Cash flow from operations	\$M	1,908	2,251
Total investments and cash ^(3,4,5)	\$M	25,091	28,541
Total assets ⁽⁵⁾	\$M	40,964	48,383
Shareholders' funds ⁽⁵⁾	\$M	10,222	11,159
Return on average shareholders' funds ⁽⁶⁾	%	18.4	20.9
Borrowings to shareholders' funds ⁽⁷⁾	%	29.1	32.9
Capital adequacy multiple		1.6	1.7

(1) Reflects shares notified to the Australian Securities Exchange. Refer to note 25(A) to the financial statements.

(2) Assumes that all hybrid securities are fully dilutive.

(3) Excludes ABC financial assets pledged for funds at Lloyd's.

(4) Includes financial assets, cash and investment properties.

(5) Reflects the impact of the stronger Australian dollar which was up 27.6% against the US dollar and 15.4% against sterling.

(6) 2008 return was weighted for the effect of share issues in the second half of 2008.

(7) Excludes ABC securities for funds at Lloyd's.

has been confirmed at A+ or equivalent and during the year, the credit rating for the holding company was upgraded to A.

Over the past two years, as a result of the global financial crisis, a number of deficiencies in the risk management practices and the regulation of financial institutions and capital markets around the world have been revealed. I am pleased to say that this was not the case for QBE and we have come through this difficult period extremely well. However, the problems faced by some insurers and the general approach to financial regulation means that the insurance industry can expect the introduction of more stringent regulatory frameworks and risk-based capital requirements. We anticipate increased costs to meet regulatory compliance and the level of minimum regulatory capital is expected to be higher in the various insurance markets. QBE Group's geographic and product diversity, scale of operations, financial flexibility and level of capital at entity and Group level are expected to provide us with a competitive advantage in this changing environment. QBE is well advanced in the implementation of APRA's supervisory requirements for insurance groups, has adequate systems and capital to comply with the expected regulations under the emerging Solvency II legislation in Europe and is well placed to comply with the expected increase in supervisory requirements in all markets.

In early 2009, we revised our longstanding practice of fully hedging our investment in foreign operations. With over 75% of shareholders' funds offshore from Australia, the use of forward foreign exchange contracts results in regular settlement funding and, in times of volatility, introduces liquidity risk and fluctuation of Group capital levels. Given the levels of currency volatility on our significant foreign operations, we adjusted our approach, consolidating and substantially reducing our exposure to forward foreign exchange contracts.

With the Australian dollar strengthening during the year, up 28% against the US dollar and 15% against sterling, the translation

of our investment in foreign operations to Australian dollars at year end resulted in a negative movement in the foreign currency translation reserve of \$2.2 billion with the effect that shareholders' funds decreased by 8% to \$10,222 million.

We continue to manage our exposure to foreign currency in each territory by matching liabilities with assets of the same currency.

The current economic environment requires that companies operating in the financial sector demonstrate a strong focus on risk management. QBE has an industry leading risk management framework with a clear focus on the key profit drivers and our track record established over many years shows that we have effective risk controls in place. The annual report includes a number of statements on our risk management methodology and associated corporate governance structure. Details are set out on pages 16 to 18 in the statement on risk management, regulatory developments and climate change and pages 47 to 48 in the Group's corporate governance statement.

The success of QBE's business is highly dependent on the quality of our staff. The board strongly supports staff development, succession planning and the provision of adequate incentives to reward and retain our quality people. The 2009 annual report includes 32 pages of detailed information on remuneration and incentive arrangements, and a larger group of key people are included in the key management personnel disclosed in the directors' report and in note 28 to the financial statements.

During 2009, the remuneration committee undertook a review of QBE's remuneration and reward frameworks. This was designed to take into account feedback from shareholders and regulators and to ensure our remuneration policies are aligned with current market practice and APRA's prudential standards.



Michael O'Loughlin of the Sydney Swans.

In light of broad-reaching debate about appropriate levels of executive remuneration and the need to ensure an appropriate balance between risk and reward, we have made a number of changes to our at-risk reward structures for key executives for 2010. In summary, these are:

- the deferred equity component of at-risk remuneration is subject to a claw-back for material subsequent deterioration of the relevant return on equity;
- the introduction of a new long-term incentive scheme with challenging future performance hurdles;
- no automatic vesting of future equity awards in the event of death, disability, redundancy or retirement; and
- all future share grants to the Group chief executive officer will be subject to shareholder approval.

We expect that 2010 will be another difficult year with continuing low yields on fixed interest and cash investments, particularly in the UK and the US markets. Capital markets are expected to remain cautious and potentially volatile, and a strong Australian dollar will negatively impact results when translating overseas revenue to Australian dollars. Compared with this time last year, global economic growth prospects are improving although they may take some time to return to more normal levels. Given these circumstances, we will be very pleased if we are able to maintain our insurance profitability at 2009 levels. We continue to look for opportunities to enhance the return on shareholders' funds and to grow our business.

The Group's targets for 2010 are set out on page 15. The achievement of these targets is subject to: no material movement in budgeted foreign exchange rates; large individual risk and catastrophe claims not exceeding the substantial allowance in our business plans; and stable debt and equity markets. Our targets are based on our proven strategy for growth through acquisition and product and geographic

The Sydney Swans are one of the most well-established teams in the Australian Football League. Michael O'Loughlin, who played for the club for 15 years and retired in 2009, was one of the clubs most talented athletes. He played in three AFL grand finals. Recognised as one of the most enduring relationships in Australian sport, QBE has been behind the Swans since 1987 through the highs and lows, providing support when required and celebrating achievements.

QBE Group's performance was recognised in the Australian Banking & Finance Magazine Awards as Best General Insurance Company in 2009. QBE has remained in the top five global insurers based on return on equity over the past five years.

diversification. This strategy has been successful over many years and has consistently added to the wealth of QBE shareholders. Management has in place efficient and effective business planning processes, clearly focused on minimising risk relating to our insurance and investment operations and designed to protect the interests of all our stakeholders. Our prospects for the future have been, and will continue to be, influenced by changes in global economic and environmental conditions. Your directors and management will maintain a careful watch on markets and matters affecting our industry and we will adjust our strategies and plans as appropriate.

On behalf of the directors, I acknowledge the significant achievements and hard work of all staff around the world. In particular, congratulations to the chief executive officer, Frank O'Halloran, and his management team for their oversight and contribution in protecting the assets of the Group and producing another solid financial and technical result in what has been a very difficult year for the global insurance and financial sectors. The board recognises the dedication of the QBE staff and their commitment to customer service and upholding the values associated with the unique QBE culture, which have been such an important part of the company's history, growth and success over many years.

I would like to welcome John Green to the board, whose appointment from March 2010 was recently announced. I am sure he will add considerable depth and expertise to the board and wish him well in his future service to the Group.

I would particularly like to acknowledge the significant contribution of each of my fellow directors to the development and supervision of the Group during the year.

John Cloney AM
Chairman

10 year history

FOR THE YEAR ENDED 31 DECEMBER ⁽¹⁾		2009	2008	2007	2006	2005	2004	2003	2002	2001	2000
Gross written premium	\$M	14,455	13,142	12,406	10,372	9,408	8,766	8,350	7,723	6,793	4,406
Gross earned premium	\$M	14,074	12,853	12,361	10,069	9,171	8,571	7,816	7,197	6,298	4,399
Net earned premium	\$M	12,149	11,087	10,210	8,158	7,386	6,781	6,036	5,642	4,634	3,456
Claims ratio	%	60.3	57.6	54.3	55.8	59.9	61.3	63.3	67.6	76.6	71.2
Commission ratio	%	16.2	17.2	18.5	17.0	16.9	17.5	18.2	17.7	20.2	18.3
Expense ratio	%	13.1	13.7	13.1	12.5	12.3	12.4	12.3	12.4	12.8	13.0
Combined operating ratio	%	89.6	88.5	85.9	85.3	89.1	91.2	93.8	97.7	109.6	102.5
Investment income ⁽²⁾											
before investment gains/losses	\$M	827	1,210	776	609	502	431	303	340	336	250
after investment gains/losses	\$M	1,237	1,177	1,132	822	718	519	413	189	349	310
Insurance profit (loss)	\$M	2,064	2,183	2,262	1,788	1,288	928	627	406	(119)	186
Insurance profit (loss) to net earned premium	%	17.0	19.7	22.2	21.9	17.4	13.7	10.4	7.2	(2.6)	5.4
Operating profit (loss)											
before income tax	\$M	2,432	2,420	2,549	2,012	1,523	1,115	765	311	(99)	220
after income tax and minority interest	\$M	1,970	1,859	1,925	1,483	1,091	857	572	279	(25)	179
Number of shares on issue ⁽³⁾	millions	1,025	987	886	819	794	745	672	615	585	429
Shareholders' funds	\$M	10,222	11,159	8,479	6,283	5,093	4,032	3,313	2,954	2,620	1,709
Total assets	\$M	40,964	48,383	39,613	31,757	29,665	25,036	20,443	20,567	18,611	13,948
Net tangible assets per share ⁽³⁾	\$	5.16	5.73	6.83	5.95	4.76	4.10	4.17	3.96	3.67	3.13
Borrowings to shareholders' funds ⁽⁴⁾	%	29.1	32.9	40.8	37.6	41.8	44.8	40.3	49.3	32.0	53.5
Basic earnings per share ⁽⁵⁾	cents	195.6	207.7	224.1	184.8	142.5	123.1	86.5	42.7	(10.5)	42.6
Diluted earnings per share ⁽⁵⁾	cents	192.8	205.9	217.3	173.5	131.5	109.3	77.5	43.4	(4.9)	40.7
Return on average shareholders' funds ⁽⁶⁾	%	18.4	20.9	26.1	26.1	23.9	24.5	18.3	10.0	(1.1)	12.6
Dividend per share	cents	128.0	126.0	122.0	95.0	71.0	54.0	42.0	35.0	30.0	31.0
Dividend payout	\$M	1,306	1,187	1,068	774	556	392	281	213	155	132
Cash flow from operations	\$M	1,908	2,251	2,374	2,039	1,987	2,110	2,089	1,511	280	173
Total investments and cash ^(7,8)	\$M	25,091	28,541	24,606	19,972	17,597	14,975	11,823	11,504	9,183	7,334

- (1) Financial information for 2004 and subsequent years is presented in accordance with Australian equivalents to International Financial Reporting Standards ("AIFRS"). Financial information for 2003 and prior years has not been restated to AIFRS.
- (2) Excludes amortisation and impairment of goodwill/intangibles.
- (3) Reflects shares notified to the Australian Securities Exchange. Refer to note 25(A) to the financial statements.
- (4) Excludes ABC securities for funds at Lloyd's.
- (5) Assumes that all hybrid securities are fully dilutive.
- (6) 2008 return was weighted for the effect of the share issues in the second half of that year.
- (7) Excludes ABC financial assets pledged for funds at Lloyd's.
- (8) Includes financial assets at fair value through the income statement, cash and cash equivalents and investment properties.

10 year history in US dollars

FOR THE YEAR ENDED 31 DECEMBER ⁽¹⁾		2009	2008	2007	2006	2005	2004	2003	2002	2001	2000
Gross written premium	\$M	11,239	11,015	10,391	7,839	7,171	6,484	5,407	4,184	3,502	2,445
Gross earned premium	\$M	10,943	10,773	10,353	7,610	6,990	6,340	5,061	3,899	3,246	2,441
Net earned premium	\$M	9,446	9,293	8,552	6,166	5,630	5,016	3,909	3,056	2,389	1,918
Investment income ⁽²⁾											
before investment gains/losses	\$M	643	1,014	650	460	383	319	196	184	173	139
after investment gains/losses	\$M	962	987	948	621	547	384	267	102	180	172
Insurance profit (loss)	\$M	1,605	1,830	1,895	1,351	982	686	406	220	(61)	103
Operating profit (loss)											
before income tax	\$M	1,891	2,028	2,135	1,521	1,161	825	495	168	(51)	122
after income tax and minority interest	\$M	1,532	1,558	1,612	1,121	832	634	370	151	(13)	99
Foreign exchange rates											
Cumulative average rate	US\$/A\$	77.8	83.8	83.8	75.6	76.2	74.0	64.8	54.2	51.5	55.5
Spot rate	US\$/A\$	89.6	70.2	87.7	79.0	73.3	78.3	75.2	56.1	51.1	55.9

- (1) This information is presented as a simple translation of income statement amounts to US dollars using the cumulative average rate of exchange applicable for each financial year.
- (2) Excludes amortisation and impairment of goodwill/intangibles.

Chief executive officer's report

QBE continued to produce strong underwriting and insurance profits despite the insurance industry experiencing a high frequency of large individual risk claims from the severe downturn in economic conditions and historically low interest yields on policyholders' funds. 2009 is the fifth year in succession we have reported a combined operating ratio of less than 90%.



QBE's diverse geographic and product spread ensured an excellent insurance profit of 17.0%, within our target range of 16% to 18% stated in the last annual report. This was after an increase in frequency of large individual risk claims, mainly in financial and property products. As expected, savings on central estimates of prior year claims provisions were much lower than the past three years.

All five insurance divisions produced a return on allocated capital above our minimum target of 15%. Our insurance margins and return on equity also remain in the top quartile of our peers in Australia, Asia Pacific, Europe, the US and Latin America. The return on equity on allocated capital for each of the operating divisions based on management results, excluding internal reinsurance arrangements, was Australia 20.8%, Asia Pacific 25.8%, Europe 23.1% and the Americas 17.1%.

Net profit after income tax was up 6% to \$1,970 million. Pre-tax profit included a number of significant items resulting from the volatility as a result of the economic downturn, in particular:

- foreign exchange gains of \$365 million, mainly due to the orderly unwinding of our hedges of foreign operations as the Australian dollar strengthened during the year. This compared with a gain of \$409 million last year;
- net realised and unrealised gains on equities of \$97 million compared with net losses of \$554 million last year;
- a profit of \$70 million on the repurchase of QBE debt securities compared with a profit of \$303 million last year;
- an unrealised loss of \$50 million on the revaluation of properties, mainly in the US;
- claims attributable to the global financial crisis on financial, trade credit and other insurance policies of \$144 million compared with \$200 million last year; and

- continued low yields on cash and government securities adversely impacting investment income.

We achieved an overall increase of 4% in premium rates which was slightly ahead of expectations. We have had to lapse or not renew some business and restrict our new business due to inadequate pricing and economic conditions, particularly in the US and Europe.

A slight improvement in the yield curve in 2009 increased the probability of adequacy of outstanding claims from 86.1% to 88.1% at the end of 2009. We have used risk-free government bond rates for the purpose of discounting our claims. We expect government bond yields to rise in 2010 and this will further benefit risk margins. The probability of adequacy of our total insurance liabilities (i.e. outstanding claims and unearned premium) was 95.5% compared with 93.2% at the end of 2008.

In response to requests from analysts and shareholders, this year's financial statements include additional information on our claims development (note 22) and a reconciliation of that development with the claims incurred included in the income statement (note 9). This additional disclosure is provided to assist the readers of our accounts.

Cash flow from operations reduced from \$2.3 billion to \$1.9 billion. Cash flow was impacted by the volatile Australian dollar, particularly against the US dollar and sterling, lower interest income and increased income tax payments relating to prior years.

Income tax expense reduced from 23% of profit before tax to 18%, due to the lower tax rates on foreign exchange and other gains and increased profits in lower tax paying countries.

GROSS WRITTEN PREMIUM

\$14,455M

Up 10% from last year

INSURANCE PROFIT

\$2,064M

Down 5% from last year

GROUP KEY RATIOS

		HALF YEAR TO 30 JUN 2009	HALF YEAR TO 31 DEC 2009	FULL YEAR TO 31 DEC 2009	HALF YEAR TO 30 JUN 2008	HALF YEAR TO 31 DEC 2008	FULL YEAR TO 31 DEC 2008
Gross written premium	\$M	8,057	6,398	14,455	6,603	6,539	13,142
Gross earned premium	\$M	7,118	6,956	14,074	5,958	6,895	12,853
Net earned premium	\$M	6,186	5,963	12,149	5,108	5,979	11,087
Claims ratio	%	60.8	59.9	60.3	54.7	60.1	57.6
Commission ratio	%	17.0	15.4	16.2	17.2	17.2	17.2
Expense ratio	%	11.5	14.7	13.1	13.9	13.5	13.7
Combined operating ratio	%	89.3	90.0	89.6	85.8	90.8	88.5
Insurance profit to net earned premium	%	17.5	16.5	17.0	21.8	17.7	19.7
Return on average shareholders' funds	%	19.0	18.6	18.4	19.9	22.2	20.9

GEOGRAPHIC SEGMENTS

GROSS EARNED PREMIUM	2009 %	2008 %
Australia	23.6	21.8
Asia Pacific	4.8	4.9
European operations	35.6	37.0
the Americas	36.0	35.7
Equator Re	-	0.6

QBE continued its successful strategy of growth from acquisition with a further four businesses acquired during the year. We have now completed over 125 acquisitions since our first acquisition in 1982. These acquisitions have enabled us to build our worldwide business and further improve our product diversification and geographic spread. We considered a number of acquisitions in 2009, but converted fewer than we would have liked mainly due to increased competition and our discipline on price.

The acquisitions made in late 2008 and in 2009 assisted growth and profit for the year. These acquisitions are expected to add around \$750 million of additional gross written premium in 2010. The acquisitions in 2009 include the Endurance property business in London; Carlife agency in Central Europe specialising in car warranty insurance; SLG underwriting agency specialising in US health stop loss insurance; and Elders

insurance and Elders agency business in Australia effective from 30 September 2009.

The acquisition of a number of specialist product underwriting agencies in the past three years is part of our strategy to increase our distribution channels, secure profitable premium income and further diversify our product range. These acquisitions reduce our total commission and expense ratio because the commission paid to acquired underwriting agencies is eliminated when we consolidate the profits of these agencies. The insurance profit benefited by 2.6% from the acquired agencies compared with 0.7% last year.

QBE's investments are substantially managed by our in-house investment team. We continued our low risk approach to managing our investment portfolio. Our focus on a high quality and short duration cash and fixed interest portfolio

INSURANCE LIABILITIES

AS AT	31 DECEMBER			
	2009 \$M	2008 \$M	2007 \$M	2006 \$M
Outstanding claims	14,350	16,161	13,871	11,645
Unearned premium net of deferred insurance costs	4,880	5,139	4,015	3,233
	19,230	21,300	17,886	14,878
Central estimate	17,106	19,137	15,433	12,656
Risk margin – outstanding claims	1,134	1,199	1,591	1,389
Risk margin – unearned premium	990	964	862	833
	19,230	21,300	17,886	14,878
Risk margin in excess of 75% probability of adequacy using APRA's risk weighted capital adequacy model	1,336	1,162	1,577	1,486



NSW Swifts wing attack, Vanessa Ware, in full flight.

has meant that we have had no permanent impairment of any fixed interest investments in 2008 and 2009. Our decision to increase our exposure to quality corporate paper early in 2009 significantly assisted investment income. We continue to adopt a cautious approach to equities resulting in gains on our equity portfolio underperforming the market.

INSURANCE PROFITABILITY

The Group's insurance profit reduced by 5% to \$2,064 million. The reduction was primarily due to lower savings from prior year central estimates of claims provisions and lower interest yields. Insurance profit comprises the underwriting result plus income on investments set aside to meet our liabilities to policyholders. Our insurance profit compares favourably with our peers and reflects the Group's continued focus on ensuring each product and each country meets QBE minimum requirements for return on allocated capital.

The Group's combined operating ratio (i.e. total claims, commissions and expenses as a percentage of net earned premium) was 89.6% compared with 88.5% last year. The higher combined operating ratio was primarily due to lower savings from prior year central estimates, partly offset by an increased contribution from acquired underwriting agencies. All of our insurance divisions continued to produce underwriting profits and the great majority of our products and operations in 47 countries continued to meet our minimum profit requirements.

Gross written premium increased by 10% to \$14,455 million and gross earned premium increased by 9% to \$14,074 million. Growth was lower than our original targets primarily due to the substantial strengthening of the Australian dollar since we published our annual report last year. Growth was mainly from acquisitions made in 2008 and new distribution channels. Our customer retention remains high; however,

QBE proudly sponsors the Sydney Swifts, a leading Australian netball team whose players have a strong track record of elite performance in national and international competition. The Swifts won the 2008 national championships. They have developed a winning culture where each team member is focused on delivering the highest level of personal commitment and contributing to the success of the team.

QBE was named BRW Magazine's 2009 Most Respected Company in the Insurance Industry in Australia, which is a testament to the Group's culture of strong and strategic leadership.

new business was below target due to the economic conditions, market competition and our stance on pricing. Overall average premium rate increases of 4% were in line with target with rate increases being achieved in all divisions, albeit small in the US and Asia Pacific divisions. Net earned premium increased by 10% to \$12,149 million, in line with the growth in gross written premium.

The Group's cost of reinsurance protections as a percentage of gross earned premium remained unchanged at 13.7%. Synergies from the 2008

acquisitions and other initiatives were offset by the increased cost of reinsurance protections. QBE's net exposure to major catastrophes from the largest single realistic disaster scenario was 4.3% of projected net earned premium at year end. The purchase of reinsurance protections is a very important part of risk management. Our approach involves the purchase of excess of loss protections for large individual risk claims and catastrophes to reduce volatility in the income statement and to protect the Group's capital adequacy ratios. QBE also uses proportional reinsurance to balance aggregate exposures across catastrophe zones, for capacity to write lead lines and also to meet the requirements of some of our intermediaries.

Gross claims incurred as a percentage of gross earned premium reduced from 60.2% to 58.0% mainly due to the lower level of catastrophe claims in 2009. Net claims incurred, which is after recovery from our reinsurance protections, increased from 57.6% to 60.3% of net earned premium. Our attritional claims ratio (i.e. claims below \$2.5 million), excluding savings on central estimates of prior year claims provisions and claims attributable to the global financial crisis, was 51.4% compared with 50.7% last year. The higher ratio was mainly due to increased attritional claims in European operations' property, aviation and professional liability portfolios. Savings on central estimates of prior year claims provisions were 0.7% of net

BORROWINGS MATURITY⁽¹⁾

AS AT	31 DECEMBER 2009		31 DECEMBER 2008	
	\$M	%	\$M	%
Less than one year	861	29	1,120	31
One to five years	575	19	1,673	46
More than five years	1,535	52	873	23
	2,971	100	3,666	100

(1) The maturity profile assumes that borrowings will be payable at the first call date.

BORROWINGS PROFILE

AS AT	31 DECEMBER 2009		31 DECEMBER 2008	
	\$M	%	\$M	%
Bank loans	24	1	632	17
Senior debt	1,558	52	1,055	29
Eurobonds	326	11	399	11
Hybrid securities	535	18	735	20
Subordinated debt	329	11	463	13
Capital securities	199	7	382	10
	2,971	100	3,666	100

earned premium compared with 3.3% last year, after allowing for a \$70 million increase in the provision for old latency claims. We considered this prudent given recent court awards and publicity in relation to asbestos, industrial deafness and similar claims. We continue to maintain our survival ratio in the upper quartile when compared with our peers. The net claims ratio also includes 1.2% for estimated claims from the global financial crisis compared with 1.8% last year. Large individual risk and catastrophe claims (i.e. claims of \$2.5 million and above) were 7.4% compared with 8.4% last year. QBE experienced an increased frequency of large individual risk claims which were more than offset by a reduction in catastrophe claims. The Victorian bushfire loss was our largest claim in 2009, contributing \$100 million to net claims incurred.

The combined commission and expense ratio reduced from 30.9% to 29.3%, reflecting the benefit of the underwriting agencies acquired in 2008, in particular ZC Sterling in the US. The commission ratio was 16.2% compared with 17.2% with the reduction due to the elimination of commission margins paid to acquired underwriting agencies. The expense ratio reduced slightly from 13.7% to 13.1%, primarily due to the growth in fixed remuneration for staff being less than the growth in premium income and a reduction in staff incentives based on the 2009 year results. Expenses include further costs of new systems initiatives, in particular the consolidation of systems from acquisition activity over recent years.

More detail on insurance profitability in each division is contained on pages 24 to 37.

INVESTMENT INCOME

Investment income, net of borrowing costs and expenses, increased from \$1,177 million to \$1,237 million. Net realised and unrealised gains on our equity portfolio were \$97 million compared with net losses of \$554 million last year. Foreign exchange gains were \$365 million compared with \$409 million last year. Profit on the repurchase of some of our debt securities

was \$70 million compared with \$303 million last year. The continued low interest yields adversely impacted returns on our short dated cash and fixed interest portfolio; however, we were able to take advantage of the wider credit spreads in March 2009 by increasing our exposure to quality corporate paper. Overall, we continue to remain at the short end of the yield curve, providing us with flexibility as interest rates rise. Our conservative strategy has resulted in no permanent impairments to date on our fixed interest portfolio. We maintained a cautious approach to equities and this limited our equity gains to considerably less than the market. Gross investment income was \$1,097 million compared with \$766 million last year. The gross investment yield was 4.1% compared with 2.9% last year and the net yield was 5.3% compared with 5.1%.

We continue to adopt a prudent approach to the management of investment funds set aside to meet the obligations to our policyholders. Policyholders' funds at year end were \$17 billion, or 67% of total investments and cash, compared with \$19 billion last year. The reduction was due to substantial strengthening of the Australian dollar.

Our approach continues to be cautious, focusing on quality investments and maintaining a relatively short duration for cash and fixed interest securities. The average duration of our cash and fixed interest portfolio is currently at 0.5 years. We intend to increase our net exposure to equities up to 10% of total investments and cash when there are clear signs that equity markets are more stable.

BALANCE SHEET

Our balance sheet remains conservative with a low risk investment portfolio that is marked to market value, insurance liabilities that are estimated to have a probability of adequacy of 95.5%, a low debt to equity ratio of 29.1% and a Group capital adequacy multiple at 1.6 times APRA's minimum capital requirement.

SUMMARY BALANCE SHEET

AS AT	31 DECEMBER 2009 \$M	31 DECEMBER 2008 \$M
Investments and cash	25,091	28,541
Trade and other receivables	4,300	5,041
Reinsurance recoveries – outstanding claims	2,068	2,692
Reinsurance recoveries – IBNR	1,615	2,351
Deferred insurance costs	1,955	1,987
Intangibles	5,014	5,586
Other assets	921	2,185
Total assets	40,964	48,383
Outstanding claims	18,033	21,204
Unearned premium	6,835	7,126
Borrowings	2,971	3,666
Other liabilities	2,827	5,142
Total liabilities	30,666	37,138
Net assets	10,298	11,245
Minority interests	76	86
Shareholders' equity	10,222	11,159

MINIMUM CAPITAL REQUIREMENT

AS AT	31 DECEMBER 2009 \$M	31 DECEMBER 2008 \$M
Tier 1		
Share capital and reserves	10,264	11,230
Perpetual securities	199	382
Excess risk margins	1,336	1,162
Deductions ⁽¹⁾	(5,708)	(5,657)
	6,091	7,117
Tier 2		
Subordinated debt and hybrid securities	573	805
Total capital base⁽²⁾	6,664	7,922
Insurance risk charge	2,731	2,996
Concentration risk charge	535	510
Investment risk charge	880	1,115
Minimum capital requirement	4,146	4,621
Excess capital	2,518	3,301
Capital adequacy multiple	1.61	1.71

(1) Includes intangibles of \$5,014 million (2008 \$5,586 million) net of \$84 million (2008 \$601 million) of contingent consideration.

(2) QBE's capital base does not include any allowance for the substantial investment to date of \$1.6 billion in wholly-owned underwriting agencies.

OUTSTANDING REINSURANCE RECOVERIES – RATING

AS AT	31 DECEMBER 2009		31 DECEMBER 2008	
	\$M	%	\$M	%
S&P rating				
AAA	157	4	231	5
AA	1,398	38	2,739	54
A	1,830	50	1,756	35
BBB or lower	104	3	148	3
Non-rated	194	5	169	3
	3,683	100	5,043	100

Within our operations, currency liabilities are matched with assets of the same currency. As mentioned at the 2009 annual general meeting, our currency exposure to investments in foreign operations is currently no longer fully protected through forward foreign exchange contracts.

The considerable volatility of foreign exchange markets has had a significant impact on our overseas assets and liabilities in the Australian dollar balance sheet. The Australian dollar at the end of 2009 was 27.6% higher against the US dollar and 15.4% higher against sterling compared with the rates at the end of 2008. With around 46% of our revenue in US dollars, supplementary information in US dollars is provided to assist readers of the financial statements.

Reinsurance recoveries on outstanding claims reduced from \$5,043 million to \$3,683 million. This was partly due to the strength of the Australian dollar. Reinsurance recoveries include recoveries on claims incurred but not reported (IBNR) of around 44% of total recoveries. We regularly review the recoveries on paid, outstanding and IBNR claims and we maintain a prudent approach to the use of reinsurance and the provisions for doubtful recoveries.

Australian Accounting Standards require Australian insurers to discount outstanding claims using a risk-free rate. We have adopted government bond yields as the indicative rate. The slightly higher yields beyond one year assisted the probability of adequacy of outstanding claims which has increased from 86.1% to 88.1%, well in excess of the minimum 75% required by APRA. We are of the view that the use of risk-free government rates for calculating the discount is extremely conservative, particularly as our low risk investment portfolios consistently yield well in excess of the government bond rates used. We also anticipate that investment yields will rise beyond the current yield curve during the next 12 months. Net outstanding claims of \$14.4 billion are expected to be paid out over 25 years. The weighted average term to settlement at 31 December 2009 was 2.8 years.

We continue to experience savings on prior accident year claims provisions although at a substantially lower level than recent years. It is expected that the substantial risk margins held for 2009 and prior accident years will result in savings over time as our claims continue to be settled within central estimates.

The Group balance sheet includes significant insurance provisions and risk margins raised following the acquisition of QBE Lenders' Mortgage Insurance ("QBE LMI") in 2008 to cover an increase in mortgage defaults. QBE LMI has performed substantially better than expectations during 2009; however, at this time, we consider it prudent to retain the risk margins raised at acquisition.

OUTLOOK

The outlook for growth in our existing business and for a continuation of strong underwriting profits is positive. Growth will be assisted by the additional premium from the acquisition of ZC Sterling in late 2008 and Elders Insurance in Australia effective from 30 September 2009. We are targeting to further increase our high customer retention ratio and to increase overall average premium rates by around 2%. Organic growth will continue to remain low due to pricing and competition. The expected stronger average Australian dollar will adversely impact the translation of overseas premium income and profits in 2010. In Australian dollars, we expect 3% growth in gross written premium based on average exchange rates of US\$0.90 and £0.58 compared with US\$0.78 and £0.50 in 2009. In US dollars, we expect gross written premium and net earned premium to grow by around 18%. No allowance has been made for acquisitions that will be converted during the year.

The risk profile of our insurance and reinsurance operations around the world continues to be carefully managed. We have purchased substantial reinsurance protections for the 2010 year at slightly lower cost than 2009. We have increased the participation of Equator Re, our captive reinsurer, on our external placements and this means our maximum event retention will increase slightly in 2010. We believe this is appropriate given the size of the Group and after analysis of results of business ceded to our external reinsurers over the past 10 years. We have maintained the Group reinsurance protection purchased for three years commencing 1 January 2008 which provides cover against a frequency of catastrophes and large individual risk claims. We expect our 2010 attritional claims ratio (i.e. net claims less than \$2.5 million) to be around 51% due to our product diversification, geographic spread, actions taken on a small number of portfolios and the rate increases achieved in 2009 and expected for 2010. We expect a reduction in the frequency of claims from the global economic downturn, particularly for credit-related products. Subject to large individual risk and catastrophe claims net of reinsurance protections not exceeding the significant allowance in our business plans, we expect to achieve a combined operating ratio which will be better than 2009; however, the lower interest rate environment is likely to result in an insurance profit margin between 16% and 18%.

2010 TARGETS

GROSS WRITTEN PREMIUM GROWTH

In **A\$ 3%**

In **US\$ 18%**

NET EARNED PREMIUM GROWTH

In **A\$ 3%**

In **US\$ 18%**

COMBINED OPERATING RATIO

Less than **89%**

INSURANCE PROFIT MARGIN

Target range

16% to 18%
of net earned premium

KEY FOREIGN EXCHANGE RATE MOVEMENTS AGAINST THE A\$

	CUMULATIVE AVERAGE RATE OF EXCHANGE			CLOSING RATE OF EXCHANGE		
	YEAR ENDED	YEAR ENDED	MOVEMENT %	AS AT	AS AT	MOVEMENT %
	31 DECEMBER 2009	31 DECEMBER 2008		31 DECEMBER 2009	31 DECEMBER 2008	
US dollar	77.8	83.8	(7.2)	89.6	70.2	27.6
Sterling	50.1	45.8	9.4	55.5	48.1	15.4
Euro	56.1	57.6	(2.6)	62.6	50.2	24.7

OWNED AGENCY RESULTS

FOR THE YEAR ENDED 31 DECEMBER	UNDERWRITING RESULT		PROFIT BEFORE INCOME TAX ⁽¹⁾	
	2009 \$M	2008 \$M	2009 \$M	2008 \$M
Australian operations	52	32	56	38
the Americas	267	42	267	41
	319	74	323	79

(1) Excludes amortisation of intangibles.

The combined commission and expense ratio is targeted to remain below 30% in 2010. We will be incurring substantial additional cost to reduce the number of legacy systems from acquisitions around the world and to improve the interface with our intermediaries. Our underwriting agencies are targeted to contribute a similar profit in 2010 compared with 2009 or around 2% of net earned premium. The substantial majority of insurance premium produced by our wholly-owned underwriting agencies, estimated to be around \$1.6 billion, will be underwritten by QBE.

The gross investment yield will be adversely impacted by the continued low yields on our worldwide cash and fixed interest investment portfolios. We are targeting a gross investment yield of close to 3%. In the current environment, we feel it is more important to maintain our proven strategy and not take additional risk on our investment portfolio to improve yields. We anticipate that interest rates will rise to more normal levels over the next 12 to 18 months. A 1% increase in overall interest rates is equivalent to \$108 million of investment income and a 1% increase in discount rates means a 6% movement in the probability of adequacy of the outstanding claims provision, assuming that none of this increase is taken to profit.

In the past three decades, we have built a significant presence in the major insurance markets in Europe, the Americas and Australasia through our acquisition strategy and the development of our businesses. We will continue to maintain minimum performance hurdles for each product and each country. Our business plans for 2010 have been approved by the board and senior management. We have had to withdraw from some small portfolios which currently do not meet, and are unlikely to meet, our minimum hurdle requirements.

We will continue to pursue our successful strategy of growth, product diversification and geographic spread by acquisition. We have a number of experienced QBE teams around the world looking for acquisitions of insurance companies and distribution channels using our established criteria, particularly being earnings per share accretive in year one. In the past few years we have also targeted acquisitions of independent underwriting agencies with specialist insurance programme business to secure our distribution channels and product diversification. We have invested over \$1.6 billion in the acquisition of these agencies in the past two years. We expect the pre-tax return on our investment to be around 20% going forward. The acquired underwriting agencies, before allowance for the profit on new business underwritten by QBE, produced a pre-tax profit of \$323 million in 2009. We will continue to manage these agencies as part of our insurance businesses, ensuring that we foster the entrepreneurial approach adopted by the previous owners whilst maintaining and enhancing the value of these businesses.

QBE continues to lead the terms and conditions of most of the business written in the countries in which we operate. Our target is to increase the retention of our quality customers above the current high levels. We will focus on developing our people using our proven nine essential behaviours known by the acronym OPENUPQBE. We continue to maintain a low turnover of senior staff and have a pool of quality individuals capable of filling more senior roles in the Group. All of our teams around the world understand that they must operate within the parameters of our approved business plans and that capital will only be allocated to products capable of meeting our minimum return on equity requirements.

Over 75% of gross written premium is in foreign currencies and close to 46% of premium is written in US dollars. A 5% appreciation or depreciation of the Australian dollar against all currencies impacts gross written premium by around \$540 million and net profit after tax by around \$67 million. This significant volatility reduces if our presentation currency were US dollars. A number of large Australian companies report in US dollars rather than Australian dollars. We will review our position on the most appropriate presentation currency in 2010.

2010 is likely to be another difficult year for the insurance industry with a continuation of low interest yields and premium rate increases being less than claims inflation for many products. We are confident about our prospects for maintaining our underlying underwriting profit; however, the strengthening of the Australian dollar and the continued low interest rates will adversely impact our reported profit. Our focus on building our business through acquisitions will continue and we expect our shareholders to benefit significantly as interest rates rise on our high quality and short duration cash and fixed interest investment portfolio.

The 2009 result was an excellent achievement considering the difficult economic conditions. We would not have achieved our results without the dedication of our professional teams around the world. I appreciate the enormous support and loyalty that I receive from the QBE team. I also appreciate the support, guidance and encouragement that the directors have given to me, especially during the economic downturn.

I look forward to working with the QBE team to convert further acquisition opportunities and to further build the Group for the benefit of our shareholders going forward.

FM O'Halloran
Group chief executive officer

WORLDWIDE PORTFOLIO MIX

GROSS EARNED PREMIUM FOR THE YEAR ENDED 31 DECEMBER

	2009 %	2008 %
Property	29.5	27.4
Motor and motor casualty	19.3	19.6
Liability	15.2	16.8
Marine, energy and aviation	9.8	10.0
Workers' compensation	7.4	9.2
Professional indemnity	6.8	6.9
Accident and health	3.5	3.8
Other	3.5	2.5
Financial and credit	3.3	2.1
Bloodstock	1.7	1.7
Total	100.0	100.0

CONTRIBUTIONS BY REGION

FOR THE YEAR ENDED 31 DECEMBER	GROSS WRITTEN PREMIUM		NET EARNED PREMIUM		NET PROFIT AFTER INCOME TAX		COMBINED OPERATING RATIO	
	2009 \$M	2008 \$M	2009 \$M	2008 \$M	2009 \$M	2008 \$M	2009 %	2008 %
Australia	3,509	2,914	2,749	2,363	576	560	89.0	90.6
Asia Pacific	706	661	479	451	62	76	88.1	82.9
European operations	5,094	5,011	3,259	3,252	467	574	91.3	85.6
the Americas	5,146	4,462	3,250	3,108	397	281	89.7	93.6
Equator Re	2,564	2,231	2,412	1,913	468	368	88.2	83.8
Elimination – internal reinsurance	(2,564)	(2,137)	–	–	–	–	–	–
Total	14,455	13,142	12,149	11,087	1,970	1,859	89.6	88.5
Direct and facultative	13,007	11,779	10,651	9,828	1,552	1,697	91.6	88.0
Inward reinsurance	1,448	1,363	1,498	1,259	418	162	75.2	92.5
Total	14,455	13,142	12,149	11,087	1,970	1,859	89.6	88.5

OTHER INSURANCE RATIOS

FOR THE YEAR ENDED 31 DECEMBER	2009 %	2008 %	2007 %	2006 %	2005 %
Premium growth in Australian dollars					
Gross written	10.0	5.9	19.6	10.2	7.3
Net earned	9.6	8.6	25.2	10.5	8.9
Premium growth in US dollars ⁽¹⁾					
Gross written	2.0	6.0	32.6	9.3	10.6
Net earned	1.6	8.7	38.7	9.5	12.2
Reinsurance expense to gross earned premium	13.7	13.7	17.4	19.0	19.5
Insurance profit to average shareholders' funds ⁽²⁾	19.3	24.5	30.6	31.4	28.2

(1) The US dollar growth is calculated by reference to the US dollar amounts reported in the table on page 5.

(2) The 2008 ratio was weighted for the effect of the December 2008 share issue.

IMPACT OF EXCHANGE RATE MOVEMENTS

	2009 ACTUAL \$M	2009 AT 2008 EXCHANGE RATES ⁽¹⁾ \$M	EXCHANGE RATE IMPACT	
			\$M	%
Gross written premium	14,455	14,164	291	2
Gross earned premium	14,074	13,789	285	2
Net earned premium	12,149	11,979	170	1
Net investment income	1,237	1,225	12	1
Net profit after income tax	1,970	1,931	39	2
Total investments and cash	25,091	28,965	(3,874)	(15)
Total assets	40,964	47,288	(6,324)	(15)
Gross outstanding claims provision	18,033	20,912	(2,879)	(16)
Total liabilities	30,666	35,491	(4,825)	(16)

(1) Income statement items are restated to 31 December 2008 cumulative average rates of exchange and balance sheet items to 31 December 2008 closing rates of exchange.

Group financial targets and performance goals

2009 FINANCIAL PERFORMANCE

TARGETS*	ACTUAL
• Insurance profit margin of 16% to 18%	• Insurance profit margin of 17.0%
• Combined operating ratio of less than 88%	• Combined operating ratio of 89.6%
• Gross written and net earned premium growth of over 20%	• Gross written premium and net earned premium increased by 10%
• Reinsurance ratio of less than 13% of gross earned premium	• Reinsurance ratio of 13.7% of gross earned premium
• Combined commission and expense ratio of around 29.0%	• Combined commission and expense ratio of 29.3%
• Tax rate of around 24%	• Tax rate of 18%
• Maintain Group capital adequacy multiple of more than 1.5 times APRA's minimum requirement for insurance groups	• Capital adequacy multiple of 1.6 times the minimum requirement for insurance groups
• Gross investment yield of around 3%	• Gross yield of 4.1%

2009 OPERATIONAL PERFORMANCE

PERFORMANCE GOALS	ACTUAL
• Maintain high retention ratios on renewable business and protect our quality customer base	• Retention ratios were generally higher in all divisions
• Target premium rate increases in all portfolios – overall average up at least 4% on renewed business	• Overall average rate increases of 4% achieved
• Secure acquisitions that add value	• Four businesses acquired in 2009
• Maintain all key balance sheet ratios at levels that will provide security and flexibility for growth	• Ratio of borrowings to shareholders' funds reduced from 32.9% to 29.1%
• Extend the OPENUPQBE manager programmes to maintain our unique culture and management style	• Numerous OPENUPQBE programmes were run during 2009
• Maintain our low risk investment strategy and absolute return criteria	• No permanent impairment of any fixed interest investments since the commencement of the global financial crisis

* Targets assume: large individual risk and catastrophe claims do not exceed the significant allowance in our business plans; no overall reduction in premium rates; no significant fall in equity markets and interest rates; no major movement in budgeted foreign exchange rates; and no material change to key inflation and economic growth forecasts.

Strategy and planning

2010 FINANCIAL PERFORMANCE

TARGETS*

- Achieve an insurance profit margin between 16% and 18%
- Achieve a combined operating ratio of less than 89%
- Gross written and net earned premium growth of 3% in Australian dollars but 18% in US dollars
- A reinsurance ratio of less than 13.5% of gross earned premium
- A combined commission and expense ratio of less than 30%
- Achieve an income tax expense rate around 20%
- Maintain Group capital adequacy multiple of more than 1.5 times APRA's minimum requirement for insurance groups
- Achieve a gross investment yield of around 3%

2010 OPERATIONAL PERFORMANCE

PERFORMANCE GOALS

- Target an increase in our customer retention ratio
- Target overall premium rate increases of 2% on renewed business
- Secure acquisitions that add value, subject to our disciplined approach and acquisition criteria
- Maintain flexible balance sheet ratios to take advantage of opportunities
- Continue to develop our staff and protect our intellectual capital
- Maintain our cautious approach to investments
- Target increased use of our captive reinsurer, Equator Re, to reduce reinsurance costs and protect divisional operations
- Target a return on equity in excess of 15%

QBE has a business planning framework which ensures that there is a systematic and disciplined approach to planning throughout the Group.

The framework helps to:

- establish a clear direction and parameters for carrying on business in each product and operating division;
- build confidence in our ability to execute our corporate strategies and deliver against our business plans;
- more accurately project profitability and financial performance;
- improve alignment of internal resources with external opportunities;
- generate greater accountability and transparency in decision making; and
- target the reduction of uncertainty and volatility, thereby reducing the likelihood and impact of events that could threaten our ability to meet our business objectives.

The QBE board of directors approves the Group's strategy and detailed business plans prepared by management and reviews actual performance against the plans. The strategy is consistent with shareholder expectations, our corporate financial profile, our organisational culture and our capacity to manage risks effectively. The strategy and plans form the basis of our risk tolerance within the Group.

Business plans are developed for all classes of insurance business, for our investment portfolios and for all support functions. The plans clearly document our strategy for achieving financial targets and performance goals within the limits set. Annual budgets included in the business plans form the basis for delegating authorities to all managers and staff with specific responsibilities, including underwriters, investment managers and claims managers.

Business plans are subject to detailed review by local and Group senior management. They are prepared annually and actual results are monitored regularly to identify adverse trends so that remedial action can be taken at an early stage. Regular reporting to both local and Group boards on performance against the business plans, including action plans to correct adverse variances, is a fundamental control within the Group.

Risk management, regulatory developments and climate change

Our ability to manage risk is central to the success of our business. We have developed processes and controls over several years to identify and manage key areas of risk exposure. As risk management is a continuous process, our approach is targeted to ensure that risk management is enhanced and tailored to suit our business requirements whilst remaining within our risk tolerances.

GEORGE THWAITES
GROUP CHIEF RISK OFFICER



RISK MANAGEMENT

QBE's global risk management framework defines the risks that QBE is in business to accept and the key risks that QBE needs to effectively manage. The framework defines the structure and standards of control that are needed to manage these risks and meet strategic objectives. Through robust risk management across the business, QBE aims to:

- avoid unwelcome surprises by reducing uncertainty and volatility in the achievement of strategies and objectives;
- achieve competitive advantage by better understanding the risk environments in which we operate; and
- optimise risk and more effectively allocate capital and resources by assessing the balance of risk and reward.

Risk management is a continuous process and an integral part of quality business management. QBE's approach is to integrate risk management into the broader management processes of the organisation. Risks are identified and subject to rigorous evaluation throughout the business management cycle, which forms a key part of our governance structure and includes strategic and business planning. The cycle drives the setting of limits and authorities which are embedded in the monitoring and evaluation of performance.

The Group risk management policy, strategy and framework are incorporated in the daily management practices and business procedures of our Group head office and each of the divisions, providing a consistent approach to managing risk across the organisation. The implementation of risk management at the divisional level enables local management to use their specialised knowledge of each portfolio to ensure that risks are mitigated at that level. The consistency of approach allows a Group-wide view of relative risks and returns.

QBE's internal economic capital modelling ("ECM") process provides an important tool for assessment of the risk to reward profile of QBE's business units. During 2009, QBE worked with regulators and rating agencies worldwide to embed the ECM in regulatory and rating processes, and it has been approved by regulators for the setting of minimum capital in some of the countries in which QBE operates. The ECM allows a sophisticated quantification of QBE's risks and provides insight into the range of possible outcomes for the business and the interaction of insurance, market, credit and other profitability drivers. Inputs are set by risk managers and the experts across the business and this ensures the model uses expert knowledge of each of the risks to the business.

BLAIR NICHOLLS
GROUP CHIEF
ACTUARIAL OFFICER





Wild Oats XI, Sydney to Hobart 2008.

The ECM risk to reward profile is used for:

- allocation of capital;
- setting risk-based remuneration;
- setting regulatory minimum capital requirements; and
- reinsurance analysis.

Risk tolerances are in place for each of the categories of risk faced by the Group:

- insurance risk;
- operational risk, including loss of key QBE people;
- acquisition risk; and
- funds management and treasury risks.

By evaluating risks against our predetermined tolerances, QBE is able to direct resources appropriately and manage risk to acceptable levels. The Group's overall tolerance for each category of risk is defined in terms of the maximum pre-tax loss that the Group is prepared to accept whilst continuing to achieve profitability targets.

As part of the overall risk management process, QBE applies a rigorous methodology to assessing potential catastrophe claims including the use of realistic disaster scenarios, commercial catastrophe loss models and in-house catastrophe loss assessment tools. The outcomes of these assessments help to set the level of reinsurance required by QBE and, in conjunction with QBE's risk appetite and tolerance, determine the amount of risk that is retained by the Group in any one geographic region for a particular peril. After allowing for QBE's reinsurance purchases, the maximum event retention for QBE

The Sydney to Hobart Yacht Race starts in Sydney, Australia on Boxing Day. Considered one of the world's top three classic ocean races, it is a test of endurance, teamwork and skill in navigating the risk of unpredictable weather conditions. In the 2008 race, Wild Oats XI was the winner for an unprecedented fourth time in a row. It also retains its 2005 record for the fastest time in the history of the race. Wild Oats XI was placed second by a narrow margin in the 2009 race.

Risk management for QBE's global insurance operations requires interaction and negotiation with regulators in many jurisdictions and navigation of a complex governance environment. It is a tribute to the expertise and vigilance of QBE's global risk management teams headed by George Thwaites, Group chief risk officer, that QBE was awarded the insurance industry's Australian Federal Treasurer's Good Governance and Practice award for 2009.

is \$535 million at 31 December 2009. An important input into setting the risk tolerance is the planned allowance for large individual risk and catastrophe claims in the business plan. This is the level of claims that QBE can afford to fund in any one year without affecting the planned profitability of the Group. To provide greater certainty, QBE renewed a reinsurance cover for certain large individual risk and catastrophe claims between 8.9% and 10.9% of 2010 targeted net earned premium.

REGULATORY DEVELOPMENTS

The flexibility of QBE's principles-based risk framework enables us to adapt to changes in the regulatory or business environment. Regulators, rating agencies and investors continue to converge in their focus on understanding the risks taken by insurers, how they control those risks

and the capital required in order to provide adequate protection to policyholders and other stakeholders.

In April 2009, in response to the global financial crisis, the G-20 major economic powers established the Financial Stability Board to address vulnerabilities in the global financial system and to develop and implement strong regulatory, supervisory and other policies in the interests of financial stability. As the member of the Financial Stability Board responsible for international standards on the regulation of insurers, the International Association of Insurance Supervisors has issued a number of proposals which indicate that further extensions to supervision are likely to continue in several areas.

APRA continues to refine its prudential framework, with a particular focus on group supervision through the introduction of a number of requirements for insurance groups which took effect on 31 March 2009. A revised Solvency II proposal was adopted by the European Parliament in April 2009 and is expected to come into force on 31 October 2012. The US National Association of Insurance Commissioners is continuing to introduce various state-based reforms during 2010 against a background of potential federal regulation or oversight.

A significant majority of the major regulators overseeing the operations of the Group utilise a risk-based approach to both supervisory methodologies and capital models. Rating agencies also now either explicitly assess enterprise risk management in their rating process or include the key elements of risk management as part of their broader rating approach. Ongoing discussions with these stakeholders indicate that the QBE risk management framework meets expectations, and Standard & Poor's currently rates the Group as strong on enterprise risk management with an improving trend noted. QBE continues to be committed to sound and practical risk management in order to protect and enhance shareholders' and policyholders' interests.

CLIMATE CHANGE

QBE's products and services are insurance contracts that do not produce direct carbon emissions through use or disposal, and emissions relating to external distribution or logistics are negligible. To the extent that QBE Group's businesses have an indirect effect on the environment, we monitor the impacts and, where practical, Group companies adopt practices that are energy efficient and designed to eliminate waste. The Group chief risk officer and Group chief actuarial officer are responsible for monitoring and managing ongoing risks and opportunities relating to climate change in order to mitigate any adverse effect on QBE's businesses and to protect shareholders' funds.

Measurement of the Group's environmental impact to date has focused on two key carbon emission metrics being business air travel and electricity usage. Based on these key metrics, the Group's estimated carbon emissions (CO₂e) for 2009 were 46,440 tonnes (2008 47,420 tonnes), a decrease of around 2%. This can be summarised as:

- 760 tonnes of scope 1 direct greenhouse emissions due to natural gas and oil consumption used for heating (2008 520 tonnes);
- 34,610 tonnes of scope 2 indirect greenhouse emissions from electricity consumption (2008 36,700 tonnes); and
- 11,070 tonnes of scope 3 other indirect greenhouse emissions, defined as emissions relating to travel (10,200 tonnes in 2008).

The 2009 decrease was predominantly due to lower electricity usage by Australian operations. This was partially offset by an increase in air travel by staff in European operations and increased direct emissions such as natural gas usage for heating boilers.

QBE is a global business with a head office in Australia. The Group generates around 75% of its gross written premium offshore and long distance air travel is necessary to enable effective management of the business. QBE ensures that videoconferencing and teleconferencing are used wherever appropriate.

QBE's claims expenditure is usually in the form of financial indemnity to customers who incur their own expenditure for goods and services. We do not currently measure indirect emissions from QBE's supply chain or external distribution.

We continue to review other areas to eliminate waste, e.g. paper, printer and toner usage, the insurance policy documentation process and the utilisation of electronic storage and distribution facilities. In terms of paper usage, the annual reports for QBE Insurance Group Limited and its major operations are produced using high content recycled paper, non-petroleum based inks and environmentally safe printing processes. The annual report is available on our website on the day of release to the ASX and we encourage online access wherever practicable.

RISKS AND OPPORTUNITIES ASSOCIATED WITH CLIMATE CHANGE

At present, the insurance and financial services industries are not subject to specific emission limits and direct risks to QBE are not significant. QBE Group is aware of the potential indirect impacts of climate change on the general insurance and reinsurance industry and has identified key business risks and risk mitigation strategies.

One of the operational risks for QBE and the general insurance and reinsurance industry is the potential for increased claims costs due to the impact of climate change scenarios. An inherent strength of the QBE Group is a high level of product and geographical diversification which mitigates the potential impacts of extreme weather events in any one part of the world. This is evidenced by the strength of the Group's financial results over time even in years of extreme weather related events.

Our comprehensive systems and modelling of realistic disaster scenarios and property aggregate accumulations include assessment of the potential impacts of climate-related risks. The models used are regularly updated to incorporate the latest scientific evidence in relation to emerging climate change scenarios such as population shifts, changing property values, extra costs incurred for goods and services from demand surge and short-term and long-term seasonal weather forecasts.

General insurance companies also face asset risk relating to potential climate change impacts on the value of their investment portfolios. QBE adopts a low risk, absolute return investment strategy and at 31 December 2009 around 94% of the Group's investments comprised high quality and very liquid fixed interest securities and cash with equities currently representing less than 6% of total investments and cash.

QBE's product pricing decision framework takes into account the exposure of buildings and businesses to the adverse weather events. QBE allows discounts in its pricing for mitigation work undertaken to protect buildings and businesses from adverse weather. This effectively encourages QBE's clients to look at what can be done within their business to lessen the impact of any potential climate change exposure. An example of this is improvements on buildings to better withstand windstorms (e.g. cyclones, hurricanes, tornadoes and typhoons).

QBE people

With operations in 47 countries, QBE now employs in excess of 13,000 people worldwide. Our aim is to provide a working environment that continues to attract, develop and retain high quality employees.

JENNI SMITH
GROUP GENERAL MANAGER,
HUMAN RESOURCES



OUR PEOPLE STRATEGY

Our people are selected for their ability, experience, potential and 'can do' approach to their work. The continued development and retention of our people through our personal development, performance management and reward framework is recognised as paramount for QBE to achieve consistently high standards of business excellence and ultimately deliver superior returns to our shareholders. The Group maintains a focus on six key strategies which promote alignment of our employees' day to day activities and behaviours with our core business strategies and support the QBE vision and values. These key strategies are to:

- promote and enhance the OPENUPQBE culture across the Group;
- retain and attract quality people;
- offer competitive remuneration and rewards that encourage our people to perform to the highest standards whilst focusing on longer term commitment to retain and reward our key managers and senior employees;
- align employee performance with company objectives;
- develop our own talent and ensure succession planning is in place; and
- provide an effective Group-wide communication strategy that keeps our people informed.

QBE CULTURE

Underpinning our strategy of attracting, developing and retaining quality people is the OPENUPQBE programme which is actively promoted to staff across the Group. The programme, which was developed in 1994, has the full support of the Group board and is sponsored by the Group chief executive officer and Group chief operating officer. The programme is based on QBE essential behaviours which form the basis of our business performance and leadership standards and define the values which embody the QBE culture.

These behaviours provide consistency in all key activities and create a common language throughout our organisation. One of the Group's core strategies over the past 25 years has been diversification by product and geography, which has largely been achieved through over 125 acquisitions. The strength of the QBE culture has provided a platform for the successful integration of diverse teams from these acquisitions.



Jacob Burns of the Perth Glory.

OPENUPQBE IN ACTION

The OPENUPQBE programme continues to evolve and is now an established series of workshops on how the OPENUPQBE values and behaviours can be applied to increase the capabilities and commercial awareness of staff in key functional areas and, in so doing, deliver improved leadership and business skills. The content of the programme is written by experienced senior managers to provide rigour and credibility and deliver practical applications. The OPENUPQBE series of workshops is structured as action-learning programmes that immerse participants in intensive 'real' business projects. This enables the identification and leveraging of development opportunities for both the individual and the organisation that have direct relevance to actual business processes and operations. Within the framework of the QBE essential behaviours, the OPENUPQBE workshops exercise each individual participant's skills and develop their knowledge through the rigour of the business improvement projects, whilst management philosophies are explored through QBE case studies.

Since the workshop programmes were introduced, they have further increased awareness of the impact employees have upon QBE's key profit drivers and their contribution to the business. The fact that the most senior staff in QBE are engaged in the workshops, which offer personal guidance and clarity around expectations, is a unique and highly motivating factor for OPENUPQBE participants.

The OPENUPQBE programmes seek to reflect the essential behaviours as they are demonstrated in the workplace, highlighting their relevance as they manifest themselves within each functional area.

QBE's commitment to emerging sporting teams has been evident through a 13 year association with Hyundai A-League football team Perth Glory. QBE has supported the Glory from its inauguration in 1996 as the club quickly established itself as a powerhouse in the Australian football landscape, celebrating back to back championships in 2002-03 and 2003-04.

QBE's core values around leadership and business acumen are entrenched in the way we do business. It is pleasing that many of our QBE global teams and leaders have been acknowledged for their efforts in 2009. Amongst these were Frank O'Halloran who was named as Insurance Leader of the Year (Australia and New Zealand Insurance Industry Awards 2009); Neil Drabsch who was named as Chief Financial Officer of the Year (Australian Financial Review, CFO Magazine); and Peter Grove, our European operations' chief underwriting officer, who received the award for lifetime achievement in the London insurance and reinsurance market (Reactions London Market Awards 2009).

In addition to the common culture defined by the nine essential behaviours, business improvement projects continue to be one of the keys to the success of the OPENUPQBE programmes. By addressing key strategic and tactical issues within the Group through real business projects and case study teaching, OPENUPQBE aims to:

- broaden participants' business awareness;
- provide a forum for the generation and sharing of ideas;
- encourage communication that builds successful teamwork and understanding;
- identify best practice; and
- formulate and propose recommendations that will positively influence QBE's key profit drivers and deliver superior returns to shareholders.

PERFORMANCE MANAGEMENT, EMPLOYEE DEVELOPMENT AND SUCCESSION PLANNING

Our annual performance review process provides the forum for setting objectives and measuring employee performance, with most individuals assessed against QBE essential behaviours as outlined above. These essential behaviours are also the base for QBE's commitment to providing a range of personal development opportunities for employees to realise their full potential and progress within the organisation. Our principal goal is to ensure that the best people occupy the key positions at all levels of the business and that robust succession plans are in place for each of those roles. Key roles throughout the organisation have been identified and documented using a

- O** Open thinking
- P** Personal impact
- E** Entrusting
- N** Networking
- U** Utmost integrity
- P** Planning perspective
- Q** Quality customer focus
- B** Business acumen
- E** Entrepreneurship

Motivating our people

Driving decisions

Optimising outcomes

Delivering superior returns to shareholders

formalised succession management framework. As a result of cascading the succession planning process throughout the organisation, we have identified potential candidates for future technical and business leadership roles and their development needs. We have created a Group-wide talent management strategy which brings together all of our succession and people development activities into a single framework of consistent processes focused on identifying, developing and retaining high performing, high potential individuals for the future at all levels of the organisation.

REMUNERATION AND REWARD

2009 has been a year of significant focus on executive remuneration. In April 2009, the leaders of the G-20 endorsed the application of "sound compensation principles consistent with a company's long-term goals and prudent risk taking". APRA has since introduced a principles-based framework for the financial sector aligned with the G-20 recommendations which will become effective from April 2010. The Financial Services Authority in the UK and the US Department of Treasury have also produced similar guidelines.

As part of its ongoing activities, the QBE remuneration committee focuses on ensuring that remuneration and reward strategy and frameworks are aligned with robust risk management practices and strong governance principles. During 2009, the QBE remuneration and reward frameworks were reviewed by the remuneration committee and adjustments made to align with current best practice in the market, including the principles set out in the APRA guidelines. In summary, QBE aims to operate a total reward framework which is aligned with the interests of our shareholders and conveys to our people the full value they represent to the business. The total package includes all components from fixed remuneration, at-risk pay in the form of short-term and deferred compensation incentives as well as more intangible non-cash benefits such as development and career path opportunities. Full details are set out in the remuneration report on pages 56 to 76 of the annual report.

QBE operates in a competitive global market where the diversity of individual roles and the complexity of each operating environment is considered when designing remuneration and reward structures. QBE aims to provide a mix of financial and non-financial rewards to attract, motivate and retain high performing, 'can do' people within a cost structure aligned to shareholders' interests and which is sustainable in the long-term. Our very low turnover of senior and middle management staff demonstrates the effectiveness of our remuneration and reward system and other retention policies.

In order to encourage high levels of performance and to achieve our objective of increasing shareholder wealth, at-risk incentive arrangements are in place for most employees worldwide through participation in short-term incentive ("STI") arrangements. These arrangements reward individuals when they achieve or exceed financial targets and/or meet personal performance objectives. Our senior management group and other selected high performing individuals participate in an annual deferred compensation award, the Deferred Compensation Plan ("DCP"), with awards in the form of equity in QBE. The value of the DCP is linked to our future share price and hence to the creation of shareholder wealth. It also assists in the retention of key staff. Under the terms of the DCP applicable to the Group's 2009 performance, participants are granted conditional rights to fully paid shares. Participation in the annual equity award is contingent on meeting financial targets for STI purposes and there is a minimum vesting period of three or five years, other than for certain equitable circumstances, before the DCP conditional rights are exercisable. Also central to our incentive arrangements is the award of shares to staff (subject to meeting eligibility requirements) under the Employee Share and Option Plan ("the Plan") which has been in place since 1981. Around 10,200 of our employees at all levels of the organisation now hold shares in QBE through the Plan. Details of the Plan and the DCP are set out in the remuneration report and note 27 to the financial statements.

QBE IN THE COMMUNITY

QBE Group's involvement in the community is encouraged and is structured along divisional lines with initiatives being generated from the ground up. A common element is that QBE's community and social involvement is based around local initiatives about which employees are highly engaged and passionate. As well as donations by the Group and the divisions to numerous local charitable and other community organisations, QBE employees also make contributions through payroll deductions and giving of their time to local community volunteer projects.

The QBE teams around the world have identified various nominated charities for support in 2009. In Australia these included Mission Australia, Create Foundation, United Way and Breast Cancer Network and, in the UK, the Starlight Children's Foundation and the Lloyd's community programme. In the Americas, QBE staff engaged with a number of organisations across multiple states with a focus on four main areas: health; education; child and family welfare; and safety. Employees continue to participate in or volunteer at fundraising events which raises substantial amounts of money each year.

Group operations executive

The Group operations executive comprises the chief executive officer, the chief operating officer, the chief financial officer and the heads of the QBE insurance divisions. The key objective of this team is to build and control QBE's insurance businesses and to maximise opportunities available to the Group in the markets in which we choose to operate.



**FRANK
O'HALLORAN**

FCA, AGE 63

Mr O'Halloran was appointed chief executive officer in January 1998. He joined QBE in 1976 as Group financial controller. He was appointed chief financial officer in 1982, joined the board as director of finance from 1987 to 1994 and was director of operations from 1994 to 1997. Mr O'Halloran is a chartered accountant and has had extensive experience in professional accountancy for 14 years and insurance management for 33 years.



**NEIL
DRABSCH**

FCA, FAICD, FCIS, AGE 61

Mr Drabsch was appointed chief financial officer of QBE Insurance Group in 1994. He joined QBE in 1991 and was the Group company secretary from 1992 to 2001. Mr Drabsch has 43 years experience in insurance and reinsurance management, finance and accounting, including 24 years as a practising chartered accountant.



**VINCE
McLENAGHAN**

FANZIIF, AGE 50

Mr McLenaghan was appointed chief operating officer of the Group in 2006. Mr McLenaghan has been in the insurance industry for 33 years. During his 27 years with QBE, he has served in a number of general management roles including as managing director of our Australian and Asia Pacific operations.



**STEVEN
BURNS**

FCA, AGE 51

Mr Burns is chief executive officer of QBE's European operations. He is a chartered accountant and was finance director of the Janson Green managing agency at Lloyd's from 1987, prior to it being acquired by Limit in 1998. Mr Burns became chief executive officer of the Limit Group in August 2000. In September 2004, he was appointed chief executive officer of European operations as part of the restructure of our European company operations and Lloyd's division.



**JOHN
RUMPLER**

F Fin, FAIEx, AGE 49

Mr Rumpler was appointed president and chief executive officer, the Americas on 15 June 2009. He joined QBE in 1997 and led the development of QBE's international credit and surety businesses. Mr Rumpler was formerly a member of the QBE Australia executive team and held board positions on several QBE subsidiaries. Mr Rumpler has more than 28 years experience in international banking, government and insurance.



**TERRY
IBBOTSON**

PhD, MBA, BCom, AGE 64

Mr Ibbotson was appointed chief executive officer of QBE's Australian operations in 2007. He has 41 years experience in the insurance industry. Mr Ibbotson joined QBE in 1993 and since that time has served in various general management roles, including as chief operating officer of Australian operations.



**MICHAEL
GOODWIN**

BVSc, FIAA, FAICD, AGE 51

Mr Goodwin was appointed chief executive officer of QBE's Asia Pacific operations in 2007. He is an actuary and has been in the insurance industry for 18 years, having started his career with Mercantile Mutual. Mr Goodwin was deputy general manager of the QBE Mercantile Mutual joint venture when ING's half share was purchased by QBE in 2004 and became chief operating officer of Asia Pacific operations in 2006.

Operations overview

QBE is an international general insurance and reinsurance group underwriting most major commercial and personal lines classes of business through operations in 47 countries.

Australian operations

General insurance operations throughout Australia providing all major lines of insurance cover for personal and commercial risks.

	2009	2008
Gross written premium \$M	3,509	2,914
Gross earned premium \$M	3,328	2,800
Net earned premium \$M	2,749	2,363
Combined operating ratio %	89.0	90.6
Staff numbers	4,106	3,815

Major events impacting our Australian operations in 2009 were:

- The acquisition of Elders Insurance Limited and its agency distribution.
- The Victorian bushfires in February, resulting in significant loss of life and property damage.
- Ongoing weather-related insurance losses, particularly in Queensland and northern New South Wales.
- Significant claim activity in the trade credit portfolio arising from the global financial crisis.
- Excellent results from QBE LMI.
- Voted General Insurer of the Year by the National Insurance Brokers Association for the eighth successive year.

Asia Pacific operations

General insurance in 15 countries in the Asia Pacific region providing personal, commercial and specialist insurance covers, including professional and general liability, marine, corporate property and trade credit.

	2009	2008
Gross written premium \$M	706	661
Gross earned premium \$M	674	626
Net earned premium \$M	479	451
Combined operating ratio %	88.1	82.9
Staff numbers	1,298	1,273

Major events impacting our Asia Pacific operations in 2009 were:

- Typhoons and floods in Fiji, Philippines and Vietnam resulting in significant property damage.
- Implementation of a new integrated financial system across New Zealand and the Pacific and system improvements in Asia.
- Policies written in new Indian joint venture for the first time.
- Continuing broker relationship development resulting in significant new business.

European operations

Lloyd's division

The third largest manager of capacity and provider of capital at Lloyd's, writing commercial insurance and reinsurance business in the Lloyd's market.

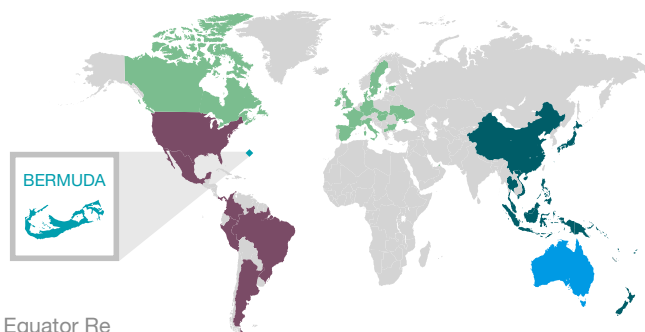
QBE Insurance Europe

General insurance business in the UK, Ireland and 15 countries in mainland Europe. Also writes reinsurance business in Ireland.

	2009	2008
Gross written premium \$M	5,094	5,011
Gross earned premium \$M	5,006	4,753
Net earned premium \$M	3,259	3,252
Combined operating ratio %	91.3	85.6
Staff numbers	2,869	2,808

Major events impacting our European operations in 2009 were:

- Growth achieved with financial performance maintained in challenging market conditions.
- UK National growth potential enhanced through brand building initiatives such as sponsorship of the UK's rugby union premier league.
- Leveraging of Lloyd's licences to start up new local offices in Dubai and Canada.
- Embedding advanced risk management activities in readiness for Solvency II.
- Initiated a substantial multi-year programme of change and rationalisation of our IT and operational landscape.



KEY

■ Australia ■ Asia Pacific ■ Europe ■ the Americas ■ Equator Re

the Americas

General insurance and reinsurance business in the Americas. Head office is in New York with operations in North, Central and South America and Bermuda.

	2009	2008
Gross written premium \$M	5,146	4,462
Gross earned premium \$M	5,066	4,590
Net earned premium \$M	3,250	3,108
Combined operating ratio %	89.7	93.6
Staff numbers	5,022	5,203

Major events impacting the Americas in 2009 were:

- Results favourably impacted by prior year agency acquisitions.
- Completion of some smaller portfolio acquisitions and new agency relationships.
- Creation of a divisional shared services company to achieve further operational efficiencies.
- Launched “QBE Connect”, an enhanced claims handling model for workers’ compensation business.
- Set up “QBE Select”, a vehicle to allow cross-selling of Regional and Specialty products to our intermediaries.

Equator Re

The Group’s captive reinsurer, Equator Re, provides reinsurance protection to, and assists the management of net exposure and capital levels for, the majority of the operating entities owned by the Group.

	2009	2008
Gross written premium \$M	2,564	2,231
Gross earned premium \$M	2,467	1,978
Net earned premium \$M	2,412	1,913
Combined operating ratio %	88.2	83.8
Staff numbers	17	15

Major events impacting Equator Re in 2009 were:

- Premium growth driven mainly by increased participations on proportional covers.
- Relative strength of the Australian dollar adversely impacted reported premium growth.
- Above average frequency of large individual risk claims.
- New underwriting and financial systems successfully implemented.

Investments

Management of the Group’s investment portfolio with over 99% of the Group’s investments managed in-house.

	2009	2008
Gross investment income \$M	1,097	766
Net investment income \$M	1,237	1,177
Gross investment yield %	4.1	2.9
Investments and cash \$M	25,091	28,541
Staff numbers	70	61

Major events impacting our investments in 2009 were:



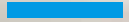










- Huge volatility in equity markets and credit spreads.
- Unprecedented financial stimulus to avoid systemic risk and economic recession.
- Historically low cash rates for an extended period of time.
- Very significant appreciation of the Australian dollar against the US dollar and sterling.

Australian operations

UNDERWRITING RESULT

FOR THE YEAR ENDED 31 DECEMBER		UNDERWRITING OPERATIONS		AGENCIES		AUSTRALIAN OPERATIONS	
		2009	2008	2009	2008	2009	2008
Gross written premium	\$M	3,509	2,914	-	-	3,509	2,914
Gross earned premium	\$M	3,328	2,800	-	-	3,328	2,800
Net earned premium	\$M	2,749	2,363	-	-	2,749	2,363
Net incurred claims	\$M	1,670	1,485	-	-	1,670	1,485
Net commission	\$M	379	316	(72)	(36)	307	280
Expenses	\$M	449	373	20	4	469	377
Underwriting result	\$M	251	189	52	32	303	221
Claims ratio	%	60.8	62.8	-	-	60.7	62.8
Commission ratio	%	13.8	13.4	-	-	11.2	11.8
Expense ratio	%	16.3	15.8	-	-	17.1	16.0
Combined operating ratio	%	90.9	92.0	-	-	89.0	90.6
Insurance profit to net earned premium	%					21.4	20.9

PORTFOLIO MIX

GROSS EARNED PREMIUM FOR THE YEAR ENDED 31 DECEMBER	2009		2008			2009		2008	
	%		%			%		%	
Property		20.3	23.7	Credit and surety		4.5	5.1		
Householders		15.3	13.1	Marine, energy and aviation		3.7	4.1		
General liability		11.6	13.8	Professional indemnity		3.6	4.4		
Motor and motor casualty		11.6	11.4	Accident and health		3.4	3.4		
Workers' compensation		8.9	9.7	Travel		1.4	2.0		
Lenders' mortgage insurance		7.5	2.3	Other		1.0	0.6		
Compulsory third party		7.2	6.4						

Australian operations produced another strong combined operating ratio of 89.0% compared with 90.6% last year. The improvement came despite claims from the Victorian bushfires and an increased frequency of attritional and large trade credit and surety claims from the global financial crisis. These were largely offset by an excellent underwriting profit from QBE Lenders' Mortgage Insurance ("QBE LMI"). The insurance profit margin improved slightly from 20.9% to 21.4%, which is an excellent result considering market conditions and when compared with the majority of our peers.

Gross written premium increased by 20% to \$3,509 million and gross earned premium increased by 19% to \$3,328 million. Growth was due to the full year impact of the acquisition of QBE LMI effective October 2008, the acquisition of Elders Insurance effective from 30 September 2009 and from new distribution channels, including acquired underwriting agencies. We achieved overall average premium rate increases on renewed business of 8% which compares favourably with the 1% increase achieved in 2008. Whilst customer retention

continues to remain high, we did not meet our new business targets primarily because of inadequate pricing. Net earned premium increased by 16% to \$2,749 million.

The claims ratio reduced from 62.8% to 60.7%. This reduction reflects the acquisitions made in 2008 and 2009 as well as the positive impact of increases in premium rates and higher claims discount rates. The claims ratio includes the cost of the Victorian bushfires net of reinsurance recoveries from Equator Re, our captive in Bermuda.

The combined commission and expense ratio increased slightly from 27.8% to 28.3%. The increase was entirely due to the cost of strategic initiatives, in particular new technology to further automate interfaces with financial institutions and other intermediaries and to improve bodily injury claims management. We continue to look for opportunities to further improve our efficiency and effectiveness by eliminating multiple handling of documentation and reducing paper flows with our customers. Our wholly-owned underwriting agencies performed better than anticipated with a contribution of \$52 million to the underwriting results compared with \$32 million last year.

The trade credit and surety portfolio was severely impacted by a high frequency of attritional and large individual risk claims from the global financial crisis. The increased frequency of claims primarily relates to policies written in 2007 and 2008. In late 2008 and early 2009, substantial action was taken to reduce exposure to a number of industry sectors and premium rate increases were significant on the remaining book of business. We are confident that the trade credit and surety account will return to profitability in 2010.

Homeowners and farm package portfolios were impacted by claims from the Victorian bushfires. Our workers' compensation, professional liability, general liability, commercial



package, property, commercial motor, aviation, comprehensive third party and lenders' mortgage insurance products all produced strong profits. The travel insurance portfolio produced a small underwriting profit following our decision to restrict our premium writings in some areas. The QBE LMI acquisition performed better than expected with greater premium growth and a reduction in mortgage defaults. We continue to retain the substantial risk margins QBE LMI held at the end of last year.

Australian operations was again voted "General Insurer of the Year" by members of the National Insurance Brokers Association. This is the eighth consecutive year that QBE has won this award recognising our high level of service, superior claims handling and competitive products.

The acquisition of Elders Insurance and Elders Insurance Agency has been consolidated from 30 September 2009. The results since that date have exceeded our expectations. Integration has commenced and teams are working on transferring and upgrading systems and substantially improving the interface with, and product availability to, Elders' large agency force.

An increase in claims cost on some portfolios and the continuation of adverse weather conditions have necessitated a further increase in premium rates. We expect overall average premium rate increases to be around 5% for 2010. This, together with the actions taken on trade credit, travel and homeowners portfolios, are aimed at improving the profitability of our business in Australia. Premium rate increases and the acquisition of Elders Insurance are likely to result in premium growth of over 15% in 2010. Assuming a full year of Elders

Australia has been a dominant force in relay swimming for over 50 years. When working together in a well co-ordinated team, individual performance often exceeds the swimmer's personal best. At QBE we encourage and nurture individuals to perform beyond their best and set new personal standards.

QBE won the National Insurance Brokers Association General Insurer of the Year award. It is arguably Australia's most prestigious general insurance industry recognition. The winner is selected by practising insurance brokers for their performance on a range of important product and service quality factors.

business, our premium in Australia has grown by around 60% in the last four years mainly from acquisitions and strong support from intermediaries.

We continue to identify new strategic initiatives to improve our top and bottom line going forward. Subject to large individual risk and catastrophe claims not exceeding the allowances in our business plans, we expect an improved combined operating ratio and insurance margin in 2010. Our expectations will be assisted by the premium rate increases achieved in 2009 and anticipated in 2010.

We have a high quality, experienced team of insurance professionals and management in Australian operations with a track record of outperforming our peers. We have a strong market share in commercial lines insurance and excellent results for many of our products. The minimum return on equity requirements of 15% are being achieved for the majority of our portfolios. We are confident in the outlook for our Australian business for 2010 and opportunities for further building our business.

A big thank you to the entire Australian operations team for their continued hard work, the professional way in which they managed the Victorian bushfire claims and for the enormous contribution they have made to the success of our Australian operations over many years.

Terry Ibbotson

Chief executive officer – Australian operations

Asia Pacific operations

UNDERWRITING RESULT

FOR THE YEAR ENDED 31 DECEMBER

		2009	2008
Gross written premium	\$M	706	661
Gross earned premium	\$M	674	626
Net earned premium	\$M	479	451
Net incurred claims	\$M	223	186
Net commission	\$M	99	93
Expenses	\$M	100	95
Underwriting result	\$M	57	77
Claims ratio	%	46.5	41.2
Commission ratio	%	20.7	20.6
Expense ratio	%	20.9	21.1
Combined operating ratio	%	88.1	82.9
Insurance profit to net earned premium	%	14.8	24.8

PORTFOLIO MIX

GROSS EARNED PREMIUM

FOR THE YEAR ENDED 31 DECEMBER

	2009 %	2008 %		2009 %	2008 %
Property	22.1	21.8	Accident and health	6.0	6.7
Marine	14.7	14.2	Engineering	4.5	4.7
Motor and motor casualty	14.2	14.7	Financial and credit	3.9	3.7
Professional indemnity	12.3	12.5	Householders	2.1	2.2
Liability	9.3	9.5	Travel	1.8	1.9
Workers' compensation	7.4	6.5	Other	1.7	1.6

Asia Pacific produced another strong underwriting result despite an increase in the frequency of catastrophes during the year. The combined operating ratio was 88.1% compared with 82.9% last year. New Zealand, Pacific Islands, Singapore, Malaysia, Indonesia, Vietnam, Hong Kong and Macau continued to produce strong underwriting profits. The Philippines experienced five typhoons and Fiji experienced two cyclones, all creating extensive flood damage. 12 of the 15 countries in which we operate produced underwriting profits with the exceptions being the Philippines, Fiji and Thailand.

The insurance profit margin was much lower at 14.8% compared with 24.8% last year. The lower margin was due to catastrophe claims and the considerable reduction in interest yields on investments set aside to meet policyholders' liabilities.

Gross written premium was up 7% to \$706 million and gross earned premium was up 8% to \$674 million. This growth was due to continued high customer retention and solid organic growth through major intermediaries. Overall average premium rates increased by 1%, in line with expectations. Strong premium rate increases are being achieved in New Zealand and the Pacific Islands; however, Asia continues to remain very competitive. Net earned premium increased by 6% to \$479 million. Net earned premium is after deducting quota share reinsurance at market rates with our captive insurer, Equator Re.

The claims ratio increased from 41.2% to 46.5%. The increase was largely due to the increase in frequency of catastrophes. It has been a long time since the Asia Pacific team experienced the level of catastrophe and large claim activity of 2009. In the circumstances, we are very pleased with the 2009 underwriting results. These results compare favourably with our peers in the majority of the countries in which we operate. The combined commission and expense ratio was 41.6% compared with 41.7% last year. The expense ratio improved slightly reflecting the efficiencies of new systems implemented in 2007 and 2008.

We are very pleased with the development of our relationships with international brokers in Asia Pacific. We have increased and strengthened our technical expertise to support this business initiative. We have also generated new business from the close working relationships we have developed with portfolio underwriters in our European operations division. We expect to see further growth from major intermediaries going forward.



New Zealand women's double sculls team.

The Evers-Swindell twins from New Zealand won gold in the women's double sculls rowing event in the Athens 2004 and Beijing 2008 Olympics. The pair have dominated the event in recent years winning the 2002 and 2003 world championships and were named as the Rowing Female Crew of the Year by the International Rowing Federation in 2005. Rowing has been an Olympic event since 1900 and is a sport requiring a fine balance between speed and endurance resulting in some of the highest power outputs of athletes in any sport.

QBE's New Zealand operation is among the most profitable in the Asia Pacific division with a comprehensive range of products in the corporate, commercial and professional insurance sectors. Our New Zealand specialist underwriting and claims teams draw upon local expertise and networks established over many years, as well as having access to the broader international QBE Group network.

Our joint venture in India, Raheja QBE General Insurance Company Limited, commenced writing business during the year. We are taking a cautious approach to growing this business due to the substantial reduction in premium rates following the elimination of the tariff in that market. QBE has a 26% interest in the joint venture and we have the right to increase our holding to 50% when permitted by the regulators.

We aim to finalise our strategy for China this year and are only interested in distributing our core commercial lines products. QBE has had a representative office in Guangdong province since 1997.

We continue to enhance the new systems that were successfully implemented in all our major operations. Our current initiatives are designed to improve our efficiency and our interface with intermediaries. We continue to build on our highly cost effective applications development centre in the Philippines, which provides low cost support services to our Asia Pacific operations. We will continue to develop this centre to further provide efficiencies and benefits for the QBE Group going forward.

We continue to focus on maximising customer retention and increasing our specialist product writings through major international brokers. We are also building on our 6,000 strong agency force. We anticipate overall average premium rate increases to be less than 1% in 2010. Subject to the Australian

dollar remaining at current levels, we expect growth of 10% in gross written premium in 2010.

We continue to look at acquisition opportunities but to date we have not been successful due to price expectations and the quality of balance sheets.

We expect the substantial majority of our products and countries in which we operate to meet QBE's minimum return on equity requirements. We have an excellent business throughout Asia Pacific, a dedicated team of professionals and a strong track record of profitability. We are confident that the 2010 underwriting profit will remain strong and in line with that achieved for 2009, subject of course to large individual risk claims and catastrophes not exceeding the allowance in our business plans.

I sincerely appreciate the hard work and significant contribution from the Asia Pacific team during the past year. I also appreciate the continued support we receive from our joint venture partners and our intermediaries.

Michael Goodwin
Chief executive officer – Asia Pacific operations

European operations

UNDERWRITING RESULT

FOR THE YEAR ENDED 31 DECEMBER

		2009	2008
Gross written premium	\$M	5,094	5,011
Gross earned premium	\$M	5,006	4,753
Net earned premium	\$M	3,259	3,252
Net incurred claims	\$M	2,010	1,762
Net commission	\$M	541	537
Expenses	\$M	426	483
Underwriting result	\$M	282	470
Claims ratio	%	61.6	54.2
Commission ratio	%	16.6	16.5
Expense ratio	%	13.1	14.9
Combined operating ratio	%	91.3	85.6
Insurance profit to net earned premium	%	15.6	25.3

PORTFOLIO MIX

GROSS EARNED PREMIUM

FOR THE YEAR ENDED 31 DECEMBER

	2009	2008		2009	2008
	%	%		%	%
Marine, energy and aviation	21.3	21.3	Property treaty	9.9	9.8
Public/product liability	18.7	18.6	Workers' compensation	6.3	7.7
Professional indemnity	15.2	14.2	Financial and credit	3.1	2.0
Property facultative and direct	10.7	10.0	Other	2.5	3.6
Motor and motor casualty	10.5	11.1	Accident and health	1.8	1.7

Our European operations produced another strong technical result despite the challenging market conditions. European operations comprises general insurance business written in the United Kingdom, Ireland and 15 countries in mainland Europe. It also includes general insurance and reinsurance business written in the Lloyd's market and reinsurance business written through our Dublin office.

Our business is now managed along product lines rather than by entity. We have specialist teams in each of casualty, property, commercial motor, aviation, marine and energy, specialty and reinsurance looking after business written in Lloyd's, the United Kingdom, Ireland and European markets.

As mentioned in our half year report, this means it is no longer appropriate to report our results by entity; however, as a large percentage of "catastrophe" business is written through our Lloyd's syndicates, 2009 saw a continuation of a very strong performance in Lloyd's with excellent profitability in marine and energy, international liability and reinsurance.

Our European operations experienced an increase in attritional claims and substantially lower savings on prior year claims provisions. As a result, the combined operating ratio was 91.3% compared with 85.6% last year. Trade credit, asset protection, property, aviation and UK professional liability portfolios were all affected by the increase in attritional claims ratios which was largely due to the economic downturn from the global financial crisis, together with inadequate pricing prevailing in some lines of business. Our general liability, marine and energy and reinsurance businesses continued to produce excellent results assisted by a low level of catastrophes during 2009. The insurance profit margin was 15.6% compared with 25.3% last year. The insurance profit margin was also affected by lower yields on investments set aside to meet policyholders' liabilities.

The stronger average Australian dollar against sterling restricted the increase in gross written premium to 2% or \$5,094 million. Gross earned premium increased by 5% to \$5,006 million. In sterling, gross written premium income grew by 11%. Growth was partly assisted by overall average premium rate increases of 4.5%, the acquisition of the Burnett's energy and Endurance property portfolios and teams and growth from the increase in our technical expertise and presence in regional United Kingdom and mainland Europe. We continue to deliver



Guinness Premiership, Harlequins v Gloucester.

excellent business retention levels. New business was less than anticipated due to inadequate pricing, particularly for property, aviation and some lines of liability business.

Net earned premium was unchanged at \$3,259 million, primarily due to the increased quota share reinsurance at market rates to our captive reinsurer, Equator Re. The claims ratio was 61.6% compared with 54.2% last year. The increase was due to a higher attritional claims ratio, particularly on the classes highlighted above, and substantially lower savings on prior year claims provisions. This increased frequency has meant that we have taken a more cautious approach to reserving for the 2008 and 2009 underwriting years for those lines of business.

The 2006, 2007 and 2008 financial years experienced sizeable releases from prior year claims provisions following the substantial price increases and tightening of policy terms and conditions in 2003 to 2005. The 2009 financial year saw releases at more normalised levels. We expect these more normalised levels to be the case going forward.

The combined commission and expense ratio was 29.7% compared with 31.4% last year. The reduction is very pleasing and partly reflects the profit commission received from

QBE is the official insurance partner of the UK's Guinness Premiership and the England rugby team. The Guinness Premiership is considered the world's most competitive domestic rugby union competition and currently features 12 top flight English teams. Partnering with the UK's elite rugby teams is a reflection of QBE's commitment to supporting specialists on and off the sporting field.

QBE is dedicated to team effort both within its own organisation and through the sports it supports. QBE was rated first in the market for claims service (June 2009, Gracechurch Survey), among the top three insurance companies for service overall by Insurance Times, 2008 and was chosen as the "most competitive insurer" by Post Magazine, July 2009.

external names on syndicate 386 and from Equator Re. We have commenced a business support transformational change programme under which we are substantially outsourcing the majority of our information technology support and development. This includes the early retirement of many of our legacy IT systems from previous acquisitions and consolidation on to a small number of core platforms going forward. This will mean more expenditure over the next two years but improved system performance, scalability and cost efficiencies beyond that date.

The December and January renewals have seen overall rate increases of close to 2%. This included a modest

reduction in inward reinsurance rates as expected given the low level of catastrophes in 2009. It is disappointing that the required increases in property, liability and commercial motor rates are not being achieved. Therefore we continue to focus on retaining our quality customers and we are pleased that retention remains around the 90% range. We are pleased to see that aviation, financial institutions and solicitors' professional liability premium rates have risen in response to the losses the industry has experienced. The cost of the outward reinsurance protections purchased for 2010 is slightly lower than 2009 and in line with plan.

We are the third largest manager and provider of capacity in the Lloyd's market. QBE provides 100% of the capacity for sub-syndicates 566, 2000, 1036, 5555 and 1886, which trade under the umbrella syndicate 2999, and 70% of the capacity for syndicate 386. Our Lloyd's capacity for 2010 has increased by over a quarter compared with 2009 to £1.4 billion, largely reflecting Lloyd's requirements to allow for the weakness of sterling against the major currencies, particularly the US dollar. Approximately 53% of the business we write in Lloyd's is written in US dollars.

The minimum capital requirements for our London based insurer QBE Insurance (Europe) Limited ("QIEL") and our Lloyd's managing agent QBE Underwriting Limited ("QUL") are mainly determined by the UK regulator, the Financial Services Authority ("FSA").

Changes over recent years to more stringent, risk-based criteria have generally increased the capital requirements. The pan-European Solvency II proposals, due in 2012, continue this trend and place more onus on QBE to assess its own risks and related capital requirements. In response to this new regime, we are well advanced in developing our internal risk and capital models and have already strengthened capital for the regulated entities where appropriate. QIEL has admissible capital levels of approximately 1.4 times the FSA enhanced capital requirement benchmark and our Lloyd's capital provider has eligible capital for funds at Lloyd's in excess of £860 million to support 2010 expected premium capacity.

QIEL has an A+ financial strength rating and our Lloyd's syndicates benefit from the overall A+ rating for Lloyd's.

We have further built on our initiatives for the distribution of our core lines of business outside the London market in the United Kingdom and in France, Germany, Italy, Spain and Ireland. In sterling, our gross written premium outside of the London market grew by 12% to £657 million. We now have a significant number of operations in mainland Europe and in regional United Kingdom. We experienced an increased frequency in property claims in France and Germany which affected their results. We will be strictly controlling growth in the UK regions and mainland Europe until pricing improves in core lines.

We have opened representative offices in Canada and Dubai to support our Lloyd's business. Our Central European businesses in Bulgaria, the Czech Republic, Estonia, Hungary, Macedonia, Romania, Slovakia and the Ukraine continue to develop in line with our plans and produce overall underwriting profits. The insurance operations acquired in Switzerland in 2007 and our recently established branch in Sweden are fully operational and will benefit from the product expertise in our London office.

The performance of some minor segments of our core portfolios has been below the Group's minimum return on equity requirements of 15%. We have exited classes of business where we believe that the Group's requirement cannot be met in the long-term and have cut back our underwriting in those where the short-term return is being impaired by poor pricing or increased attritional claims. Our focus is on products that will allow us to maximise the return on allocated capital. We are working closely with our colleagues in the Asia Pacific, Australian and Americas divisions on developing existing products and new opportunities. We continue to segment our business and look for ways to improve our profitability and efficiency.

We do not anticipate strong growth in 2010. Our expectation is for overall average premium rate increases to be around 2% and we will remain cautious on new business growth. We expect a slow down in the frequency of claims that we consider resulted from the economic downturn. We are targeting a combined operating ratio in 2010 between 90% and 95%. This is of course subject to large individual risk and catastrophe claims not exceeding the allowance in our business plans.

We are disappointed that many of our competitors do not also share our resolve to achieve greater premium rate increases than are currently being achieved, nor do they appear to set adequate return on equity targets for their underwriters.

European operations has continued to produce excellent returns for our shareholders. These strong returns would not have been achieved without our strong team of professional underwriters and our claims management, actuarial, finance and operations support staff. I sincerely thank the team for the enormous support I receive and the contribution they have made to another healthy return on allocated capital of 23.1% based on management results.

Steven Burns

Chief executive officer – European operations



the Americas

Our Americas businesses produced a very satisfactory underwriting and financial result considering the difficult economic environment. Our significant Americas business comprises specialty insurance programmes, regional insurance and reinsurance businesses in the US, four general insurance operations in Argentina, Brazil, Colombia and Mexico and five wholly-owned underwriting agencies.

The specialty insurance programme business focuses on a number of products, mainly written through 71 managing agents who have a proven track record of profitability. The specialty business includes the results of the wholly-owned managing agents that were acquired in the past three years, namely ZC Sterling, Community Association Underwriters, Deep South, SIU and SLG Benefits and Insurance. Our regional insurance business comprises property and casualty products that are distributed by General Casualty, National Farmers Union and QBE AGRI brand names through independent and captive agents throughout the US. Our focus is on small to medium sized businesses. The reinsurance business covers small to medium regional insurers with a limited net exposure to major catastrophes or nationwide clients.

UNDERWRITING RESULT

FOR THE YEAR ENDED 31 DECEMBER		UNDERWRITING OPERATIONS		AGENCIES		THE AMERICAS	
		2009	2008	2009	2008	2009	2008
Gross written premium	\$M	5,146	4,462	-	-	5,146	4,462
Gross earned premium	\$M	5,066	4,590	-	-	5,066	4,590
Net earned premium	\$M	3,250	3,108	-	-	3,250	3,108
Net incurred claims	\$M	2,009	1,884	(17)	(12)	1,992	1,872
Net commission	\$M	697	632	(239)	(43)	458	589
Expenses	\$M	476	436	(11)	13	465	449
Underwriting result	\$M	68	156	267	42	335	198
Claims ratio	%	61.9	60.6	-	-	61.3	60.2
Commission ratio	%	21.4	20.3	-	-	14.1	19.0
Expense ratio	%	14.6	14.0	-	-	14.3	14.4
Combined operating ratio	%	97.9	94.9	-	-	89.7	93.6
Insurance profit to net earned premium	%					14.7	11.5

PORTFOLIO MIX

GROSS EARNED PREMIUM FOR THE YEAR ENDED 31 DECEMBER		2009	2008			2009	2008
		%	%			%	%
Property		29.3	24.4	Accident and health		4.8	5.9
Motor and motor casualty		29.1	30.4	Other		3.9	2.9
Casualty		14.5	17.5	Bloodstock		3.2	3.0
Workers' compensation		7.6	10.9	Financial and credit		2.6	0.3
Householders		5.0	4.7				

QBE's operations in the Americas produced a combined operating ratio of 89.7% compared with 93.6% last year. The insurance profit margin was 14.7% compared with 11.5% last year. The combined operating ratio benefited from the results of the wholly-owned managing agents and lower attritional and catastrophe claims. These were partly offset by reduced savings on central estimates of prior year claims provisions. The insurance profit margin improved over last year from higher underwriting profits offset by lower yields on investments set aside to meet liabilities to policyholders. Our return on allocated capital for 2009 using management results was 17.1%.

Gross written premium was up 15% to \$5,146 million and gross earned premium was up 10% to \$5,066 million. Growth was assisted by the acquisition of ZC Sterling in late 2008 and the weaker average Australian dollar when compared with last year. Gross written premium in US dollars increased by 7%. Customer retention remains high; however, new business was difficult to convert mainly due to inadequate pricing. Overall average premium rates increased by 2%, in line with expectations.

Net earned premium increased by 5% to \$3,250 million. This growth was lower than the growth in gross earned premium primarily because of additional proportional reinsurance ceded at market rates to our captive, Equator Re. Total reinsurance expense was 36% of gross earned premium compared with 32% last year. Approximately 84% of the reinsurance expense was proportional reinsurance.

The net claims ratio increased from 60.2% to 61.3%. The increase was due to reduced savings on prior year claims provisions partly offset by lower attritional and catastrophe

claims. The actions taken on a number of our portfolios in QBE Regional and QBE Specialty resulted in a reduction in the 2009 accident year attritional claims ratio by 4% and 5% respectively.

The combined commission and expense ratio reduced from 33.4% to 28.4%. The reduction was due to the increased contribution from acquired underwriting agencies where the commission margin paid to those agents is eliminated on consolidation.

The specialty insurance programme gross written premium grew by 17% to US\$1,863 million. The increase from last year was due to the new premium derived from the acquisition of ZC Sterling. We cancelled some business during the year due to inadequate pricing, particularly commercial auto and workers' compensation business. We also were affected by lower premiums driven by declining construction associated with the economic downturn.

Gross written premium from regional business reduced by 7% to US\$1,340 million. The lower premium income was due to underwriting actions implemented to reduce the attritional claims ratio in a number of products and a significant reduction in sums insured for many of our clients arising from the adverse economic conditions experienced in 2009. Our customer retention remains high for the business we wish to retain.

Our reinsurance operations increased gross written premium by 17% to US\$437 million. This increase was mainly attributable to strong premium rate increases, new business and increased shares on business ceded by existing clients.

Our Latin American operations increased gross written premium by 9% to US\$352 million. In local currencies, all countries



produced considerable growth with Argentina at 11%, Brazil at 53%, Colombia at 29% and Mexico at 14%. Due to generally weaker exchange rates for these currencies during 2009, this growth reduced when consolidated and reported in Australian dollars. The Latin American operations produced strong underwriting profits and a return on allocated capital well in excess of the Group's minimum requirements.

We have substantially grown our business in the US over a number of years through acquisitions. These acquisitions include five specialist product underwriting agencies which contributed \$267 million to the underwriting profit compared with \$42 million last year. Gross written premium to QBE from the acquired underwriting agencies was US\$794 million and this is expected to increase to US\$1,042 million in 2010, primarily due to additional premium income from the ZC Sterling acquisition.

The QBE Specialty and QBE Regional businesses both experienced lower attritional and catastrophe ratios offset by reduced savings on prior year claims provisions. Improvements in the current accident year claims ratios were partly offset by a higher expense ratio, particularly in QBE Regional.

We are pleased with the current claims ratios on our portfolios in the US and Latin America; however, we need to increase efficiencies through the consolidation of legacy systems,

Baseball is an iconic national sport which is played across North America from junior league to professional level. The New York Yankees are considered to be one of the best baseball teams of all time and in 2009 they won their 27th world series, a record in the history of the championship.

QBE the Americas' extensive national intermediaries network was recognised by its peers in 2009 when QBE's General Casualty companies received the 2009 Interface Partner Award from insurance technology company Applied Systems. The award recognised General Casualty's achievements in agency carrier communication, leadership and innovation.

improved automation of many manual processes that support our agents and partners and investment in enhanced technology to support our business and customer objectives.

We expect overall average premium rate increases of around 1% in 2010; however, we also expect the difficult economic conditions to continue. We are targeting to increase gross written premium by 10% in US dollars, mainly on the back of the acquired underwriting agencies.

We have four quality insurance businesses in the Americas and five specialist underwriting agencies. We believe that the US economy will remain difficult for

at least the next 12 to 18 months; however, we are confident that we can build our businesses and maintain our underwriting profitability. This is, of course, subject to large individual risk and catastrophe claims not exceeding the allowances in our business plans.

We have a strong team of professionals in the Americas which has worked diligently to integrate the acquisitions, continually meet our clients' needs and deliver the QBE Group's return on equity requirements. I sincerely appreciate the enormous support that I have received since my appointment in June 2009.

John Rumpler
President and chief executive officer – the Americas

Equator Re

UNDERWRITING RESULT

FOR THE YEAR ENDED 31 DECEMBER

		2009	2008
Gross written premium	\$M	2,564	2,231
Gross earned premium	\$M	2,467	1,978
Net earned premium	\$M	2,412	1,913
Net incurred claims	\$M	1,433	1,083
Net commission	\$M	567	410
Expenses	\$M	127	111
Underwriting result	\$M	285	309
Claims ratio	%	59.4	56.6
Commission ratio	%	23.5	21.4
Expense ratio	%	5.3	5.8
Combined operating ratio	%	88.2	83.8
Insurance profit to net earned premium	%	17.4	20.8

PORTFOLIO MIX

GROSS EARNED PREMIUM

FOR THE YEAR ENDED 31 DECEMBER

	2009 %	2008 %		2009 %	2008 %
Public/product liability	22.1	20.5	Householders	4.7	2.1
Property	21.2	25.9	Other	1.4	0.5
Motor and motor casualty	19.6	15.2	Financial and credit	1.3	1.4
Marine, energy and aviation	15.2	16.2	Accident and health	1.2	2.0
Workers' compensation	7.9	8.4	Lenders' mortgage insurance	0.7	3.7
Professional indemnity	4.7	4.1			

DES FOGARTY

PRESIDENT - EQUATOR RE



Equator Re is QBE's wholly-owned captive reinsurer based in Bermuda. It provides reinsurance protections for QBE's operations around the world to assist in management of the Group's capital, balance sheet and net exposure to large individual risk and catastrophe claims. Equator Re provides protections to the Group's operations below the retentions deemed appropriate for the overall Group. A number of these protections include participation on various excess of loss and proportional reinsurance protections purchased from external reinsurers.

The exposures written by Equator Re are included in the Group's maximum event retention which is the estimated maximum net claim from the largest single realistic disaster scenario. The business written by Equator Re is subject to independent pricing including third party benchmarking where necessary.

Equator Re continued its record of strong results and produced a combined operating ratio of 88.2% compared with 83.8% last year and an insurance profit margin of 17.4% compared with 20.8% last year. The higher combined operating ratio and lower insurance profit margin is primarily due to Equator Re's increased exposure to proportional reinsurance from a number of the Group's operations.

Gross written premium was up 15% to \$2,564 million and gross earned premium was up 25% to \$2,467 million. The growth primarily came from the additional proportional reinsurance business written by Equator Re, in particular from the acquisitions made in the US and our



European operations. Net earned premium increased by 26% to \$2,412 million. All internal gross written and gross earned premium in Equator Re is eliminated on consolidation.

The claims ratio increased from 56.6% to 59.4%. The increase was largely due to the additional proportional business written, the increase in claims from trade credit and property portfolios as a result of the global financial crisis and Equator Re's share of other large individual risk and catastrophe claims including the Victorian bushfires.

The combined commission and expense ratio increased from 27.2% to 28.8%. This increase was due to the increase in proportional reinsurance business written and profit commissions paid to Group companies. The expense ratio includes Equator Re's share of expenses ceded by Group companies on proportional reinsurance contracts and a share of Group head office costs.

For 2010, we expect net earned premium to grow by around 5%, primarily from increased participations on excess of loss protections. Our comprehensive loss modelling has enabled us to identify a number of reinsurance contracts which Equator Re considers are appropriate for higher retention by the Group. To offset the increase in exposure, Equator Re has purchased

Relay teams from the Caribbean have set new standards at recent Olympic games, most recently the gold medal winning Jamaican 4x100m relay team in the 2008 games in Beijing. Not only do the individuals within a relay team need an elite level of ability, they must have a high level of trust in each other so the baton is passed safely. The concept of "entrusting" individuals to motivate high performance is one of the QBE essential behaviours.

The experienced Equator Re team works closely with QBE insurance operations around the world to reduce external reinsurance costs, optimise capital and manage exposures to within the Group's appetite for risk.

additional catastrophe reinsurance to ensure that the Group's maximum event retention is not exceeded. Subject to large individual risk and catastrophe claims not exceeding the substantial allowances in our business plans, we expect Equator Re to produce a combined operating ratio of less than 90% for 2010.

Equator Re had shareholders' funds at year end of \$1.4 billion and a Standard & Poor's financial strength rating of A+. Equator Re is a significant part of QBE's strategy for the management of capital, maximum event retention and large individual risk and catastrophe claims

throughout the Group. Our strategy will continue to be the provision of the appropriate levels of reinsurance protection for QBE operations whilst eliminating unnecessary external reinsurance costs.

Equator Re has a small team of professionals which manages a large number of reinsurance contracts and exposures that are written to protect the Group companies and to meet return on equity requirements. I appreciate the enormous support, hard work and dedication of my team.

Des Fogarty
President – Equator Re

Investments

INVESTMENT INCOME

FOR THE YEAR ENDED 31 DECEMBER	POLICYHOLDERS' FUNDS		SHAREHOLDERS' FUNDS		TOTAL INVESTMENT INCOME	
	2009 \$M	2008 \$M	2009 \$M	2008 \$M	2009 \$M	2008 \$M
Equity income	-	-	148	(490)	148	(490)
Income on fixed interest, short-term money and cash	706	889	275	367	981	1,256
Property income	-	-	(40)	7	(40)	7
Gains on sale of controlled entities	4	-	4	-	8	-
Other income	2	6	(2)	(13)	-	(7)
Gross investment income	712	895	385	(129)	1,097	766
Foreign exchange gains	119	29	246	380	365	409
Borrowing costs	-	-	(219)	(240)	(219)	(240)
Realised gain on repurchase of capital securities	-	-	70	303	70	303
Other expenses	(29)	(16)	(40)	(22)	(69)	(38)
Net cost of ABCs	-	-	(7)	(23)	(7)	(23)
Net investment income	802	908	435	269	1,237	1,177
Gross investment yield %	3.9	5.0	4.4	(1.5)	4.1	2.9
Net investment yield %	4.4	5.3	8.0	4.6	5.3	5.1

CURRENCY MIX

MARKET VALUE OF EQUITIES	2009 %	2008 %	MARKET VALUE OF TOTAL INVESTMENTS AND CASH	2009 %	2008 %
Australian dollar	43	36	Australian dollar	33	28
US dollar	36	36	US dollar	36	43
Sterling	13	17	Sterling	18	20
Other	8	11	Other	13	9

MARK TEN HOVE

GROUP GENERAL MANAGER
- INVESTMENTS



Our investment team delivered an outstanding result, well ahead of expectations given the continuing effect of global economic uncertainty on fixed interest, cash and equity markets. We decided that it was appropriate to maintain a cautious approach to our investment decisions and to continue the low risk strategy that has worked so well for us over many years.

In the early part of the year, we experienced falling equity markets and widening credit spreads, particularly for corporate paper in the financial sector. Our decision in the second quarter to substantially increase our investment in quality corporate paper with slightly longer duration was rewarded when the credit markets began to stabilise, resulting in higher gross yields on approximately one third of our fixed interest portfolios. However, with a large portion of our investment funds in US dollars and sterling, the lower yields, general lack of liquidity in markets, volatile credit spreads and the need for extreme care on credit necessarily limited our opportunity to enhance overall returns. Nevertheless, our gross yield on fixed interest and cash investments was a pleasing 3.9% compared with 5.1% in 2008, outperforming most of the key market benchmarks.

We also decided to take a cautious approach to equities, utilising derivatives throughout the year to protect the portfolios and the capital in our regulated entities against continuing market volatility. While we exceeded our budget for equity returns with a 9.6% gross yield, we underperformed against most equity market benchmarks.



IVECO Australian Motorcycle Grand Prix, Phillip Island.

It is pleasing to report that our cautious and low risk strategy for the Group's investment portfolio, held in 47 countries around the world, and our short duration strategy have ensured that we have not had a single case of permanent diminution in value of fixed interest investments since the global financial crisis commenced. We continue to monitor our portfolios on a daily basis and make adjustments that we consider necessary to ensure we minimise capital losses. Our short duration strategy protected us against capital losses on longer dated paper. As corporate credit spreads blew out to unprecedented highs, we significantly increased our exposure to high quality corporate debt and benefited from improved spreads during the second half of 2009.

Central bank cash rates were slashed aggressively during 2008 and 2009. For most of 2009 they were kept at unprecedented lows in the US (0.25%) and slashed further in the UK (from 1.5% to 0.5%) and Europe (from 2.0% to 1.0%). Australia was one of the very few countries that started raising cash rates in the second half of 2009. These low yields were largely offset by gains made on the tightening of credit spreads during the second half of 2009. This, together with the positive return on

MotoGP champion Casey Stoner won his third consecutive Australian Motorcycle Grand Prix in 2009. Although Casey Stoner takes the winner's podium, his success reflects the support of a high quality and well co-ordinated team. QBE Australia has been a key partner and sponsor of the Australian Motorcycle Grand Prix since 2007 and is established as one of Australia's leading and most trusted motorcycle insurers, insuring Australian motorcyclists for over 40 years.

It takes the same superb teamwork to manage the QBE Group's numerous investment portfolios in 47 countries around the world. It is an accolade to the QBE investments team to have been able to protect and grow Group assets and deliver an excellent investment return in one of the most volatile years in global financial history.

our equities, resulted in gross investment income increasing from \$766 million to \$1,097 million and the overall gross investment yield increasing from 2.9% to 4.1%. Gross investment income excludes foreign exchange gains and profit on the repurchase of discounted QBE debt securities. It includes net realised and unrealised gains on equities of \$97 million before tax compared with losses of \$554 million before income tax last year.

Net investment income which includes borrowing costs, investment expenses, foreign exchange gains and the profit on the repurchase of our debt securities increased from \$1,177 million to \$1,237 million. Foreign exchange gains were \$365 million before tax compared with \$409 million last year and the profit

on the repurchase of QBE debt securities was \$70 million before tax compared with \$303 million last year.

At 31 December 2009, our physical exposure to equities was 6% of total investments and cash. Our intention is to increase our exposure to equities to 10% of total investments and cash but only when we are satisfied that there is clear evidence that markets will improve.

Our cash and fixed interest portfolios continue to be invested in high quality securities with an average duration of 0.5 years at year end. We have no intention of changing our short-term duration strategy and our low risk approach given the current economic environment and the potential for interest rates to rise. We do not consider the environment to be conducive to maximising yield by taking unnecessary risk and exposing our shareholders and policyholders to possible capital losses.

The strengthening of the Australian dollar resulted in a 12% reduction in investments and cash from \$28.5 billion at 31 December 2008 to \$25.1 billion at 31 December 2009. The volatile Australian dollar means that it is extremely difficult to estimate the level of investments and cash by the end of 2010. Based on current exchange rates and expected cash flow from operations, the Group's total investments and cash is expected to be around \$28 billion by December 2010.

We continue to manage foreign exchange exposures at entity level by matching liabilities with assets of the same currency. Residual exposures are hedged using forward foreign exchange contracts. As mentioned at the last annual general meeting, currently we do not fully hedge overseas shareholders' funds back into Australian dollars due to the volatility that this creates on capital adequacy ratios and liquidity requirements given the extent of hedging now required. Approximately 75% of Group shareholders' funds are held in overseas countries to meet regulatory and rating agency requirements.

Interest rates currently remain at exceptionally low levels, particularly in the US and UK where we have a large percentage of our investments. The low interest rates and the significant reduction in credit spreads on quality paper, together with our relatively short duration portfolio, are expected to result in more modest gross yields. At this stage, we are targeting a gross investment yield of close to 3% for 2010.

We believe that interest rates will rise in the latter part of 2010 and that equity markets will stabilise.

The past two years have been extremely challenging for our investment team. Our task has not been made easy because of the need to maintain investments in all countries in which we operate to meet local regulatory solvency requirements and to match liabilities in those countries.

The QBE investment team should be proud of their performance over the past two years. In particular, I would like to take this opportunity to thank them for their hard work and discipline during the past year. Our investment portfolio is well positioned to benefit from rising interest rates and improved equity markets.

Mark ten Hove

Group general manager – Investments

TOTAL INVESTMENTS AND CASH

AS AT	31 DECEMBER 2009			31 DECEMBER 2008		
	POLICYHOLDERS' FUNDS \$M	SHAREHOLDERS' FUNDS \$M	TOTAL \$M	POLICYHOLDERS' FUNDS \$M	SHAREHOLDERS' FUNDS \$M	TOTAL \$M
Cash	1,147	454	1,601	1,959	777	2,736
Short-term money	8,274	3,274	11,548	12,092	4,793	16,885
Fixed interest securities and other	7,432	2,941	10,373	5,170	2,049	7,219
Equities	-	1,499	1,499	-	1,589	1,589
Investment properties	-	70	70	-	112	112
Total investments and cash	16,853	8,238	25,091	19,221	9,320	28,541

CASH AND FIXED INTEREST INVESTMENTS – SECURITY GRADING

AS AT	31 DECEMBER 2009		31 DECEMBER 2008	
	\$M	%	\$M	%
Moody's rating				
Aaa	7,277	31	6,087	23
Aa	12,854	55	19,019	71
A	2,652	11	1,320	5
<A	739	3	414	1
	23,522	100	26,840	100

CURRENT AAA CASH RATE – WEIGHTED AVERAGE YIELD

AS AT	31 DECEMBER 2009 %	31 DECEMBER 2008 %
Australian dollar	3.8	4.3
US dollar	0.3	0.3
Sterling	0.5	2.0
Other	1.1	2.3
Weighted average yield	1.6	1.9

INVESTMENT YIELDS COMPARISON

	AVERAGE AAA CASH YIELDS FOR YEAR %	ACTUAL GROSS YIELDS ACHIEVED ⁽¹⁾ %
Year end 2004	3.4	4.8
Year end 2005	4.2	5.2
Year end 2006	4.9	5.2
Year end 2007	5.4	6.3
Year end 2008	3.9	2.9
Year end 2009	1.5	4.1

(1) Includes yields on cash, fixed interest securities and equities.

Board of directors

Directors are selected to achieve a broad range of skills, experience and knowledge complementary to the Group's activities.



JOHN CLONEY AM

FANZIIF, FAIM, FAICD, AGE 69
CHAIRMAN

Mr Cloney joined QBE as managing director in 1981. He retired in January 1998, at which time he became a non-executive director. He was appointed deputy chairman in April 1998 and chairman in October 1998. He is the chairman of the chairman's and funding committees, and a member of the investment and remuneration committees. Mr Cloney is a director of Maple-Brown Abbott Limited. He is a trustee of the Sydney Cricket & Sports Ground Trust and a member of the RBS Group (Australia) Pty Limited advisory council.



LEN BLEASEL AM

FAIM, FAICD, AGE 67

Mr Bleasel was appointed an independent non-executive director of QBE in January 2001. He is chairman of the remuneration committee and a member of the audit committee. Mr Bleasel is the chairman of APA Group. He is also the chairman of the Zoological Parks Board of NSW and is a member of the RBS Group (Australia) Pty Limited advisory council.



DUNCAN BOYLE

BA, FCII, FAICD, AGE 58

Mr Boyle was appointed an independent non-executive director of QBE in September 2006. He is a member of the audit and remuneration committees. Mr Boyle is a director of Clayton Utz and Stockland Trust Group and has 37 years experience in the insurance industry in Australia, New Zealand and the UK.



ISABEL HUDSON

MA, FCII, AGE 50

Ms Hudson is based in the UK and was appointed an independent non-executive director of QBE in November 2005. She is a member of the audit and remuneration committees. Ms Hudson is chairman of the business development board of Scope, a UK charity, a director of Pearl Group and of the Pensions Regulator in the UK and a member of the Standard Life With Profits Committee. She has 29 years experience in the insurance industry in the UK and mainland Europe.



BELINDA HUTCHINSON AM

BEC, FCA, MAICD, AGE 56

Ms Hutchinson was appointed an independent non-executive director of QBE in September 1997. She is the chairman of the investment committee and a member of the audit, chairman's and funding committees. She is a director of St Vincent's Health Australia, a member of the Salvation Army Sydney and Territorial advisory board and a member of the external advisory panel of the Australian Securities & Investments Commission.



CHARLES IRBY

FCA (ENGLAND & WALES), AGE 64

Mr Irby is based in the UK and was appointed an independent non-executive director of QBE in June 2001. He is a member of the investment committee and the European operations' audit committee. He is a director of Great Portland Estates plc and North Atlantic Smaller Companies Investment Trust plc. Mr Irby is also a trustee and governor of King Edward VII's Hospital Sister Agnes.



IRENE LEE

BA, BARRISTER-AT-LAW, AGE 56

Ms Lee was appointed an independent non-executive director of QBE in May 2002. She is the chairman of the audit committee and a member of the funding and investment committees. Ms Lee is the non-executive chairman of Keybridge Capital Limited and is a director of Cathay Pacific Airways Limited, ING Bank (Australia) Limited and the Myer Family Company Pty Limited. She is a member of the Takeovers Panel, the advisory council of JP Morgan Australia and the executive council of the UTS Faculty of Business.



FRANK O'HALLORAN

FCA, AGE 63
CHIEF EXECUTIVE OFFICER

Mr O'Halloran was appointed chief executive officer in January 1998 and is a member of the chairman's, funding and investment committees. He joined QBE in 1976 as Group financial controller. He was appointed chief financial officer in 1982, joined the board as director of finance from 1987 to 1994 and continued on the board as director of operations from 1994 to 1997. He has had extensive experience in professional accountancy for 14 years and insurance management for 33 years.

Corporate governance statement

DUNCAN RAMSAY
GENERAL COUNSEL AND
COMPANY SECRETARY



This statement aims to disclose as clearly and objectively as possible QBE's corporate governance standards and practices so that they can be readily understood by our shareholders, policyholders and other stakeholders. QBE also continues to focus on other equally important issues such as the strength of its outstanding claims provision, the quality of its reinsurers and the depth of its culture of honesty, integrity and business acumen.

The statement incorporates the disclosures required by the revised recommendations of the ASX Corporate Governance Council ("ASX CGC") issued in August 2007.

BOARD OF DIRECTORS

Directors are selected to achieve a broad range of skills, experience and expertise complementary to the Group's activities. Details of individual directors are included on pages 42 and 43 and can also be found on the QBE website at www.qbe.com. The board currently comprises eight directors being the chairman, the chief executive officer and six independent non-executive directors using the "independence" definition of the ASX CGC. Applying this definition, the board has determined that a non-executive director's relationship with QBE as a professional adviser, consultant, supplier, customer or otherwise is not material unless amounts paid under that relationship exceed 1% of the Group's revenue or expenses.

The roles of chairman and chief executive officer are not exercised by the same individual.

The relationships identified by the ASX CGC as affecting a director's independent status no longer refer to the period for which a director has served on a board. Nevertheless, as a general guide, the board has agreed that a non-executive director's term should be approximately 10 years. The board considers that a mandatory limit on tenure would deprive the Group of valuable and relevant corporate experience in the complex world of international general insurance and reinsurance. Ms BJ Hutchinson AM has been a non-executive director since September 1997 and chairman of the investment committee since 2002. She was re-elected as a director at the 2009 AGM. QBE's other directors believe that Ms Hutchinson AM continues to exercise independent judgment and, through her QBE experience, makes an important contribution.

The chairman has over 50 years involvement in the insurance industry, including 17 years as chief executive officer of QBE until he retired in January 1998. He became chairman in October 1998. The chairman's former executive capacity with QBE has been fully disclosed to shareholders, who re-elected him as a director by an overwhelming majority at the 2009 AGM. QBE's other directors consider that the chairman exercises independent judgment. The chairman is not an "independent" director as recommended by the ASX CGC because there was less than a three year period between him acting as chief executive officer and being appointed chairman. The board believes it is in shareholders' and policyholders' interests to retain his wealth of experience and has resolved that he should continue in that role. The board also believes that the chairman's experience gained from directorships in other businesses provides an advantage to QBE.

The chairman oversees the performance of the board, its committees and each director. The board review procedure involves an annual assessment of the entire board and each director, comprising a combination of written questions and answers together with an interview with each director. The chairman reports the overall result to the board and it is discussed by all directors. This review procedure is a precursor to other directors determining whether to support, via the notice of meeting, a non-executive director for re-election at an AGM. The last board review was completed in accordance with the process above in December 2009 ahead of nominating Mr LF Bleasel AM and Mr DM Boyle for re-election at the 2010 AGM. The committee review procedure comprises the relevant committee considering a memorandum from the Group chairman generally dealing with its performance and contribution to QBE. The audit, investment and remuneration committees as the main committees of the board each conducted such a review in accordance with the process above during 2009 and concluded that each committee was operating soundly and meeting the terms of its charter.

QBE's constitution provides that no director, except the chief executive officer, shall hold office for a continuous period in excess of three years or past the third AGM following a director's appointment, whichever is the longer, without submission for re-election at the next AGM. Under QBE's constitution, there is no maximum fixed term or retirement age for non-executive directors.

Directors advise the board on an ongoing basis of any interest they have that they believe could conflict with QBE's interests. If a potential conflict does arise, either the director concerned may choose not to, or the board may decide that he or she should not, receive documents or take part in board discussions whilst the matter is being considered.

Corporate governance statement

Under QBE's constitution, management of the Group is vested in the board. In accordance with its board charter, the board:

- oversees corporate governance;
- selects and supervises the chief executive officer;
- provides direction to management;
- approves the strategies and major policies of the Group;
- monitors the achievement of strategies and policies;
- monitors performance against plan;
- considers regulatory compliance; and
- reviews human resources (including succession planning), information technology and other resources.

The board ensures it has the information it requires to be effective including, where necessary, independent professional advice. A non-executive director may seek such advice at the company's cost with the consent of the chairman. All directors would receive a copy of such advice. Non-executive directors may attend relevant external training courses at QBE's cost with the consent of the chairman.

Strategic issues and management's detailed budgets and three year business plans are reviewed at least annually by the board. The board receives updated forecasts during the year. Visits by non-executive directors to the Group's offices in key locations are encouraged. To help the board to maintain its understanding of the business and to effectively assess management, directors have regular presentations by the divisional chief executive officers and other senior managers of the various divisions on topics including budgets, three year business plans and operating performance. They have contact with senior employees at numerous times and in various forums during the year. The board meets regularly in Australia and, due to QBE's substantial overseas operations, in the UK and the US each year, usually for a total of five days. Meetings are held in other overseas offices as and when the board considers it appropriate. Each meeting normally considers reports from the chief executive officer and chief financial officer together with other relevant reports. The board regularly meets in the absence of management. The chairman and chief executive officer in particular, and board members in general, have substantial contact outside board and committee meetings.

COMMITTEES

The board is supported by several committees which meet regularly to consider the audit and risk management processes, investments, remuneration and other matters. The main committees of the board are the audit committee, the investment committee and the remuneration committee. These committees operate under a written charter approved by the board. Any non-executive director may attend a committee meeting. The committees have direct and unlimited access to QBE's senior managers during their meetings and may consult external advisers when necessary at QBE's cost, including requiring their attendance at committee meetings. Committee membership is reviewed regularly.

In addition, the board has established a chairman's committee comprising the chairman, Ms BJ Hutchinson AM and the chief executive officer, and a funding committee comprising the chairman, Ms BJ Hutchinson AM, Ms IYL Lee and the chief executive officer. These committees meet as required, including to deal with matters referred by the board from time to time.

The board regularly discusses its composition and is involved in the selection of new members. All directors are members of the nomination committee. This means the board is able to draw upon the views of all directors at one time to ensure the most appropriate candidates are chosen to enhance QBE's culture and strategy. External consultants may be engaged where necessary to search for prospective board members. The board has adopted non-executive director nomination guidelines. As a relatively small board of eight directors (including the chief executive officer), the directors believe that this is an efficient mechanism for dealing with this matter.

Details of directors' attendance at board and committee meetings are outlined in the table of meeting attendance set out in the directors' report on page 54. A report on each committee's last meeting is provided to the next board meeting. The company secretary acts as secretary to all committees.

Audit committee

The membership of the audit committee may only comprise non-executive directors. The audit committee normally meets four times a year. The chairman must be a non-executive director who is not the chairman of the board. The current members are Ms IYL Lee (chairman), Mr LF Bleasel AM, Mr DM Boyle, Ms IF Hudson and Ms BJ Hutchinson AM.

The role of the audit committee is to oversee the integrity of QBE's financial reporting process. This includes review of:

- the quality of financial reporting to the Australian Securities and Investments Commission ("ASIC"), ASX and shareholders;
- the consolidated entity's accounting policies, practices and disclosures; and
- the scope and outcome of external and internal audits.

The audit committee's responsibilities include the financial statements (including items such as the outstanding claims provision, reinsurance recoveries and income tax), risk management, internal controls, compliance other than regulatory compliance and significant changes in accounting policies.

The chairman of the board and other non-executive directors normally attend audit committee meetings which consider the 30 June and 31 December financial reports. Meetings of the audit committee usually include, by invitation, the chief executive officer, the chief financial officer, the chief operating officer, the chief actuarial officer, the chief risk officer, the Group internal audit manager and the external auditor. As appropriate, other relevant senior managers also attend.

The audit committee has direct and unlimited access to the external auditor. The external auditor, the Group internal audit manager, the chief risk officer and the chief actuarial officer have direct and unlimited access to the audit committee.

The chief executive officer and chief financial officer provide the board with certificates in relation to risk management and internal control as recommended by the ASX CGC and on the financial reports as required by the *Corporations Act 2001*.

Corporate governance statement

External auditor independence

QBE firmly believes that the external auditor must be, and must be seen to be, independent. The external auditor confirms its independence in relation to the 30 June and 31 December financial reports and the audit committee confirms this by separate enquiry. The audit committee has contact with the external auditor in the absence of management in relation to the 30 June and 31 December financial reports and otherwise as required. The external auditor normally confers with the audit committee in the absence of management as part of each meeting.

QBE has issued an internal guideline on external auditor independence. Under this guideline, the external auditor is not allowed to provide the excluded services of preparing accounting records, financial reports or asset or liability valuations. Furthermore, it cannot act in a management capacity, as a custodian of assets or as share registrar.

The board believes some non-audit services are appropriate given the external auditor's knowledge of the Group. QBE may engage the external auditor for non-audit services other than excluded services subject to the general principle that fees for non-audit services should not exceed 30% of all fees paid to the external auditor in any one financial year. External tax services are generally provided by an accounting firm other than the external auditor.

The external auditor has been QBE's auditor for many years. As a diverse international group, QBE requires the services of one of a limited number of international accounting firms to act as auditor. It is the practice of QBE to review from time to time the role of the external auditor. The *Corporations Act 2001*, Australian professional auditing standards and the external auditor's own policy deal with rotation and require rotation of the lead engagement partner after five years. In accordance with such policy, the lead engagement partner of the external auditor rotated in 2009.

Investment committee

The membership of the investment committee comprises four non-executive directors and one executive director. The investment committee normally meets six times a year. The chairman must be a non-executive director who is not the chairman of the board. The current members are Ms BJ Hutchinson AM (chairman), Mr EJ Cloney AM, Mr CLA Irby, Ms IYL Lee and Mr FM O'Halloran. Meetings of the investment committee usually include, by invitation, the Group general manager – investments, the chief financial officer and the chief operating officer. As appropriate, other relevant senior managers also attend.

The role of the investment committee is to oversee QBE's investment activities. This includes review of:

- investment objectives and strategy;
- investment risk management;
- currency, equity and fixed interest exposure limits;
- credit exposure limits with financial counterparties; and
- Group treasury.

The investment committee's responsibilities include review of economic and investment conditions as they relate to QBE and review of investment performance, including the performance of QBE's defined benefit superannuation funds.

Remuneration committee

The membership of the remuneration committee may only comprise non-executive directors. The remuneration committee normally meets four times a year. The chairman must be a non-executive director who is not the chairman of the board. The current members are Mr LF Bleasel AM (chairman), Mr DM Boyle, Mr EJ Cloney AM and Ms IF Hudson. Meetings of the remuneration committee usually include, by invitation, the chief executive officer, the chief operating officer and the Group general manager, human resources.

QBE's governance of remuneration focuses on ensuring that the remuneration and reward strategy and frameworks are aligned with robust risk management practices and strong governance principles and that shareholders receive value for remuneration expenditure.

The role of the remuneration committee is to oversee QBE's general remuneration practices. The remuneration committee is responsible for reviewing and making recommendations to the board on QBE's remuneration policy and practices. The remuneration committee, in particular, assesses the appropriateness of remuneration frameworks and practices in order to fairly and responsibly reward the Group chief executive officer, the Group operations executive and the Group head office management. The remuneration committee ensures rewards are commensurate with performance and that remuneration levels are competitive in the various markets in which QBE operates. The remuneration committee has access to detailed external research from independent consultants.

The remuneration committee's responsibilities include:

- recommendation of the fixed remuneration of the chief executive officer to the board and approval of the fixed remuneration of the Group operations executive and Group head office management ("Group executive");
- review and approval of short-term and deferred incentives such as equity based plans;
- review of superannuation;
- review of performance measurement criteria, succession plans and other major human resource practices;
- monitoring of personal development plans ("PDP") for the Group executive and other senior positions; and
- recommendations on non-executive director remuneration to the board.

The remuneration committee recognises that the key to achieving sustained performance is to motivate and retain quality employees and align executive reward with increasing shareholder wealth. The remuneration committee has the discretion to reduce deferred equity awards to the Group executive where financial results subsequently deteriorate.

The remuneration committee receives information on the performance of the Group executive, being the senior executives as defined by the ASX CGC (namely those employees who have the opportunity to materially influence the integrity, strategy, operation and financial performance of the QBE Group).

Corporate governance statement

A PDP involves a meeting between the relevant member of the Group executive, the chief executive officer and the Group general manager, human resources to:

- review past performance;
- discuss career opportunities; and
- consider areas of further development.

PDPs occur periodically in accordance with the process above, and several took place in 2009. In addition, the board continually monitors the performance of the Group executive through regular contact and reporting.

QBE has operations and staff in 47 countries with differing laws and customs. QBE's remuneration policy therefore reflects the fact that QBE is a global organisation, whilst also taking into account local remuneration levels and practices.

Details of remuneration

Details of remuneration of employees and non-executive directors, such as employee entitlements under the Employee Share and Option Plan and the Deferred Compensation Plan together with superannuation for non-executive directors, are included in the remuneration report on pages 56 to 76 and in notes 27 and 28 to the financial statements.

RISK MANAGEMENT

QBE's core business is the underwriting of risk. The Group's successful performance over many years clearly establishes its substantial risk management credentials.

It is QBE's policy to adopt a rigorous approach to managing risk throughout the Group. Risk management is a continuous process and an integral part of quality business management. QBE's approach is to integrate risk management into the broader management processes of the organisation. It is QBE's philosophy to ensure that risk management remains embedded in the business and that the risk makers or risk takers are themselves the risk managers.

Diversification is used as a tool to reduce the Group's overall insurance risk profile by spreading exposures, thereby reducing the volatility of results. QBE's approach is to diversify insurance risk, both by product and geographically. Product diversification is achieved through a strategy of developing strong underwriting skills in a wide variety of classes of business. A combination of core and speciality products under the control of proven employees skilled in such products allows QBE to lead underwrite in many of the markets in which we operate. Geographic diversification is achieved by operating in 47 countries.

QBE has a global risk management framework that defines the risks that QBE is in business to accept and those that we are not, together with the material business risks that QBE needs to manage and the framework and standards of control that are needed to manage those risks.

The foundation of our risk management is the obligation and desire to manage our future and create wealth for our shareholders by maximising profitable opportunities through:

- avoiding unwelcome surprises by reducing uncertainty and volatility, such as by controlling aggregate exposures and maintaining sound reinsurance arrangements;
- achieving competitive advantage through better understanding of the risk environment in which we operate;
- optimising risk and more effectively allocating capital and resources by assessing the balance of risk and reward;
- adequate pricing of risk;
- complying with laws and internal procedures; and
- improving resilience to external events.

The Group has established internal controls to manage material business risks in the key areas of exposure relevant to QBE. The broad risk categories are insurance risk, acquisition risk, operational risk and funds management and treasury risk. Internal controls and systems are designed to provide reasonable assurance that the assets of the Group are safeguarded, insurance and investment exposures are within desired limits, reinsurance protections are adequate, counterparties are subject to security assessment and foreign exchange exposures are within predetermined guidelines. The board approves a comprehensive risk management strategy ("RMS") and reinsurance management strategy ("REMS") annually, both of which are lodged with APRA. The RMS outlines the principles, framework and approach to risk management adopted by the Group, deals with all areas of significant business risk to the Group and outlines the Group's risk tolerances. The REMS covers topics such as the Group's risk tolerance and the Group's strategy in respect of the selection, approval and monitoring of all reinsurance arrangements. The Group security committee assesses reinsurer counterparty security. This management committee normally meets four times a year and holds special meetings as required.

While the RMS and REMS are approved by the board, QBE believes that managing risk is the day to day responsibility of the Group head office and the business units, and that all staff need to understand and actively manage risk. The business units are supported by risk management teams, compliance teams, the Group risk and compliance manager and by senior management. Further information on risk management is provided on pages 16 to 18 of the annual report and in notes 4 and 5 to the financial statements.

Management has reported to either the audit committee or the board on the effectiveness of QBE's management of its material business risks.

Internal audit

A global internal audit function is critical to the risk management process. QBE's internal audit function reports to senior management and the audit committee on the monitoring of the Group's worldwide operations. Internal audit provides independent assurance that the design and operation of the controls across the Group are effective. The internal audit function operates under a written charter from the audit committee. Other governance documents include a reporting protocol, internal audit manual, internal audit issue rating system, internal audit opinion levels and internal audit timetables. A risk-based internal audit approach is used so that higher risk activities are reviewed more frequently. The Group's internal audit teams work together with the external auditor to provide a wide audit scope.

Corporate governance statement

Delegated authorities

QBE has operated under an extensive written system of delegated authorities for many years. In particular, a written delegated authority with specified limits is approved by the board each year to enable the chief executive officer to conduct the Group's business in accordance with detailed budgets and business plans. This authority deals with topics such as underwriting, reinsurance protection, claims, investments, acquisitions and expenses. The chief executive officer delegates his authority to management throughout the Group on a selective basis taking into account expertise and past performance. Compliance with delegated authorities is closely monitored by management and adjusted as required for actual performance, market conditions and other factors. Management and the Group's internal audit teams review compliance with delegated authorities and any breach can lead to disciplinary procedures, including dismissal in serious cases.

Actuarial review

It is a longstanding practice of the directors to ensure that the Group's insurance liabilities are assessed by actuaries. The Group's outstanding claims provision is reviewed by experienced internal actuarial staff. The chief actuarial officer is based in head office and there are over 180 actuarial staff. Actuarial staff are involved in forming an independent view, separate from management, of the central estimate and the probability of adequacy of the outstanding claims provision and premium liabilities, premium rates and related matters. Approximately 90% of QBE's outstanding claims provision is also reviewed by external actuaries annually. External actuaries are generally from organisations which are not associated with the external auditor.

Insurance and other regulation

General insurance and, to a lesser extent, reinsurance are heavily regulated industries. In addition to the Group's accounting, legal, tax and other professional teams, each division has compliance personnel and there is a Group regulatory manager based in Australia. Regulators in Australia include ASIC, the Australian Competition and Consumer Commission, APRA, the Australian Privacy Commissioner and relevant state authorities for compulsory third party motor insurance and workers' compensation insurance. These regulatory bodies enforce laws which deal with a range of issues, including capital requirements and consumer protection. Similar local laws and regulations apply to the Group's operations outside Australia.

COMMUNICATION AND GUIDELINES

Continuous disclosure

ASX Listing Rule 3.1 requires QBE to inform the ASX immediately once QBE is or becomes aware of any information concerning it that a reasonable person would expect to have a material effect on the price or value of QBE's shares. Procedures are in place to ensure that items which potentially require announcement to the ASX are promptly notified to Group head office for assessment and released as required. The chief executive officer is responsible for authorising the release of market announcements. All market announcements are posted promptly to the Group's website.

QBE takes the spirit of its continuous disclosure obligations very seriously and issues frequent market announcements during the year to satisfy those obligations. A list of the material announcements made since 1 January 2009 is included on page 171.

Communication with shareholders

The *Corporations Act 2001* no longer requires QBE to distribute an annual report to all shareholders except to those who elect to receive it. QBE also produces a half year report which is sent to all shareholders who elect to receive it. Both reports are available on the QBE website. The website also contains historical and other details on the Group. Shareholders can discuss their shareholding with either the shareholder services department or the share registrar, both located in Sydney.

The AGM is held in Sydney each year, usually in April (although in 2010 it will be held on 31 March). Shareholders are encouraged to attend the AGM in person or by proxy. Most resolutions in the notice of meeting have explanatory notes. During the AGM, shareholders may ask questions of either the chairman or the external auditor.

Communications with analysts, investors, media, rating agencies and others

The chief executive officer, chief financial officer, chief operating officer, chief actuarial officer, chief risk officer, general counsel and company secretary, investor relations manager, divisional chief executives and divisional finance officers generally deal with analysts, investors, media, rating agencies and others, taking account of regulatory guidelines including those issued by the ASX on continuous disclosure. The presentations on the 30 June and 31 December results and other major presentations are sent to the ASX before the presentations commence and are available promptly on the Group's website. The 30 June and 31 December presentations are also generally webcast.

Corporate governance statement

Share trading guidelines

QBE has guidelines for directors and senior Group executives relating to the purchase and sale of securities of QBE. These are in addition to the insider trading provisions of the *Corporations Act 2001*. In particular, the guidelines state that directors and senior Group executives should:

- never actively trade the company's securities;
- not hedge unvested entitlements; and
- notify any intended transaction to nominated people within the Group, including notification of any hedging of vested entitlements.

The guidelines identify set periods during which directors or senior Group executives may buy or sell QBE's securities, being three to 30 days after each of the release of QBE's half year results, the release of QBE's annual report and the date of the AGM, and also three days after the issue of any prospectus until the closing date. Any QBE share dealings by directors are promptly notified to the ASX.

Other Group guidelines

The Group has adopted a code of conduct for Australian operations, Group head office and Group investment division which forms the basis for the manner in which these employees perform their work involving both legal obligations and the reasonable expectation of stakeholders. The code of conduct requires that business be carried out in an open and honest manner with our customers, shareholders, employees, regulatory bodies, outside suppliers, intermediaries and the community at large. The code also deals with confidentiality, conflicts of interest and related matters. The non-executive directors have adopted a code of conduct for themselves which is substantially the same as the code above.

Other divisions have developed codes of conduct based on the Group code above, with some differences to allow for the requirements of the particular countries in which the division operates.

There are other Group policies covering anti-discrimination, employment, harassment, QBE essential behaviours, health and safety, privacy, whistle-blowing and many other business practices. These policies, like the code of conduct, are underpinned by the Group's vision and values statements. The vision and values statements form part of the induction information given to new employees. One of the core values of the Group is integrity.

QBE in Australia follows the general insurance code of practice, a self-regulated code developed by the Insurance Council of Australia relating to the provision of products and services to customers of the general insurance industry of Australia. A revised code of practice commenced in July 2006.

QBE in Australia is a member of the Financial Ombudsman Service, an ASIC approved external dispute resolution body which deals with general insurance disputes between consumers and insurers.

Similar insurance practice rules apply to the Group in certain other countries outside Australia.

Details of indemnification and insurance arrangements are included in the directors' report on page 53.

The following documents are available either in the corporate governance area of QBE's website or on request from the company secretary:

- board charter;
- audit, investment and remuneration committee charters;
- non-executive director nomination guidelines;
- code of conduct for non-executive directors;
- code of conduct for Australian operations, Group head office and Group investment division;
- guidelines for dealing in securities of QBE Insurance Group Limited or other companies by directors and senior Group executives;
- continuous disclosure guidelines; and
- shareholder communication guidelines.

Environmental issues

QBE is a corporation involved in an industry that seeks to play a role, in conjunction with governments, individuals and organisations, in managing and reducing environmental risk. In an initiative to collaborate with the United Nations Environment Programme, QBE, together with a number of other major international insurers, is a signatory to a statement of environmental commitment by the insurance industry. QBE is also a signatory to the Carbon Disclosure Project ("CDP"). The CDP is an independent, not-for-profit organisation which acts as an intermediary between shareholders and corporations on all climate change related issues, providing climate change data from the world's largest corporations to the global market place.

QBE's response to the latest CDP questionnaire, CDP2009, was published in October 2009 and is available on our website in the investor information section.

Directors' report

FOR THE YEAR ENDED 31 DECEMBER 2009

Your directors present their report on the consolidated entity consisting of QBE Insurance Group and the entities it controlled at the end of or during the year ended 31 December 2009.

DIRECTORS

The following directors held office during the whole of the financial year and up to the date of this report:

EJ Cloney AM (chairman)
LF Bleasel AM
DM Boyle
IF Hudson
BJ Hutchinson AM
CLA Irby
IYL Lee
FM O'Halloran

At the 2010 annual general meeting ("AGM"), Mr Bleasel and Mr Boyle will retire by rotation and offer themselves for re-election. Mr John Green who will be appointed to the board as a director effective from 1 March 2010 will offer himself for election at the AGM.

Details of the directors and their qualifications are provided on pages 42 and 43.

CONSOLIDATED RESULTS

	2009 \$M	2008 \$M
Revenue		
Premium revenue	14,074	12,853
Other revenue	1,943	2,866
Net fair value gains on financial assets	460	–
Realised gains on sale of controlled entities	8	–
Investment income – ABC financial assets pledged for funds at Lloyd's	130	222
	16,615	15,941
Expenses		
Outward reinsurance premium expense	1,925	1,766
Gross claims incurred	8,157	7,743
Other expenses	3,695	3,494
Net fair value losses on financial assets	–	33
Net fair value losses on investment properties	21	–
Net fair value losses on owner occupied properties	29	–
Expenses – ABC securities for funds at Lloyd's	137	245
Finance costs	219	240
Profit before income tax	2,432	2,420
Income tax expense	448	554
Profit after income tax	1,984	1,866
Net profit attributable to minority interests	14	7
Net profit after income tax attributable to ordinary equity holders of the company	1,970	1,859

PROFIT

2009 has been another volatile year for the insurance industry as a result of the global financial crisis. In these circumstances, the directors are pleased to report a 6% increase in net profit after income tax for the year ended 31 December 2009 to \$1,970 million. This compares with \$1,859 million last year. The result benefited from our strong focus on risk management and our conservative investment strategy. The result includes a number of significant items including substantial foreign exchange gains and a continued frequency of claims from the economic downturn.

Directors' report

FOR THE YEAR ENDED 31 DECEMBER 2009

DIVIDENDS

The directors are pleased to announce a final dividend of 66.0 cents per share for the year ended 31 December 2009, up from 65.0 cents last year. The substantial growth in our overseas profits has meant that the franking of the final dividend will remain at 20%. The total dividend for 2009 is 128.0 cents, up two cents compared with 126.0 cents for the year ended 31 December 2008. The total dividend payout is \$1,306 million or 66% of net profit after tax, up from \$1,187 million last year. The bonus share plan and the dividend reinvestment plan will continue.

ACTIVITIES

The principal activities of the company and its controlled entities during the year were underwriting general insurance and reinsurance risks, management of Lloyd's syndicates and investment management.

SHAREHOLDERS' FUNDS

Shareholders' funds were \$10,222 million compared with \$11,159 million at 31 December 2008. The movement mainly reflects the adverse effect of the appreciation of the Australian dollar against the US dollar causing a reduction in the value of our overseas shareholders' funds when translated to Australian dollars, offset by the profit for the year net of the payment of the final 2008 dividend in March 2009 and the interim 2009 dividend in September 2009. Our policy of not hedging our investment in overseas shareholders' funds means that shareholders' funds now move in line with the changes in assets and liabilities in other currencies which provides greater stability in capital adequacy levels for the consolidated entity.

The number of shares advised to the Australian Securities Exchange increased from 987 million at 31 December 2008 to 1,025 million.

REVIEW OF OPERATIONS

Gross earned premium was \$14,074 million, up 9% from last year. Premium growth was mainly due to the impact of the 2008 acquisitions and new distribution channels. The average Australian dollar strengthened against sterling but weakened against the US dollar and the euro. Overall average premium rate increases of 4% were ahead of target with rate increases achieved in all divisions, albeit small increases in the US and Asia Pacific operations. Net earned premium increased 10% to \$12,149 million.

The ratio of claims, commissions and expenses to net earned premium (combined operating ratio) was 89.6% compared with 88.5% last year. The net claims ratio was 60.3% compared with 57.6% last year. As expected, savings from prior year central estimates were down to 0.7% of net earned premium compared with 3.3% last year. An increase in the frequency of large individual risk and global financial crisis claims was largely offset by a reduction in catastrophe claims. Further provisions for old latency claims were raised in addition to our already prudent provision to cover higher superimposed inflation. The strength of our provision for outstanding claims has increased slightly with the probability of adequacy at 88.1% compared with 86.1% at 31 December 2008. The combined commission and expense ratio reduced from 30.9% to 29.3% benefiting mainly from the contributions of our agency operations acquired in 2008, in particular ZC Sterling in the US.

Australian operations

Australian operations' combined operating ratio was 89.0% compared with 90.6% last year. The improvement was despite the Victorian bushfires and an increased frequency of attritional and large trade credit and surety claims from the global financial crisis. These were largely offset by an excellent underwriting profit from QBE Lenders' Mortgage Insurance ("QBE LMI"). Gross earned premium of \$3,328 million was up 19% from last year. Growth was due to the acquisitions of QBE LMI in October 2008 and Elders Insurance in September 2009, and from new distribution channels including acquired agencies. The claims ratio reduced from 62.8% to 60.7%. Whilst we experienced a slightly higher level of attritional claims, an increased frequency of trade credit claims and the effect of the Victorian bushfires and various storms, the majority of our Australian portfolios performed ahead of expectation. The combined commission and expense ratio increased from 27.8% to 28.3%. The increase was entirely due to the cost of strategic initiatives, in particular new technology to further automate the interface with financial institutions and other intermediaries and to improve bodily injury claims management.

Asia Pacific operations

Asia Pacific operations' combined operating ratio was 88.1%, up from 82.9% last year. Gross earned premium was up 8% to \$674 million. This growth was due to continued high customer retention and solid organic growth from major intermediaries, partly offset by a stronger Australian dollar. The claims ratio was up from 41.2% to 46.5% with the increase largely due to a greater frequency of catastrophe claims. The combined commission and expense ratio reduced slightly from 41.7% to 41.6%. The expense ratio again improved following the efficiencies generated from new systems implemented in 2007 and 2008.

European operations

European operations' combined operating ratio was 91.3% compared with 85.6% last year, reflecting an increase in attritional claims and substantially lower savings on prior year central estimate provisions. Gross earned premium grew due to overall premium rate increases of 4.5% on renewed business, the depreciation of sterling against the US dollar, the initiatives to build our regional UK and mainland European businesses and the impact of the Burnett and Endurance acquisitions. Net earned premium was stable at \$3,259 million. The claims ratio increased from 54.2% to 61.6% for the reasons explained above. The combined commission and expense ratio decreased from 31.4% to 29.7%. The reduction partly reflects the profit commission received from external names on syndicate 386 and from Equator Re.

Directors' report

FOR THE YEAR ENDED 31 DECEMBER 2009

the Americas

The Americas division reported gross earned premium growth of 10% to \$5,066 million. Growth was mainly due to the weaker average Australian dollar and the effect of the 2008 acquisitions. The combined operating ratio was 89.7% compared with 93.6% last year with the improved result mainly due to profits from acquired underwriting agencies. The agencies contributed net underwriting profits of \$267 million compared with profits of \$42 million last year. The net claims ratio increased from 60.2% to 61.3% due to the reduced benefit from savings on prior accident year claims provisions partly offset by the reduced frequency of attritional and catastrophe claims. The combined commission and expense ratio decreased from 33.4% last year to 28.4% primarily due to the increased contribution from acquired agencies where the commission margin paid to those agents is eliminated on consolidation.

Equator Re

Equator Re is QBE's wholly-owned captive reinsurer based in Bermuda. The division reported gross earned premium growth of 25% to \$2,467 million due to additional proportional reinsurance business, in particular from our European operations and the acquisitions made in the US. As the premium income is derived from other Group companies, it is eliminated on consolidation. The combined operating ratio was 88.2% compared with 83.8% last year. The net claims ratio was up from 56.6% to 59.4% largely due to the additional proportional business written, the increase in trade credit and property claims from the global financial crisis and Equator Re's share of the Victorian bushfires. The combined commission and expense ratio was 28.8% compared with 27.2% last year due to the increased proportional business written and profit commissions paid to Group companies.

Investment income

Net investment income was \$1,237 million compared with \$1,177 million last year. The result includes net fair value gains on equities of \$97 million compared with losses of \$554 million last year, further gains of \$70 million on the repurchase of QBE debt securities compared with \$303 million last year and foreign exchange gains of \$365 million compared with gains of \$409 million last year. The gross investment yield before borrowing costs, foreign exchange gains, gains on the repurchase of QBE debt securities and investment expenses was 4.1% compared with 2.9% last year.

Income tax

Income tax expense reduced from 23% of profit before tax last year to 18% due to increased profits earned in lower tax countries and lower tax payable on the foreign exchange and debt repurchase gains.

Outstanding claims provision

The provision for outstanding claims for the majority of Group entities is determined after consultation with internal and external actuaries. The outstanding claims assessment takes into account the statistical analysis of past claims, allowance for claims incurred but not reported, recoveries and future interest and inflation factors. As in previous years, the directors consider that substantial risk margins are required in addition to actuarial central estimates to cover uncertainties such as latency claims, changes in interest rates and superimposed inflation. The APRA prudential standards provide a capital credit for outstanding claims in excess of a probability of adequacy of 75%. The directors and management have set an internal target range of 85% to 94% using risk-free discount rates. The directors have satisfied themselves that the Group's outstanding claims provision is within the internal target range.

Directors' report

FOR THE YEAR ENDED 31 DECEMBER 2009

GROUP INDEMNITIES

Article 115 of the company's constitution provides that the company indemnifies past and present directors, secretaries or other officers against any liability incurred by that person as a director, secretary or other officer of the company or its controlled entities. The indemnity does not apply to any liability (excluding legal costs):

- owed to the company or its controlled entities (e.g. breach of directors' duties);
- for a pecuniary penalty or compensation order under the *Corporations Act 2001*; or
- which did not arise out of conduct in good faith.

The indemnity extends to legal costs other than where:

- in civil proceedings, an exclusion above applies;
- in criminal proceedings, the person is found guilty;
- the person is liable for civil remedies in proceedings brought by the Australian Securities and Investments Commission ("ASIC"), a corresponding regulator in another jurisdiction or a liquidator (unless as part of the investigation before proceedings are commenced); or
- the court does not grant relief after an application under the *Corporations Act 2001* or corresponding legislation in another jurisdiction that the person acted honestly and having regard to all the circumstances ought fairly to be excused for negligence, default, breach of trust or breach of duty in civil proceedings.

DIRECTORS' AND OFFICERS' INSURANCE

The consolidated entity pays a premium each year in respect of a contract insuring directors, secretaries, senior managers and employees of the consolidated entity together with any natural person who is either a trustee or a member of a policy committee for a superannuation plan established for the benefit of the consolidated entity's employees against liabilities past, present or future. The officers of the consolidated entity covered by the insurance contract include the directors listed on page 50, the secretary, DA Ramsay, and deputy secretary, P Smiles.

In accordance with normal commercial practice, disclosure of the total amount of premium payable under, and the nature of liabilities covered by, the insurance contract is prohibited by a confidentiality clause in the contract.

No such insurance cover has been provided for the benefit of any external auditor of the consolidated entity.

SIGNIFICANT CHANGES

There were no significant changes in the state of affairs of the consolidated entity during the financial year.

EVENTS SUBSEQUENT TO THE BALANCE DATE

No matter or circumstance has arisen since 31 December 2009 that has significantly affected, or may significantly affect:

- the consolidated entity's operations in future financial years;
- the results of those operations in future financial years; or
- the consolidated entity's state of affairs in future financial years.

LIKELY DEVELOPMENTS

Information on likely developments in the consolidated entity's operations in future financial years and the expected results of those operations has not been included in this report because disclosure of the information would be likely to result in unreasonable prejudice to the consolidated entity.

ENVIRONMENTAL REGULATION

The consolidated entity's operations are not subject to any significant environmental regulations under either Commonwealth or State legislation.

Directors' report

FOR THE YEAR ENDED 31 DECEMBER 2009

MEETINGS OF DIRECTORS

	FULL MEETINGS OF DIRECTORS ⁽¹⁾	MEETINGS OF COMMITTEES				
		AUDIT	CHAIRMAN'S	FUNDING	INVESTMENT	REMUNERATION
Number of meetings held	12	4	1	–	6	5
Number attended						
LF Bleasel AM	12	4	–	–	–	5
DM Boyle	12	4	–	–	–	5
EJ Cloney AM	12	–	1	–	6	5
IF Hudson	12	4	–	–	–	5
BJ Hutchinson AM	12	4	1	–	6	–
CLA Irby	11	–	–	–	6	–
IYL Lee	12	4	–	–	6	–
FM O'Halloran ⁽²⁾	12	–	1	–	6	–

(1) Included a five day review meeting in London and New York and a two day review meeting in Brisbane. In addition, directors attended meetings for each of the Australian regulated insurance companies.

(2) Mr O'Halloran attends audit and remuneration committee meetings by invitation, not being a member of these committees.

During the February and November 2009 board meetings, the board also met as the nomination committee. Further meetings occurred during the year, including meetings of the chairman and chief executive officer, meetings of the directors with management and meetings of non-executive directors. From time to time, directors attend meetings of committees of which they are not currently members.

DIRECTORSHIPS OF LISTED COMPANIES HELD BY THE MEMBERS OF THE BOARD

From 1 January 2007 to 26 February 2010, the directors also served as directors of the following listed companies:

	POSITION	DATE APPOINTED	DATE CEASED
LF Bleasel AM			
APA Group	Chairman	30 October 2007	–
DM Boyle			
Stockland Trust Group	Director	7 August 2007	–
EJ Cloney AM			
Boral Limited	Director	3 March 1998	28 October 2009
IF Hudson			
Pearl Group	Director	18 February 2010	–
BJ Hutchinson AM			
Coles Group Ltd	Director	23 September 2005	23 November 2007
Telstra Corporation Limited	Director	16 November 2001	7 November 2007
CLA Irby			
Aberdeen Asset Management plc	Chairman	1 August 1999	22 January 2009
Great Portland Estates plc	Director	1 April 2004	–
North Atlantic Smaller Companies Investment Trust plc	Director	10 December 2002	–
IYL Lee			
Cathay Pacific Airways Limited	Director	13 January 2010	–
Keybridge Capital Limited	Chairman ⁽¹⁾	26 October 2006	–
Ten Network Holdings Limited	Director	13 October 2000	25 October 2007

(1) Ms Lee stepped down from her position as executive chairman on 9 October 2009 and now has the role of non-executive chairman.

Directors' report

FOR THE YEAR ENDED 31 DECEMBER 2009

QUALIFICATIONS AND EXPERIENCE OF COMPANY SECRETARIES

DA Ramsay B Comm, LLB, LLM, FANZIIF, FCIS

Mr Ramsay is general counsel and company secretary of QBE Insurance Group Limited. His legal career commenced in March 1986 with Freehills, where he worked in the general commercial and litigation areas. In June 1993, he joined QBE as general counsel. Since May 2001, he has acted as general counsel and company secretary for the consolidated entity. He is also a director or secretary of a number of QBE controlled entities and acts as chairman of the policy committee and a trustee respectively of QBE sponsored superannuation plans in Australia and New Zealand.

P Smiles LLB, MBA, ACIS

Mr Smiles is the deputy company secretary of QBE Insurance Group Limited and company secretary of various QBE Australian subsidiaries. He has 18 years insurance experience, which includes 11 years as a corporate lawyer. Prior to commencing employment with QBE in 2002, Mr Smiles worked for the NRMA Insurance Group in various corporate roles. In addition to his current company secretarial duties, he also acts as a corporate lawyer advising QBE Group head office departments and Asia Pacific offices.

DIRECTORS' INTERESTS AND BENEFITS

(A) Ordinary share capital

Directors' relevant interests in the ordinary share capital of the company at the date of this report are as follows:

Director	2009 NUMBER	2008 NUMBER
LF Bleasel AM	57,604	52,604
DM Boyle	8,697	5,247
EJ Cloney AM	635,621	635,621
IF Hudson	9,221	8,732
BJ Hutchinson AM	63,496	52,132
CLA Irby	15,000	15,000
IYL Lee	26,749	26,749
FM O'Halloran	1,109,173	1,067,991

(B) Options and conditional rights

At the date of this report, Mr O'Halloran had 466,544 (2008 338,740) options over ordinary shares of the company and 138,562 (2008 105,152) conditional rights to ordinary shares of the company under the Deferred Compensation Plan ("DCP"). Details of the DCP are provided in the remuneration report and in note 27 to the financial statements.

The names of all persons who currently hold options granted under the Employee Share and Option Plan ("the Plan") and conditional rights to ordinary shares of the company are entered in the registers kept by the company pursuant to section 168 of the *Corporations Act 2001* and the registers may be inspected free of charge.

(C) Loans to directors and executives

Information on loans to directors and executives, including amounts, interest rates and repayment terms are set out in note 28 to the financial statements.

(D) Related entity interests

Details of directors' and executives' interests with related entities are provided in note 28 to the financial statements.

Directors' report

FOR THE YEAR ENDED 31 DECEMBER 2009

REMUNERATION REPORT

Key features of executive remuneration in 2009

We have revised the presentation of this year's remuneration report and have included additional detail that we consider appropriate in order to more clearly communicate our approach to remuneration, the changes that we have made and why we considered these changes necessary.

The information provided in this remuneration report has been audited as required by section 308(3C) of the *Corporations Act 2001*.

A	QBE's approach to remuneration – overview	Page 56
B	Executive remuneration framework changes for 2010	Page 57
C	Glossary of key remuneration terms	Page 58
D	QBE's key management personnel	Page 59
E	Executive remuneration	Page 60
F	Group chief executive officer remuneration	Page 66
G	Executive contractual remuneration	Page 66
H	Relationship between remuneration and performance	Page 69
I	Employment agreements	Page 69
J	Total remuneration	Page 70
K	Share based remuneration	Page 71
L	Non-executive director remuneration	Page 74

The board is cognisant of the difficult economic and commercial landscape within which we operate. Due to the uncertain conditions in the last 18 months and the easing in global demand for skilled executives, the upward pressure on remuneration has reduced. This change in the global landscape has resulted in the increase in fixed remuneration for executives being limited, with exceptions made only where a promotion or a significant market re-positioning has taken place. The remuneration committee specifically considered and approved the following:

- fixed remuneration increases for executives on 1 January 2009 were limited to an average of 3.1%;
- no fixed remuneration increases were awarded to executives in the 1 January 2010 review; and
- the directors resolved not to increase directors' fees for 2010.

The remuneration committee also specifically considered and approved the following:

- no at-risk reward (Short-Term Incentive ("STI"), Deferred Compensation Plan ("DCP") or Group Executive Restricted Share Plan ("GERSP")) is payable to Group head office executives if the consolidated entity's return on equity ("ROE") is less than 14%; and
- similarly nothing is payable to the executives in our Australian, Asia Pacific or Americas operations unless a divisional ROE of 15% is achieved and, for Europe, a divisional ROE of 10% is achieved. Our ROE minimum benchmarks are set above those of our peers in the various markets in which we operate. In most cases, these minimum hurdles exceed the hurdles at which the at-risk reward of our peers is maximised.

(A) QBE's approach to remuneration – overview

QBE's approach to remuneration is designed to ensure that shareholders receive value for remuneration and at-risk reward expenditure. The remuneration committee assesses the appropriateness of remuneration frameworks and practices in order to fairly and responsibly reward the executive director, executives and non-executive directors, ensuring rewards are commensurate with performance and that remuneration levels are competitive in the various markets in which we operate. The remuneration committee focuses on ensuring that remuneration and reward strategy and frameworks are aligned with robust risk management practices and strong governance principles.

QBE focuses on ensuring that remuneration and at-risk reward practices provide sustainable long-term value for shareholders whilst attracting, retaining and motivating high quality talent. Although the overall structure of remuneration within QBE has been in place for several years, the organisation and the environment in which we operate is constantly evolving and we aim to ensure that our remuneration framework is flexible enough to adapt to these changes. Options issued in 2007 and 2008 to executives continue to remain below the share price at the grant date (details are provided on page 71) and the value of conditional rights granted in these years has fallen due to the lower QBE share price, demonstrating the alignment between shareholder returns and executive remuneration.

The remuneration committee undertook a review of QBE's remuneration and reward framework during the year to take into account feedback from shareholders and regulators. Key changes were approved for 2010, details of which are outlined on page 57.

During 2009, the remuneration committee has actively considered the guidance published by various regulatory bodies on aligning remuneration frameworks with sound risk management structures and with the consolidated entity's risk appetite. Guidelines and principles published by the Financial Stability Forum, the UK Financial Services Authority and the US Department of Treasury have been considered, and the remuneration committee considers that QBE's remuneration framework is broadly aligned with these guidelines. Specifically, the changes to QBE's remuneration framework for 2010 take into account the principles released by APRA.

Directors' report

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(B) Executive remuneration framework changes for 2010

In light of broad-reaching debate about appropriate levels of executive remuneration and the need to ensure an appropriate balance between risk and reward, the key changes to our at-risk reward structures are:

- the deferred equity component of at-risk remuneration is, and will continue to be, subject to a claw-back for material subsequent deterioration of the relevant ROE;
- the introduction of a new long-term incentive scheme with challenging future performance hurdles;
- no automatic vesting of the total equity award in the event of death, disability, redundancy or retirement; and
- all future share grants to the Group chief executive officer will be subject to shareholder approval.

The table below provides more detail on the changes to executive remuneration:

2009 AT-RISK REMUNERATION	2010 AT-RISK REMUNERATION	COMMENT
<p>STI scheme – annual cash award.</p> <p>DCP – deferred equity award of conditional rights subject to a three and five year tenure hurdle. The award is contingent on there being no material subsequent deterioration of the relevant entity's ROE.</p> <p>Australian, Asia Pacific and European divisional executives are also eligible to receive additional conditional rights when the relevant divisional ROE exceeds 22% or more.</p> <p>The award of options and interest free personal recourse loans under the DCP was discontinued after the March 2009 award.</p>	<p>STI and DCP will be combined to become the QBE Incentive Scheme ("QIS") – consisting of an annual cash incentive and deferred equity award (conditional rights).</p> <p>Vesting of equity under the QIS is subject to a three and five year tenure hurdle and is contingent on there being no material subsequent deterioration of the relevant entity's ROE.</p> <p>The divisional executives are also eligible to receive additional conditional rights when the relevant divisional ROE exceeds 22% or more.</p>	<p>The deferred component of QIS is subject to reduction at the discretion of the remuneration committee.</p> <p>The vesting of the DCP in shares or cash, in both 2009 and 2010, is at the discretion of the remuneration committee.</p> <p>The change to QIS involves no increase in the percentage of at-risk reward.</p> <p>Details are provided on pages 62 to 64 of this report.</p>
<p>The Group general manager – investments' total DCP award is subject to a three year tenure hurdle.</p>	<p>The Group general manager – investments' total DCP award will be subject to a three and five year tenure hurdle, consistent with other executives.</p>	
<p>GERSP – deferred equity award of conditional rights when the consolidated entity's ROE hurdle of 21% is exceeded.</p> <p>Vesting is subject to a three year tenure hurdle. The award is contingent on there being no material subsequent deterioration of the consolidated entity's ROE.</p>	<p>GERSP will be replaced by the Long-Term Incentive Plan ("LTI").</p> <p>Vesting will be subject to the following future performance hurdles:</p> <ul style="list-style-type: none"> • 50% of the award allocation will be contingent on the consolidated entity's average diluted earnings per share ("EPS") increasing by a compound 7.5% per annum over a five year vesting period; and • 50% of the award allocation will be contingent on the consolidated entity's average ROE and combined operating ratio being in the top 10% of the top 50 largest global insurers and reinsurers as measured by net earned premium for the five year vesting period. <p>Vesting will also be subject to a five year tenure hurdle requiring the executive to be employed at the vesting date.</p>	<p>Specific challenging performance hurdles have been included in the LTI in response to shareholders' requests to ensure sustainable business development whilst providing appropriate returns to shareholders.</p> <p>The remuneration committee will have the discretion to vest a proportion of the unvested amount in shares or cash in the event of death, disability, redundancy or retirement.</p>
<p>Notional dividends are added to the value of conditional rights during the vesting period.</p>	<p>Notional dividends are added to the value of conditional rights during the vesting period.</p>	

Further details on all of these changes to our at-risk reward framework are provided in the body of this remuneration report.

Directors' report

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(C) Glossary of key remuneration terms

Set out below are the key remuneration terms and abbreviations used in the remuneration report:

TERM	DEFINITION
Deferred Compensation Plan or DCP	<p>A remuneration arrangement which came into existence on 1 January 2009 and which grants equity benefits (in the form of conditional rights) to participants. Vesting is subject to a tenure hurdle and is contingent on no material subsequent deterioration of the relevant entity's ROE during the vesting period, which is either three or five years. Refer to page 62 for further details.</p> <p>In 2009, the DCP had approximately 530 participants including the consolidated entity's key management personnel.</p>
Executive	<p>For the purpose of the remuneration report, executives comprise the executive director and the other key management personnel who are members of the Group operations executive or Group head office management. Details are provided on page 59 of this report.</p>
Group Executive Restricted Share Plan or GERSP	<p>A remuneration arrangement which came into existence on 1 January 2008, granting conditional rights to participants if the consolidated entity's ROE target of 22% is exceeded. During 2008, the equity under GERSP was referred to as "restricted shares"; however these instruments have the same terms as conditional rights under the DCP.</p> <p>Vesting is subject to a three year tenure hurdle and is contingent on no material subsequent deterioration of the consolidated entity's ROE during the vesting period. Refer to page 64 for further details.</p> <p>Only key management personnel (excluding executive and non-executive directors) were invited to participate in the GERSP. The GERSP ceased on 31 December 2009.</p>
Legacy Deferred Compensation Plan ("Legacy DCP")	<p>A remuneration arrangement which ceased with effect from 1 January 2009, granting equity benefits (in the form of conditional rights and options) to participants. Vesting is subject to a three or five year tenure hurdle. Refer to page 64 for further details.</p>
Long-Term Incentive Plan or LTI	<p>The new long-term incentive plan for key management personnel that replaces the GERSP effective from 1 January 2010. Vesting is subject to a five year performance hurdle and is contingent on no material subsequent deterioration of the consolidated entity's ROE during the vesting period. In addition, two additional performance hurdles have been introduced, being:</p> <ul style="list-style-type: none"> • 50% of the award allocation is contingent on the consolidated entity's average diluted EPS increasing by a compound 7.5% per annum over a five year vesting period; and • 50% of the award allocation is contingent on the consolidated entity's average ROE and combined operating ratio being in the top 10% of the top 50 largest global insurers and reinsurers as measured by net earned premium for the five year vesting period. <p>Participation in the LTI is limited to key management personnel excluding non-executive directors. Refer to page 65 for further details.</p>
QBE Incentive Scheme or QIS	<p>The at-risk reward structure that comprises the STI and DCP effective from 1 January 2010. The QIS will consist of:</p> <ul style="list-style-type: none"> • a cash award delivered annually for meeting ROE or investment income performance targets, linked to annual budget metrics; and • a deferred equity award of conditional rights, subject to a three and five year tenure hurdle.
Short-Term Incentive or STI	<p>Cash remuneration linked to the financial performance of the consolidated entity in a financial year and paid in the following financial year. Refer to page 62 for further details.</p>

Directors' report

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(D) QBE's key management personnel

This report details the remuneration of the directors (executive and non-executive) and those persons having authority and responsibility for planning, directing and controlling the activities of the consolidated entity, either directly or indirectly. This group is collectively defined as "key management personnel". AASB 124: Related Party Disclosures specifically requires that non-executive directors are included as key management personnel even though they are not part of QBE's "management".

Key management personnel of the consolidated entity in 2009 are listed in the tables below. The executives included in the table below are considered to be key management personnel because they are members of either the Group operations executive ("GOE") or the Group head office management ("GHOM"), these being the management bodies responsible for the consolidated entity's strategy and operations.

NAME	POSITION
Non-executive directors	
LF Bleasel AM	Director
DM Boyle	Director
EJ Cloney AM	Chairman
IF Hudson	Director
BJ Hutchinson AM	Director
CLA Irby	Director
IYL Lee	Director

NAME	POSITION	EXECUTIVE RESPONSIBILITY
Executive director		
FM O'Halloran	Group chief executive officer	GHOM, GOE
Executives		
SP Burns	Chief executive officer, European operations	GOE
NG Drabsch	Group chief financial officer	GHOM, GOE
D Fogarty	General manager, Equator Re	GHOM
MJ Goodwin	Chief executive officer, Asia Pacific operations	GOE
MD ten Hove	Group general manager – investments	GHOM
TW Ibbotson	Chief executive officer, Australian operations	GOE
V McLenaghan	Group chief operating officer	GHOM, GOE
BM Nicholls ⁽¹⁾	Group chief actuarial officer	GHOM
DA Ramsay ⁽¹⁾	Group general counsel and company secretary	GHOM
J Rumpler ⁽²⁾	President and chief executive officer, the Americas	GOE
JM Smith ⁽¹⁾	Group general manager, human resources	GHOM
GB Thwaites ⁽¹⁾	Group chief risk officer	GHOM

(1) Mr Nicholls, Mr Ramsay, Ms Smith and Mr Thwaites are included as key management personnel for the first time this year. Comparative remuneration information is included throughout this report.

(2) Mr Rumpler was appointed president and chief executive officer of QBE the Americas on 15 June 2009.

(3) The table above includes the five highest paid executives of the consolidated entity as required by the *Corporations Act 2001*.

Directors' report

FOR THE YEAR ENDED 31 DECEMBER 2009

(E) Executive remuneration

(i) Remuneration and reward philosophy

Remuneration practices vary in each of the markets within which QBE operates, and therefore the diversity of individual roles and the complexity of each operating environment is considered. The remuneration committee recognises that the consolidated entity operates in a competitive environment where the key to achieving sustained performance is to motivate and retain quality employees and to align executive reward with increasing shareholder wealth.

The guiding principles applied in managing remuneration and reward for executives combine:

- linking individual performance to the achievement of financial targets and business strategies;
- the achievement of short-term and long-term financial profit targets that deliver top quartile ROE performance against our peers, being the top 50 global insurers and reinsurers as measured by net earned premium;
- sustained growth in value for shareholders through the ROE, insurance profit and investment performance;
- providing a transparent performance and reward methodology that is well understood; and
- using market data to set competitive fixed remuneration levels.

The remuneration committee seeks the advice of independent remuneration consultants and advisers to ensure that remuneration and reward levels are appropriate and are in line with market conditions in the various countries in which the consolidated entity operates. The remuneration committee endeavours to have remuneration structures in place that encourage the achievement of a return for shareholders in terms of both dividends and growth in share price.

The remuneration committee reviews and approves the terms of the cash awards under the STI scheme and the deferred equity awards under the DCP and GERSP, details of which are set out in this report. It also approves the total cash incentive and deferred compensation for executives based on the applicable audited financial results (other than the Group chief executive officer whose quantum is approved by the board). The success of the schemes is demonstrated by the low turnover of senior employees over many years and the wealth that has been created for shareholders as demonstrated in the table on page 69.

(ii) Performance and reward

QBE has a highly experienced executive team with a strong retention record. The average tenure of QBE's executive team (including the Group chief executive officer) is 16.3 years. All executives have position descriptions in place which set out their roles, accountabilities and duties. They also have employment contracts which confirm their remuneration and reward arrangements, including entitlements on termination.

Executives are required to adhere to a range of Group wide policies to ensure risk taking is managed, strong governance structures are in place and high ethical standards are maintained. These policies are communicated to employees across various intranets in operation throughout the Group.

All executives have their performance evaluated annually by the Group chief executive officer through formal business review assessments to ensure financial performance targets are achieved. This is generally followed by a formal Personal Development Plan ("PDP") process. The PDP process provides feedback to an executive on their overall performance against their position description, demonstrated behaviours and an assessment of current capability and future potential.

The current executive remuneration and reward structures ensure remuneration properly reflects the accountabilities and duties of the role, and sustained high performance is rewarded based on the achievement of financial results which deliver top quartile performance against our peers in the insurance industry.

(iii) Remuneration framework

Total remuneration for executives is made up of the following components:

TOTAL REMUNERATION	PURPOSE	COMPONENTS OF REMUNERATION
Fixed remuneration	Attraction and retention – market competitive, positioned between 62.5th and 75.0th percentile	Consists of base salary, superannuation, other guaranteed benefits and applicable fringe benefit taxes
At-risk reward	Link to performance – ROE targets linked to Group and divisional performance, and reflecting the skills and expertise of the individual	Consists of: <ul style="list-style-type: none"> • cash award through the STI • deferred equity award through the DCP From the 2010 performance year, the STI and DCP together will be referred to as the QBE Incentive Scheme or QIS
	Alignment to shareholder value – consolidated entity ROE target must be exceeded	Consists of deferred equity award through the GERSP From the 2010 performance year, the GERSP will be replaced with a Long-Term Incentive Plan or LTI

When considering remuneration and reward structures, the remuneration committee reviews each component with a view to ensuring that the appropriate balance is achieved between fixed and at-risk remuneration. Independent remuneration consultants normally prepare external comparative benchmark data on the Group chief executive officer and executives.

Directors' report

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(E) Executive remuneration continued

(iv) Fixed remuneration

QBE's fixed remuneration includes base (cash) salary, superannuation and other benefits (such as the value of motor vehicles, health insurance, life assurance, personal accident insurance, allowances, and the applicable taxes thereon). It excludes deemed interest on employee share loans and long service leave accruals (if applicable).

Fixed remuneration is targeted at the external market between the 62.5th and 75.0th percentile which is considered a competitive position consistent with the consolidated entity's reward philosophy. To assess competitiveness of fixed remuneration for Australian-based executives, the remuneration committee will consider a defined comparative group of companies with a similar market capitalisation to the consolidated entity (i.e. generally 50% to 200% of the consolidated entity's market capitalisation based on the most recent six month average market value information available) as well as applying judgment to determine what is appropriate to the individual and the role. For those executive roles where there is insufficient market data, the sizing criteria is expanded to 25% to 400% of market capitalisation. Market data on the US and the UK is gathered from relevant external surveys. A similar benchmarking approach, with the emphasis on a comparative group of a similar size to the relevant US or UK operations, is used to filter survey data for both the US and UK executives.

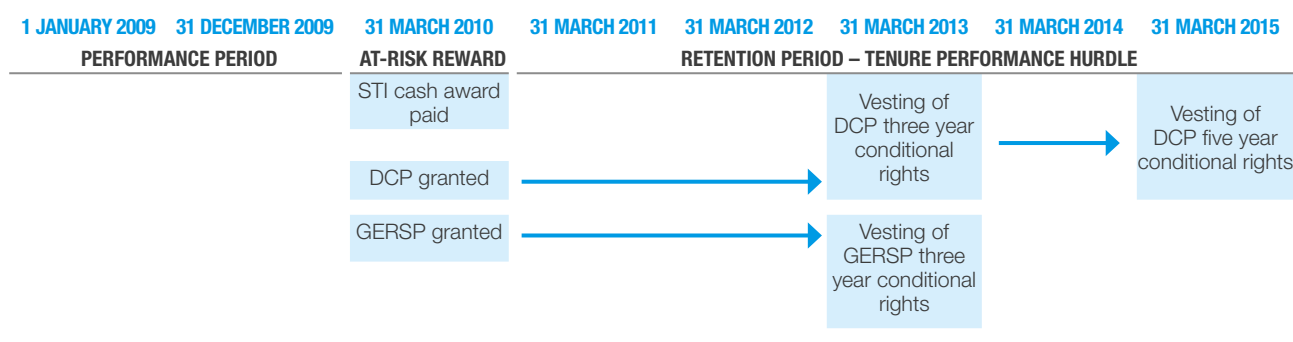
Fixed remuneration is generally reviewed annually against equivalent roles in the market and with reference to the sustained performance of the executive.

(v) 2009 at-risk reward

The consolidated entity's at-risk remuneration structures reward the achievement of ROE targets. During 2009, at-risk remuneration included three components:

- cash awards paid under the STI scheme;
- deferred equity awards granted under the DCP; and
- deferred equity awards granted under the GERSP.

The diagram below illustrates the consolidated entity's at-risk reward delivery structure in relation to cash and deferred equity awards.



To appropriately align executive remuneration and reward, the remuneration committee has determined that the achievement of top quartile performance against peers in the insurance industry is the appropriate basis for granting at-risk rewards. This is considered a more meaningful benchmark than measuring our performance relative to a market index or against average market returns.

The remuneration committee has considered implementation of a performance hurdle based on a Total Shareholder Return ("TSR") measured against an identified peer group, TSR being the change in capital value of a listed entity's share price over a defined period, including reinvested dividends, expressed as a percentage of the opening value. This was rejected due to the absence of an appropriate peer group benchmark in Australia. In addition, the view of the remuneration committee is that executives do not have direct control or substantial influence over a TSR performance measure, and its value in sustaining growth for shareholders cannot be substantiated. A focus on outperformance of our competitors and peers is therefore considered to add more value to shareholders over the longer term.

The philosophy of the consolidated entity has been, and remains, that its long-term success is a result of sound operating performance measured by financial metrics such as ROE and investment performance, prudent risk taking, solid strategic decision making and the focus of key executives on the underlying business performance indicators and profit drivers. The achievement of ROE targets continues to be appropriate as the most fundamental performance measure of the strength of the consolidated entity. It is a strong objective measure of value created, it represents shareholders' "bottom line" and is understood and accepted by institutional investors.

ROE targets on a financial year basis are considered to be the most appropriate measure of executive performance. To ensure that focus is maintained on the achievement of ROE targets, the board approves the consolidated entity's business plan and appropriate financial targets for each performance year, including minimum ROE hurdles commencing at levels well above the majority of QBE's peers around the world. The board regularly reviews progress against ROE targets.

Directors' report

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(E) Executive remuneration continued

The consolidated entity's business plan is the sum of the individual business unit, entity and divisional business plans. Entity plans are cascaded into individual employee performance objectives, with a link to each division's ROE target and non-financial performance measures. Individual employee performance is generally measured on a bi-annual basis through QBE's performance management process ("PMP"). An individual's assessment through the PMP is linked to each division's STI scheme.

Short-term incentive (STI) scheme

The STI scheme is a performance-based incentive delivered in the form of an annual cash award for a performance measurement period of 12 months. The STI scheme is designed to reward executives by recognising the contributions and achievements of individuals when annual ROE and investment income targets relating to the previous financial year's performance of the business unit, the division or the consolidated entity as appropriate are achieved or exceeded.

The table below summarises the 2009 financial performance targets for each executive defined as key management personnel of QBE. It also sets out the STI achievable as a percentage of fixed remuneration. The varying STI achievement levels applicable to each executive reflect an executive's relative influence on organisational performance. STI schemes are aligned with shareholders' interests to ensure that short-term incentives are more beneficial to executives when minimum ROE targets are exceeded.

EXECUTIVE	FINANCIAL TARGET	RESULT BASIS	RETURN ON EQUITY		MAXIMUM STI AS A % OF FIXED REMUNERATION
			MINIMUM	MAXIMUM	
SP Burns	European operations ROE	Financial year result	10%	22%	133%
NG Drabsch	Consolidated entity ROE	Financial year result (seven year spread basis)	14%	21%	117%
D Fogarty ⁽¹⁾	Consolidated entity ROE	Financial year result (seven year spread basis)	14%	21%	94%
MJ Goodwin ⁽²⁾	Asia Pacific operations ROE	Financial year result	15%	24%	125%
MD ten Hove	Investment income as a % of budget income and individual performance measures. Management key performance indicators	Financial year result	n/a	n/a	100% 25%
TW Ibbotson ⁽³⁾	Australian operations ROE	Financial year result	15%	24%	125%
V McLenaghan	Consolidated entity ROE	Financial year result (seven year spread basis)	14%	21%	133%
BM Nicholls	Consolidated entity ROE	Financial year result (seven year spread basis)	14%	21%	94%
DA Ramsay	Consolidated entity ROE	Financial year result (seven year spread basis)	14%	21%	94%
J Rumpler ⁽⁴⁾	the Americas ROE	Financial year result	15%	22%	133%
JM Smith	Consolidated entity ROE	Financial year result (seven year spread basis)	14%	21%	94%
GB Thwaites	Consolidated entity ROE	Financial year result (seven year spread basis)	14%	21%	94%

(1) Mr Fogarty is based in Dublin. STI is calculated using his base (cash) salary.

(2) Mr Goodwin is based in Singapore. STI is calculated using his overseas (assignment) net salary (excluding any positive cost of living adjustment).

(3) Mr Ibbotson's STI is calculated using fixed remuneration less rental allowance.

(4) Mr Rumpler was appointed to the role of president and chief executive officer, the Americas on 15 June 2009. From 1 January to 14 June 2009, Mr Rumpler's STI was calculated using the Australian operations ROE.

Deferred Compensation Plan (DCP)

Key management personnel (excluding non-executive directors) and other key senior employees are eligible to participate in the DCP. It provides executives with the opportunity to acquire equity in the form of conditional rights to fully paid shares without payment by the executive.

An executive is entitled to participate in the DCP only when the STI is earned. The DCP aims to retain key executives and to increase shareholder value by motivating executives to increase profit and the value of QBE shares. The board believes that the DCP is a valuable reward mechanism which encourages retention of key talent.

Deferred equity delivered under the terms of the DCP is subject to a tenure hurdle. Shares will only vest if the individual has remained in service throughout the three or five year vesting period. Notional dividends, payable in the form of QBE shares, accrue on the conditional rights during the vesting period. The remuneration committee has the discretion to pay cash in lieu of shares in certain circumstances such as death, disability, redundancy or retirement if the individual is not subject to disciplinary proceedings or notice on that date. The tenure hurdle places significant focus on sustained share price growth over the longer term and provides a significant retention element for the executive.

Directors' report

FOR THE YEAR ENDED 31 DECEMBER 2009

(E) Executive remuneration continued

DCP operative from 1 January 2009 and applicable to awards in March 2010

For DCP awards made in March 2010 and thereafter in respect of financial performance for 2009 and later financial years, executives will only receive conditional rights to fully paid shares. The maximum DCP award is based on an amount which is the lesser of 80% of the STI award (previously 66.67%) in that year or 100% of fixed remuneration or base (cash) salary as at 31 December in the financial year prior to the year in which the STI award is paid.

The maximum DCP award is used as the basis of calculating the number of conditional rights to fully paid shares as follows:

- conditional rights to the value of 50% of the DCP award, converted to shares after three years; and
- conditional rights to the value of 50% of the DCP award, converted to shares after five years.

The share price upon which the allocation of conditional rights is calculated is the weighted average sale price of QBE shares over the five trading days on the ASX prior to the grant date.

The ultimate vesting of the conditional rights is also contingent on there being no material subsequent deterioration of the consolidated entity's ROE during the vesting period. Notional dividends earned are added to the value of the conditional rights granted during the vesting period.

The following example illustrates how a DCP award is calculated:

STI AWARD			DCP AWARD – CONDITIONAL RIGHTS				
FIXED REMUNERATION	% OF FIXED REMUNERATION	STI	MAXIMUM DCP AWARD ⁽¹⁾	THREE YEARS		FIVE YEARS	
				50% OF DCP AWARD	NO. OF SHARES ⁽²⁾	50% OF DCP AWARD	NO. OF SHARES ⁽²⁾
\$400,000	50%	\$200,000	\$160,000	\$80,000	3,810	\$80,000	3,810

(1) Lesser of 80% of STI award or 100% of fixed remuneration.

(2) This example assumes a share price of \$21.

Enhanced DCP awards based on divisional ROE achievement

Divisional chief executive officers are eligible to benefit from an enhanced DCP award with effect 1 January 2008. The first award was made in March 2009. This enhanced DCP award aims to retain and reward these key executives and to increase shareholder value by motivating them to exceed ROE targets. It provides the relevant divisional executives with the opportunity to acquire additional equity in the form of conditional rights without payment by the executive if the division for which the relevant executive is responsible exceeds a specified divisional ROE target for STI.

Deferred equity under this award is subject to a three year tenure hurdle. Shares will only vest if the individual has remained in service throughout the vesting period. The remuneration committee has the discretion to pay cash in lieu of shares in certain circumstances such as death, disability, redundancy or retirement if the individual is not subject to disciplinary proceedings or notice on that date. Notional dividends, payable in the form of QBE shares, accrue on the conditional rights during the vesting period. The ultimate vesting of the conditional rights is contingent on no material subsequent deterioration of the division's ROE during the vesting period.

The value of the conditional rights allocated varies for each executive ranging from 3% up to 15% of fixed remuneration or base (cash) salary as appropriate, except for Mr Burns whose award ranges from 5% to 50% of STI. To calculate the number of conditional rights granted, the award value is divided by the weighted average sale price of QBE shares over the five trading days on the ASX prior to the grant date (generally the first week of March). The relevant ROE hurdles, the minimum and maximum awards and the actual award for the 2009 financial year are shown in the table below.

EXECUTIVE	MINIMUM AND MAXIMUM ROE HURDLES	MINIMUM AND MAXIMUM AWARD AS A % OF FIXED REMUNERATION	ACTUAL AWARD AS A % OF FIXED REMUNERATION ⁽⁴⁾
Performance hurdles in relation to divisional ROE achievement			
SP Burns ⁽¹⁾	22% – 32%	5% – 50%	6%
MJ Goodwin ⁽²⁾	22% – 27%	3% – 15%	11%
TW Ibbotson ⁽³⁾	22% – 27%	3% – 15%	–

(1) Mr Burns' award is determined as a percentage of STI.

(2) Mr Goodwin is based in Singapore. His award is calculated using his Australian plan (superannuation) salary.

(3) Mr Ibbotson's award is calculated using fixed remuneration less rental allowance.

(4) Mr Rumpler did not participate in this scheme for 2009. His participation will commence in the 2010 financial year.

Directors' report

FOR THE YEAR ENDED 31 DECEMBER 2009

(E) Executive remuneration continued

Legacy DCP operative until 31 December 2008 and applicable to awards in March 2009 and prior

For DCP awards made up to and including March 2009 in relation to financial performance in 2008 and prior years, executives were provided with the opportunity to acquire equity in the form of conditional rights to fully paid shares without payment by the executive and options to subscribe for shares at market value at the grant date. The DCP award amount was restricted to the lesser of 66.67% of the STI award in that year or 100% of fixed remuneration or base (cash) salary as at 31 December in the financial year prior to the year in which the STI award was paid.

This DCP award amount was used to acquire conditional rights to fully paid shares and options respectively as follows:

- conditional rights to shares to the value of 60% of the DCP award; and
- options over ordinary shares to the value of 40% of the DCP award, with the resulting number multiplied by three.

Conditional rights and options relating to the achievement of profit targets in the financial year were granted in March of the following year. Interest free personal recourse loans were available on terms permitted by the Employee Share and Option Plan to persons in the employment of the consolidated entity who hold options under the DCP, to fund the exercise of the options.

Conditional rights and options issued in 2004 and prior financial years were exercisable after three years. Options issued in 2005 and later financial years are exercisable after five years, with the exception of options for senior employees in the Group investment division which continue to be exercisable after three years. The issue of options and interest free personal recourse loans under the DCP will cease after the final vesting of all incentives granted in March 2009.

Group Executive Restricted Share Plan (GERSP)

Key management personnel (excluding non-executive directors, the Group chief executive officer and Mr Burns) were eligible to participate in the GERSP with effect from its inception on 1 January 2008. The GERSP will be replaced in 2010 by the Long-Term Incentive Plan or LTI. Refer to page 65 for further details of the LTI.

The first award was made in March 2009. The GERSP aims to retain and reward key executives and to increase shareholder value by motivating executives to exceed consolidated entity ROE targets. It provides executives with the opportunity to acquire additional equity in the form of conditional rights (referred to as restricted shares in 2008) without payment by the executive if the consolidated entity's ROE target is exceeded.

Each participant receives an award of conditional rights if the consolidated entity exceeds a ROE on a seven year spread basis of 21%.

The benefit to each participant is maximised when the consolidated entity achieves a ROE of 26%. The actual ROE for 2009 on the seven year spread basis of accounting was 20.2% which means that no awards will be made under the GERSP.

Deferred equity delivered under the terms of the GERSP is subject to a three year tenure hurdle. Shares will only vest if the individual has remained in service throughout the vesting period. Notional dividends, payable in the form of QBE shares, accrue on the conditional rights during the vesting period. The ultimate vesting of the conditional rights is contingent on no material subsequent deterioration of the consolidated entity's ROE during the vesting period.

The value of the conditional rights allocated varies for each executive ranging from 3% up to 25% of fixed remuneration or base (cash) salary as appropriate. To calculate the number of conditional rights to be granted, the award value is divided by the weighted average sale price of QBE shares over the five trading days on the ASX prior to the grant date (generally the first week of March). The results used for determining the minimum and maximum awards that could be earned under the GERSP for the 2009 financial year are shown in the table below.

EXECUTIVE	MINIMUM AND MAXIMUM ROE HURDLES	MINIMUM AND MAXIMUM AWARD AS A % OF FIXED REMUNERATION	ACTUAL AWARD AS A % OF FIXED REMUNERATION ⁽⁴⁾
Performance hurdles in relation to the consolidated entity's ROE achievement			
NG Drabsch	22% – 26%	5% – 25%	–
D Fogarty ⁽¹⁾	22% – 26%	3% – 15%	–
MJ Goodwin ⁽²⁾	22% – 26%	3% – 15%	–
MD ten Hove	22% – 26%	3% – 15%	–
TW Ibbotson ⁽³⁾	22% – 26%	3% – 15%	–
V McLenaghan	22% – 26%	5% – 50%	–
BM Nicholls	22% – 26%	3% – 15%	–
DA Ramsay	22% – 26%	3% – 15%	–
JM Smith	22% – 26%	3% – 15%	–
GB Thwaites	22% – 26%	3% – 15%	–

(1) Mr Fogarty is based in Dublin. His GERSP award is calculated using his base (cash) salary.

(2) Mr Goodwin is based in Singapore. His GERSP award is calculated using his Australian plan (superannuation) salary.

(3) Mr Ibbotson's GERSP award is calculated using fixed remuneration less rental allowance.

(4) Mr Rumpler did not participate in GERSP for 2009. His participation in the LTI will commence from the 2010 financial performance year.

Directors' report

FOR THE YEAR ENDED 31 DECEMBER 2009

(E) Executive remuneration continued

2010 Long-Term Incentive Plan (LTI)

From the 2010 financial year, a new LTI has been introduced to replace the GERSP. The first award will be granted in March 2011 and, subject to achievement of the performance hurdles below, will vest in March 2016. Specific risk-related performance measurements and an EPS measure will be introduced to ensure alignment with APRA's guidelines on prudent risk taking for long-term financial soundness of the business and with shareholders interests. The Group chief executive officer has been invited to participate in the LTI. He was not a participant in the GERSP.

The LTI will comprise an award of conditional rights at no cost to executives including the Group chief executive officer. The award will be subject to a five year tenure hurdle and will also be contingent on the achievement of two future performance hurdles as follows:

- 50% of the award allocation will be contingent on the consolidated entity's average diluted EPS increasing by a compound 7.5% per annum over the five year vesting period; and
- 50% of the award allocation will be contingent on the consolidated entity's average ROE and combined operating ratio being in the top 10% of the top 50 largest global insurers and reinsurers as measured by net earned premium for the five year vesting period.

These combined performance hurdles will determine the number of conditional rights to vest in March 2016, up to a maximum of between 15% to 50% of fixed remuneration or base (cash) salary as appropriate to each executive as shown in the table below.

	AWARD AS A % OF FIXED REMUNERATION – DILUTED EPS HURDLE	AWARD AS A % OF FIXED REMUNERATION – ROE AND COMBINED OPERATING RATIO HURDLE	MAXIMUM AWARD AS A % OF FIXED REMUNERATION
Executive Director			
FM O'Halloran	25.0%	25.0%	50.0%
Executives			
SP Burns	7.5%	7.5%	15.0%
NG Drabsch	12.5%	12.5%	25.0%
D Fogarty	7.5%	7.5%	15.0%
MJ Goodwin	7.5%	7.5%	15.0%
MD ten Hove	7.5%	7.5%	15.0%
TW Ibbotson	7.5%	7.5%	15.0%
V McLenaghan	25.0%	25.0%	50.0%
BM Nicholls	7.5%	7.5%	15.0%
DA Ramsay	7.5%	7.5%	15.0%
J Rumpler	7.5%	7.5%	15.0%
JM Smith	7.5%	7.5%	15.0%
GB Thwaites	7.5%	7.5%	15.0%

The remuneration committee will continue to exercise discretion when determining the vesting of awards under the LTI. The remuneration committee has the discretion to allocate a pro-rata amount in cash in lieu of shares in certain circumstances such as death, disability, redundancy or retirement.

Directors' report

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(F) Group chief executive officer remuneration

Consistent with other executives, in addition to fixed remuneration, Mr O'Halloran is entitled to an annual cash incentive award under the STI scheme if specified targets are achieved, calculated as a percentage of fixed remuneration. Mr O'Halloran's at-risk rewards are based on the achievement of a target ROE for the 2009 financial year determined using QBE's seven year spread management basis of accounting. The seven year spread basis of accounting spreads realised and unrealised gains on equities and properties evenly over a period of seven years. The net profit after tax for 2009 using the seven year spread basis of accounting was \$2,018 million compared with \$1,818 million in 2008. On this basis, the return on opening shareholders' funds adjusted for dividends, currency translation and share capital issued during the year was 20.2% compared with 22.6% last year.

The table below outlines Mr O'Halloran's incentives based on target and actual ROE:

	GROUP RETURN ON EQUITY %	STI AWARD AS A % OF FIXED REMUNERATION
Minimum target	14%	15%
Maximum target	21%	134%
Achieved result	20.2%	119%

Mr O'Halloran, on a basis consistent with other executives, is also entitled to receive conditional rights to fully paid shares under the DCP in relation to 2009 performance. These will vest in three and five years respectively. The remuneration committee has the discretion to pay cash in lieu of shares on Mr O'Halloran's retirement.

The table below illustrates how Mr O'Halloran's STI and DCP awards are calculated:

STI AWARD			DCP AWARD – CONDITIONAL RIGHTS				
FIXED REMUNERATION	% OF FIXED REMUNERATION	STI	MAXIMUM DCP AWARD ⁽¹⁾	THREE YEARS		FIVE YEARS	
				50% OF DCP AWARD	NO. OF SHARES ⁽²⁾	50% OF DCP AWARD	NO. OF SHARES ⁽²⁾
\$2,157,435	119%	\$2,560,568	\$2,048,454	\$1,024,227	45,562	\$1,024,227	45,562

(1) Lesser of 80% of STI award or 100% of fixed remuneration.

(2) This example assumes a share price of \$22.48.

Based on the achievement of an actual ROE of 20.2%, Mr O'Halloran is entitled to receive the following awards:

- a short-term incentive payment of \$2,560,568; and
- conditional rights to fully paid shares without payment under the terms of the DCP with a value of \$2,048,454. This equates to an award of 91,124 shares.

The maximum DCP award is based on an amount which is the lesser of 80% of the STI award or 100% of fixed remuneration. The maximum DCP award is used as the basis for calculating the number of conditional rights (50% vesting in three years and 50% vesting in five years).

The actual share price used to determine the final number of shares that will be issued to Mr O'Halloran in relation to his award of conditional rights will be the weighted average price of the company's ordinary shares traded on the ASX during the five trading days from 26 February 2010, being the date on which QBE's annual result is announced to the ASX. For indicative purposes, a share price of \$22.48 has been used above, being the weighted average price of the company's ordinary shares traded on the ASX during the five day period to 12 February 2010.

Mr O'Halloran did not participate in the GERSP but has been invited to participate in the LTI with effect from 1 January 2010. The potential value of the LTI award will be up to a maximum of 50% of fixed remuneration at grant date.

(G) Executive contractual remuneration

(i) 2009 contractual entitlements

The following table summarises the contractual remuneration arrangements for each executive for the financial year ended 31 December 2009. This table reflects individual remuneration arrangements as they are viewed by the consolidated entity. The value of the equity component reflects the award earned under the DCP and GERSP that will be used to fund conditional rights awarded to the executive. It does not use the valuation methods set out under the accounting standards. Information using valuation methods as required by accounting standards is included in total remuneration on page 70.

Directors' report

FOR THE YEAR ENDED 31 DECEMBER 2009

(G) Executive contractual remuneration continued

	FIXED REMUNERATION ⁽¹⁾ \$'000	STI RESULT %	STI AWARD \$'000	DCP \$'000	TOTAL \$'000
Executive director					
FM O'Halloran	2,157	119	2,561	2,048	6,766
Executives					
SP Burns ⁽²⁾	1,703	133	2,271	2,170	6,144
NG Drabsch	989	104	1,025	820	2,834
D Fogarty	629	83	523	419	1,571
MJ Goodwin ⁽²⁾	414	125	516	628	1,558
MD ten Hove	979	125	1,223	979	3,181
TW Ibbotson	815	89	684	547	2,046
V McLenaghan	1,100	118	1,280	1,024	3,404
BM Nicholls	630	83	525	420	1,575
DA Ramsay	750	83	606	485	1,841
J Rumppler	1,143	81	508	406	2,057
JM Smith	592	83	493	394	1,479
GB Thwaites	600	83	479	383	1,462

(1) Fixed remuneration is at 31 December 2009. It excludes deemed interest on employee share loans and long service leave accruals (if applicable). For executives located overseas, amounts have been converted to Australian dollars using cumulative average rates of exchange.

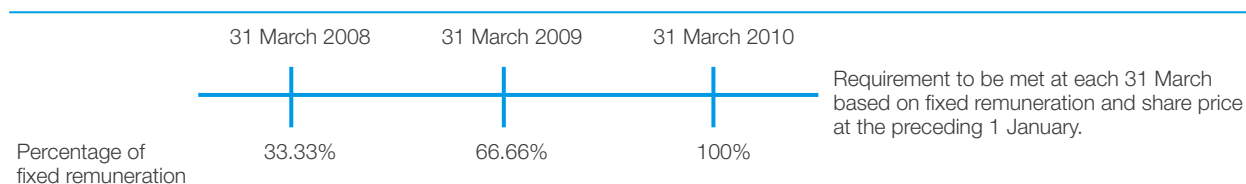
(2) Equity awards include enhanced DCP awards. Refer to page 63 for detail.

The following specific arrangements exist in addition to the benefits outlined in the table above:

EXECUTIVE	EMPLOYMENT ARRANGEMENT
SP Burns	Subject to the achievement of financial hurdles, Mr Burns will receive a contractually agreed bonus payment on 31 December 2010 of one year's fixed remuneration. In addition, 100,000 future performance options are being granted at \$20.44 in tranches of 20,000 over a five year period from March 2007 and vesting within three months of 31 December 2010. The agreed bonus payment and options were approved by the remuneration committee in October 2005 as a five year retention incentive.
V McLenaghan	In addition to annual awards under the DCP and GERSP, 20,000 conditional rights were granted on 1 January 2009 which will vest in March 2012. The award of conditional rights was in recognition of Mr McLenaghan's additional responsibilities as acting president and chief executive officer in the Americas from September 2008 to June 2009.

(ii) Executive minimum shareholding requirement

With effect from 31 March 2008, a policy was introduced whereby key management personnel (excluding non-executive directors) are required to accumulate and maintain a minimum vested shareholding in the consolidated entity equivalent to one year's fixed remuneration by 31 March 2010. New executives are required to build their shareholdings over a three year period after the first equity grant vests. The executive minimum shareholding requirement encourages executives to actively build their shareholdings and ensures they have significant exposure to the consolidated entity's share value and, by so doing, ensures their long-term interests are aligned with the best interests of shareholders. If an executive does not meet the minimum shareholding as at the requirement date annually (i.e. 31 March), the consolidated entity will impose a restriction on the sale of any further equity grants. Effective 31 March 2009, all key management personnel had met the necessary minimum shareholding requirement with the exception of Mr Goodwin who has been granted an exemption until 31 March 2012 due to his recent appointment.



Directors' report

FOR THE YEAR ENDED 31 DECEMBER 2009

(G) Executive contractual remuneration continued

(iii) Hedging policy

Guidelines exist stating that non-executive directors, key management personnel and key senior employees should notify any intended share transaction to nominated people within the Group, including hedging of vested entitlements. The guidelines also prohibit the hedging of unvested entitlements. The purpose of this prohibition is to ensure that, until awards granted under the DCP and GERSP have vested, there is an alignment between the interests of key management personnel and shareholders, with the effect that market share value movements (either positive or negative) will economically impact the executive.

In addition, trading in QBE ordinary shares is generally only permitted during designated trading windows.

The guidelines are enforced by requiring each non-executive director and key management personnel to sign an annual declaration that indicates compliance with the restrictions on hedging.

(iv) Total reward mix

The total reward mix for executives includes "fixed remuneration" and "at-risk" components based on the contractual entitlements outlined on page 67. Base salary, superannuation and benefits are "fixed remuneration" whilst the STI, DCP and GERSP are "at-risk". Consistent with market practice, the mix of total remuneration and reward is reflective of the executive's ability to influence the consolidated entity's financial results. Total maximum potential reward mix and the actual reward mix for the current and prior reporting periods is as follows:

	YEAR	MAXIMUM POTENTIAL REWARD MIX				ACTUAL REWARD MIX			
		FIXED REMUNERATION	AT-RISK REWARD			FIXED REMUNERATION	AT-RISK REWARD		
		%	STI %	DCP %	GERSP %	%	STI %	DCP %	GERSP %
Executive director									
FM O'Halloran	2009	30	40	30	–	32	38	30	–
	2008	32	44	24	–	32	44	24	–
Executives									
SP Burns	2009	28	37	35	–	28	37	35	–
	2008	26	35	39	–	26	35	39	–
NG Drabsch	2009	30	35	28	7	35	36	29	–
	2008	33	38	21	8	34	40	23	3
D Fogarty	2009	35	33	27	5	40	33	27	–
	2008	38	36	20	6	40	37	21	2
MJ Goodwin	2009	25	31	39	5	27	33	40	–
	2008	28	36	31	5	29	37	32	2
MD ten Hove	2009	29	37	29	5	31	38	31	–
	2008	32	41	22	5	62	23	12	3
TW Ibbotson	2009	29	35	32	4	40	33	27	–
	2008	34	37	25	4	35	39	24	2
V McLenaghan	2009	26	35	26	13	32	38	30	–
	2008	28	37	21	14	31	41	23	5
BM Nicholls	2009	35	33	27	5	40	33	27	–
	2008	38	36	20	6	40	37	21	2
DA Ramsay	2009	35	33	27	5	40	33	27	–
	2008	38	36	20	6	40	37	21	2
J Rumpfer	2009	33	38	29	–	48	29	23	–
	2008	36	41	23	–	48	33	19	–
JM Smith	2009	35	33	27	5	40	33	27	–
	2008	38	36	20	6	40	37	21	2
GB Thwaites	2009	35	33	27	5	40	33	27	–
	2008	38	36	20	6	40	37	21	2
Former key management personnel									
TM Kenny	2009	–	–	–	–	–	–	–	–
	2008	33	43	24	–	60	40	–	–

Directors' report

FOR THE YEAR ENDED 31 DECEMBER 2009

(H) Relationship between remuneration and performance

Although the commercial and economic landscape over the last 18 months has been challenging, the remuneration committee is of the view that QBE's remuneration approach has contributed to its significant results outperformance relative to its domestic and global peers in the current market conditions.

QBE's remuneration and reward frameworks encourage the achievement of a return for shareholders in terms of both dividends and growth in share price. A significant component of executive remuneration is at-risk, ensuring a direct link between the consolidated entity's performance and the reward for executives. An overview of "at-risk" remuneration is included on page 61. Overall levels of executive remuneration take into account the ROE performance of the consolidated entity over a number of years, with greater emphasis given to the current financial year. The use of financial profit targets ensures that executives focus on delivering superior returns to shareholders.

Over the period from 2005 to 2009:

- the consolidated entity's net profit after income tax increased by an average of 16% per annum;
- dividends per share increased by an average of 16% per annum;
- return on average shareholders' funds has averaged 23%;
- basic EPS increased by 8% per annum; and
- the share price increased from \$19.60 to \$25.62, an average of 7% per annum.

During the same period, average executive remuneration (fixed remuneration and at-risk STI) grew by approximately 7% per annum.

QBE's strong results in the last five years across a number of key performance indicators are summarised below:

		2005	2006	2007	2008	2009
Earnings						
Net profit after income tax	\$M	1,091	1,483	1,925	1,859	1,970
Basic earnings per share	cents	144.3	186.4	225.7	208.8	196.5
Return on equity						
Return on average shareholders' funds	%	23.9	26.1	26.1	20.9	18.4
Return on equity (seven year spread basis)	%	26.3	29.3	28.4	22.6	20.2
Returns to shareholders						
Dividends paid	cents per share	71.0	95.0	122.0	126.0	128.0
Share price at 31 December	\$ per share	19.60	28.85	33.34	25.81	25.62

(I) Employment agreements

The terms and conditions of employment of each executive reflect market conditions at the time of their contract negotiation and appointment. The material terms of the employment agreements for the Group chief executive officer and executives are summarised in the table below:

CONTRACTUAL TERM	PERSONS AFFECTED	CONDITIONS
Duration of contract	CEO and other executives	Permanent full-time contract until notice given by either party.
Notice to be provided by executive or QBE	CEO and other executives	Written notice varies from four weeks up to 12 months.
Involuntary termination	CEO and other executives	In the event of termination through death, disability, redundancy or retirement and no disciplinary procedure or notice is pending, the executive is entitled to the value of outstanding STI, legacy DCP and GERSP awards for previous years plus a pro-rata share of the value of STI and conditional rights for the current financial year.
Voluntary termination	CEO and other executives	In the case of voluntary termination, executives forfeit all conditional rights to ordinary shares not yet vested under the DCP and GERSP and all unexercised options under the DCP. QBE may pay an executive fixed remuneration and STI for the unexpired portion of the notice period and statutory entitlements such as accrued annual and long service leave (where applicable) together with superannuation benefits.
Retirement benefit	CEO Other executives	One years fixed remuneration at retirement and statutory entitlements. No specific arrangements in place.
Post-employment restraints	CEO Other executives	Three year non-compete agreement post-retirement. No specific arrangements in place.

Directors' report

FOR THE YEAR ENDED 31 DECEMBER 2009

(J) Total remuneration

The following table provides details of the remuneration of key management personnel of QBE (excluding non-executive directors) paid or payable for services provided for the year to 31 December 2009.

	YEAR	SHORT-TERM EMPLOYEE BENEFITS			POST EMPLOYMENT BENEFITS	OTHER LONG-TERM EMPLOYMENT BENEFITS	SHARE BASED PAYMENTS ⁽¹⁾		TERMINATION BENEFITS	TOTAL
		BASE SALARY \$'000	OTHER ⁽²⁾ \$'000	STI ⁽³⁾ \$'000	SUPER-ANNUATION \$'000	LONG SERVICE LEAVE \$'000	CONDITIONAL RIGHTS \$'000	OPTIONS \$'000	\$'000	\$'000
Executive director										
FM O'Halloran	2009	1,878	458	2,561	268	64	996	387	–	6,612
	2008	1,762	634	2,807	260	140	883	305	–	6,791
Executives										
SP Burns ⁽⁴⁾	2009	1,285	427	2,271	–	–	1,676	591	–	6,250
	2008	1,363	447	2,411	–	–	1,251	486	–	5,958
NG Drabsch	2009	814	242	1,025	119	23	445	182	–	2,850
	2008	785	334	1,123	116	27	423	151	–	2,959
D Fogarty ⁽⁴⁾	2009	629	78	523	111	–	225	77	–	1,643
	2008	595	71	559	106	–	202	60	–	1,593
MJ Goodwin ⁽⁴⁾	2009	529	326	516	63	15	126	31	–	1,606
	2008	512	309	626	59	12	52	19	–	1,589
MD ten Hove	2009	888	265	1,223	90	19	353	110	–	2,948
	2008	851	347	356	99	–	413	152	–	2,218
TW Ibbotson	2009	715	60	684	69	13	279	87	–	1,907
	2008	632	116	894	97	16	212	74	–	2,041
V McLenaghan	2009	938	141	1,280	133	27	649	172	–	3,340
	2008	900	178	1,397	128	30	416	137	–	3,186
BM Nicholls	2009	616	22	525	26	16	269	105	–	1,579
	2008	557	28	564	39	30	296	90	–	1,604
DA Ramsay	2009	619	148	606	91	23	250	98	–	1,835
	2008	594	186	658	88	33	232	80	–	1,871
J Rumppler ^(4,5)	2009	822	121	508	8	10	123	49	–	1,641
	2008	443	46	304	35	1	121	40	–	990
JM Smith	2009	579	9	493	13	5	203	80	–	1,382
	2008	537	8	541	38	8	189	65	–	1,386
GB Thwaites	2009	536	20	479	46	17	172	48	–	1,318
	2008	472	55	508	37	36	120	35	–	1,263
Former key management personnel										
TM Kenny ^(4,6)	2009	–	–	–	–	–	–	–	–	–
	2008	855	69	890	22	–	402	213	2,902	5,353
Total	2009	10,848	2,317	12,694	1,037	232	5,766	2,017	–	34,911
	2008	10,858	2,828	13,638	1,124	333	5,212	1,907	2,902	38,802

(1) The fair value at grant date of options and conditional rights is calculated using a binomial model. The fair value of each option and conditional right is earned evenly over the period between grant and vesting which is three years for conditional rights and three or five years for options. Details of grants of conditional rights and options are provided in note 28 to the financial statements.

(2) "Other" includes the deemed value of the share loans, provision of motor vehicles, health insurance, staff insurance discount benefits received during the year, life assurance and personal accident insurance and the applicable taxes thereon. It includes interest on share loans which is also disclosed in note 28(C) to the financial statements. Directors' and officers' liability insurance has not been included in other remuneration since it is not possible to determine an appropriate allocation basis.

(3) STI is the accrued entitlement for the financial year.

(4) Mr Burns is located in London, Mr Fogarty is located in Dublin, Mr Goodwin is located in Singapore and Messrs Rumppler and Kenny are based in New York. Their remuneration has been converted to Australian dollars using the cumulative average rate of exchange for the relevant year.

(5) Mr Rumppler was appointed as president and chief executive officer, the Americas on 15 June 2009. Before this appointment, he was Group General Manager, Credit and Surety based in Australia. In 2009, Mr Rumppler's total remuneration is shown, whether as key management personnel or otherwise. Amounts received in his position as key management personnel amount to \$1,122,000, comprising: base salary of \$596,000; other short-term employee benefits of \$10,000; superannuation of \$8,000; and STI of \$508,000.

(6) Mr Kenny ceased employment on 12 September 2008.

Directors' report

FOR THE YEAR ENDED 31 DECEMBER 2009

(K) Share based remuneration

(i) Key management personnel – investment in QBE

	ORDINARY SHARES NUMBER	OPTIONS NUMBER	CONDITIONAL RIGHTS NUMBER	TOTAL POTENTIAL SHARES IN QBE AT 31 JAN 2010 NUMBER	VALUE OF POTENTIAL SHARES AT 31 JAN 2010 ⁽¹⁾ \$'000	COST TO ACQUIRE SHARES ⁽²⁾ \$'000	NET INVESTMENT IN QBE AT 31 JAN 2010 \$'000
Executive director							
FM O'Halloran	1,109,173	466,544	138,562	1,714,279	39,291	(15,117)	24,174
Executives							
SP Burns	54,695	597,075	268,892	920,662	21,102	(11,360)	9,742
NG Drabsch	179,439	228,899	66,447	474,785	10,882	(6,570)	4,312
D Fogarty	49,827	95,680	33,997	179,504	4,114	(2,106)	2,008
MJ Goodwin	13,017	52,039	27,909	92,965	2,131	(1,026)	1,105
MD ten Hove	316,261	123,836	46,333	486,430	11,149	(6,753)	4,396
TW Ibbotson	30,787	124,669	45,459	200,915	4,605	(2,497)	2,108
V McLenaghan	202,305	220,104	105,148	527,557	12,092	(5,619)	6,473
BM Nicholls	33,935	123,260	36,886	194,081	4,448	(2,826)	1,622
DA Ramsay	215,952	124,045	37,404	377,401	8,650	(3,958)	4,692
J Rumpfer	58,595	60,727	17,715	137,037	3,141	(1,642)	1,499
JM Smith	21,149	101,341	30,431	152,921	3,505	(2,046)	1,459
GB Thwaites	31,137	62,484	27,162	120,783	2,768	(1,484)	1,284

(1) The closing share price at 31 January 2010 was \$22.92.

(2) Includes the value of share loans and the anticipated future cost of exercising options.

Amounts in the above table include relevant interests but do not include interests attributable to personally related parties.

(ii) Options

DCP options

DCP options affecting remuneration of key management personnel in the previous, current or future reporting periods are as follows:

GRANT DATE	DATE EXERCISABLE	EXPIRY DATE	EXERCISE PRICE	VALUE PER OPTION AT GRANT DATE ⁽¹⁾
3 March 2004	2 March 2007	3 March 2008	\$11.08	\$2.12
3 March 2005	3 March 2008	3 March 2009	\$14.85	\$3.04
3 March 2005	3 March 2010	3 March 2011	\$8.04	\$6.90
3 March 2005	3 March 2010	3 March 2011	\$11.08	\$5.17
3 March 2005	3 March 2010	3 March 2011	\$14.85	\$3.60
8 April 2005	8 April 2010	8 April 2011	\$14.85	\$3.60
2 March 2006	2 March 2009	2 March 2010	\$20.44	\$3.85
2 March 2006	1 March 2011	2 March 2012	\$20.44	\$4.58
7 April 2006	6 April 2011	7 April 2012	\$20.44	\$5.63
2 March 2007	1 March 2010	2 March 2011	\$32.68	\$5.05
2 March 2007	1 March 2012	2 March 2013	\$32.68	\$6.28
4 April 2007	3 April 2012	4 April 2013	\$32.68	\$6.28
4 March 2008	3 March 2011	3 March 2012	\$24.22	\$3.98
4 March 2008	4 March 2013	4 March 2014	\$24.22	\$4.63
4 April 2008	3 April 2013	4 April 2014	\$27.00	\$5.16
6 March 2009	5 March 2012	6 March 2013	\$17.57	\$2.36
6 March 2009	5 March 2014	6 March 2015	\$17.57	\$2.81

(1) The fair value at grant date of DCP options is calculated using a binomial model. The fair value of each option is earned evenly over the three or five year period between grant and vesting.

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(K) Share based remuneration continued

Details of DCP options over the ordinary shares in the company provided as remuneration to the key management personnel are set out below. When exercisable, each option is convertible into one ordinary share of the company. The options granted in March 2009 were earned under the DCP terms for the 2008 performance year.

	NUMBER OF OPTIONS GRANTED IN THE YEAR		NUMBER OF OPTIONS VESTED IN THE YEAR		NUMBER OF OPTIONS EXERCISED IN THE YEAR	
	2009	2008	2009	2008	2009	2008
Executive director						
FM O'Halloran	127,804	74,257	-	-	-	-
Executives						
SP Burns	125,307	76,700	-	-	-	-
NG Drabsch	51,144	35,169	-	-	-	-
D Fogarty	28,839	16,605	-	-	-	-
MJ Goodwin	29,028	7,934	-	-	-	-
MD ten Hove	16,222	37,161	46,799 ⁽¹⁾	66,707	-	66,707 ⁽²⁾
TW Ibbotson	40,696	19,187	-	-	-	-
V McLenaghan	63,589	42,835	-	-	-	-
BM Nicholls	25,681	15,525	-	-	-	-
DA Ramsay	29,962	19,872	-	-	-	-
J Rumppler	13,835	10,489	-	-	-	-
JM Smith	24,611	16,146	-	-	-	-
GB Thwaites	23,113	14,516	-	-	-	-
Former key management personnel						
TM Kenny ⁽⁵⁾	-	51,941	228,587 ⁽³⁾	-	144,736 ⁽⁴⁾	-

(1) Options are exercisable at \$20.44 per option.

(2) Options exercised at \$14.85 per option.

(3) Mr Kenny ceased employment on 12 September 2008. All DCP options granted up to 12 September 2008 and unvested at 31 December 2008 vested and became exercisable on 31 March 2009.

(4) Mr Kenny exercised 75,750 options at \$14.85 per option and 68,986 options at \$20.44 per option.

(5) Mr Kenny exercised a further 51,941 options at \$24.22 per option on 4 January 2010.

Future performance options

Future performance options that affect remuneration of the key management personnel in the previous, current or future reporting periods are as follows:

NAME	GRANT DATE	NUMBER OF OPTIONS GRANTED	EXERCISE PRICE	VALUE PER RIGHT AT GRANT DATE ⁽¹⁾
SP Burns	2 March 2007	20,000	\$20.44	\$12.55
SP Burns	4 March 2008	20,000	\$20.44	\$3.36
SP Burns	6 March 2009	20,000	\$20.44	\$2.77

(1) The fair value at grant date of options is calculated using a binomial model. The fair value of each option is earned evenly over the period between grant and vesting.

(2) All options are exercisable within three months of 31 December 2010 and expire on 1 April 2011. The vesting of these options is subject to European operations achieving an average insurance profit of at least 8% for underwriting years 2006 to 2010.

Mr Kenny ceased employment on 12 September 2008. 100,000 future performance options granted up to 12 September 2008 and unvested at 31 December 2008 vested and became exercisable on 31 March 2009. During 2009, Mr Kenny exercised 60,000 options at \$14.81 per option and 40,000 options at \$20.44 per option.

Directors' report

FOR THE YEAR ENDED 31 DECEMBER 2009

(K) Share based remuneration continued

(iii) Conditional rights

Details of conditional rights issued under both the DCP and the GERSP affecting remuneration of key management personnel in the previous, current or future reporting periods are as follows:

GRANT DATE	DATE EXERCISABLE	VALUE PER RIGHT AT GRANT DATE ⁽¹⁾
3 March 2005	3 March 2008	\$15.30 to \$17.81
8 April 2005	7 April 2008	\$16.94
2 March 2006	2 March 2009	\$23.09
7 April 2006	6 April 2009	\$24.23
2 March 2007	1 March 2010	\$32.68
4 April 2007	2 April 2010	\$32.68
4 March 2008	3 March 2011	\$24.22
4 April 2008	4 April 2011	\$27.00
1 January 2009	2 January 2012	\$25.37
6 March 2009	5 March 2012	\$17.57

(1) The fair value at grant date of conditional rights is calculated using a binomial model. The fair value of each conditional right is earned evenly over the period between grant and vesting.

Details of conditional rights to ordinary shares in the company provided as remuneration to the key management personnel are set out below. When exercisable, each conditional right is convertible into one ordinary share of the company.

	NUMBER OF RIGHTS GRANTED IN THE YEAR		NUMBER OF RIGHTS VESTED IN THE YEAR	
	2009	2008	2009	2008
Executive director				
FM O'Halloran	63,902	37,128	41,182	50,142
Executives				
SP Burns	132,272	80,963	47,006	68,469
NG Drabsch	29,943	17,585	21,462	28,199
D Fogarty	16,261	8,302	11,025	5,030
MJ Goodwin	20,261	3,967	884	4,201
MD ten Hove	10,706	18,581	19,904	27,930
TW Ibbotson	25,720	9,594	10,604	11,627
V McLenaghan	61,356	21,417	16,648	20,302
BM Nicholls	14,480	7,763	17,594	8,021
DA Ramsay	16,893	9,936	11,475	13,995
J Rumpler	6,917	5,245	5,831	6,372
JM Smith	13,877	8,073	9,597	11,308
GB Thwaites	13,032	7,258	3,184	3,695
Former key management personnel				
TM Kenny ⁽¹⁾	–	25,970	77,282	31,718

(1) Mr Kenny ceased employment on 12 September 2008. All conditional rights granted up to 12 September 2008 and unvested at 31 December 2008 vested and became exercisable on 31 March 2009.

Directors' report

FOR THE YEAR ENDED 31 DECEMBER 2009

(L) Non-executive director remuneration

(i) Remuneration philosophy

Non-executive director remuneration reflects QBE's desire to attract, motivate and retain high quality directors and to ensure their active participation in the consolidated entity's affairs for the purposes of corporate governance, regulatory compliance and other matters. QBE aims to provide a level of remuneration for non-executive directors comparable with its peers, which include multinational financial institutions. The board reviews surveys published by independent remuneration consultants and other public information to ensure that fee levels are appropriate. The remuneration arrangements of non-executive directors are distinct and separate from the Group's chief executive officer and other executives.

(ii) Non-executive directors' fee pool

The aggregate amount approved by shareholders at the 2007 AGM was \$2,700,000 per annum.

(iii) Fee framework

Under the current fee framework, non-executive directors receive a base fee. In addition, a non-executive director (other than the chairman) may receive further fees for membership or chairmanship of a board committee. Future fees may be sacrificed into the QBE non-executive directors' share plan. The following table details the relevant annual fees:

	2009 \$'000	2008 \$'000
Base fees		
Chairman	603	585
Non-executive director	194	188
Committee chairman fees		
Audit committee	45	44
Chairman's committee	-	-
Funding committee	-	-
Investment committee	31	30
Remuneration committee	31	30
Committee membership fees		
Audit committee	24	23
Chairman's committee	-	-
Funding committee	-	-
Investment committee	22	21
Remuneration committee	22	21

The directors have resolved not to increase directors' fees for 2010.

Directors' report

FOR THE YEAR ENDED 31 DECEMBER 2009

(L) Non-executive director remuneration continued

(iv) Remuneration

Details of the nature and amount of each component of the remuneration of our non-executive directors for the year ended 31 December 2009 are set out in the table below.

	YEAR	SHORT-TERM EMPLOYEE BENEFITS		POST EMPLOYMENT BENEFITS		TOTAL
		DIRECTORS' FEES \$'000	OTHER ⁽²⁾ \$'000	SUPERANNUATION \$'000	RETIREMENT BENEFITS \$'000	\$'000
LF Bleasel AM	2009	248	–	22	5	275
	2008	241	–	22	7	270
DM Boyle	2009	239	1	21	–	261
	2008	232	1	21	–	254
EJ Cloney AM	2009	603	5	54	26	688
	2008	585	4	53	30	672
IF Hudson ⁽¹⁾	2009	304	–	–	–	304
	2008	296	–	–	–	296
BJ Hutchinson AM	2009	248	–	22	13	283
	2008	241	–	22	15	278
CLA Irby ⁽¹⁾	2009	304	–	–	5	309
	2008	296	–	–	6	302
IYL Lee	2009	261	–	23	4	288
	2008	253	–	23	4	280
Total	2009	2,207	6	142	53	2,408
	2008	2,144	5	141	62	2,352

(1) Mr Irby and Ms Hudson are UK residents. They each receive an annual travel allowance of \$40,000 and, in lieu of superannuation, additional fees of 9%, both of which are included in directors' fees.

(2) Staff insurance discount benefits received during the year.

Directors' report

FOR THE YEAR ENDED 31 DECEMBER 2009

(L) Non-executive director remuneration continued

(v) Other benefits

Non-executive directors do not receive any performance-based remuneration such as cash incentives or equity awards. Under the company's constitution, non-executive directors are entitled to be reimbursed for all travel and related expenses properly incurred in connection with the business of the company. Non-executive directors based overseas receive an annual cash travel allowance in addition to fees.

(vi) Superannuation

QBE pays superannuation of 9% to Australian non-executive directors. Non-executive directors based overseas receive the cash equivalent amount as fees.

(vii) Other retirement benefits

Non-executive directors previously received a retirement allowance based on their period of service. The allowance was limited to the aggregate of the director's fees in the last three years of service, subject to a minimum of 10 years service. Where service was less than 10 years, a pro-rata amount was paid. With effect from 31 December 2003, the board terminated the retirement allowance to non-executive directors. Accrued retirement benefits at 31 December 2003 are preserved until retirement and are subject to an annual increase equal to the average five year Australian government bond rate. Shareholders approved an increase in non-executive directors' remuneration and the company's constitution was amended at the 2004 AGM to recognise this change.

The following table sets out the preserved retirement allowances of the relevant non-executive directors at the balance date:

	RETIREMENT ALLOWANCE	
	2009 \$'000	2008 \$'000
LF Bleasel AM	131	126
EJ Cloney AM	576	550
BJ Hutchinson AM	295	282
CLA Irby	116	111
IYL Lee	84	80

Directors' report

FOR THE YEAR ENDED 31 DECEMBER 2009

AUDITOR

PricewaterhouseCoopers, Chartered Accountants, continues in office in accordance with section 327B of the *Corporations Act 2001*.

NON-AUDIT SERVICES

During the year PricewaterhouseCoopers has performed certain other services in addition to its statutory duties.

The board of directors has considered the position and, in accordance with the advice received from the audit committee, is satisfied that the provision of the non-audit services is compatible with the general standard of independence for auditors imposed by the *Corporations Act 2001*. The directors are satisfied that the provision of non-audit services by the auditor, as provided in note 30 to the financial statements, did not compromise the auditor independence requirements of the *Corporations Act 2001* for the following reasons:

- all non-audit services have been reviewed by the audit committee to ensure that they do not impact the impartiality and objectivity of the auditor; and
- none of the services undermine the general principles relating to auditor independence as set out in APES 110: Code of Ethics for Professional Accountants.


A copy of the auditor's independence declaration required under section 307C of the *Corporations Act 2001* is set out on page 78.

Details of amounts paid or payable to PricewaterhouseCoopers for audit and non-audit services are provided in note 30 to the financial statements.

ROUNDING OF AMOUNTS

The company is of a kind referred to in the ASIC class order 98/0100 dated 10 July 1998 (as amended by class order 04/667 dated 15 July 2004) relating to the "rounding off" of amounts in the directors' report. Amounts have been rounded off in the directors' report to the nearest million dollars or, in certain cases, to the nearest thousand dollars in accordance with that class order.

Signed in SYDNEY this 26th day of February 2010 in accordance with a resolution of the directors.



EJ Cloney AM
Director



FM O'Halloran
Director

Directors' report

FOR THE YEAR ENDED 31 DECEMBER 2009

Auditor's independence declaration for the year ended 31 December 2009

As lead auditor for the audit of QBE Insurance Group Limited for the year ended 31 December 2009, I declare that, to the best of my knowledge and belief, there have been:

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

This declaration is in respect of QBE Insurance Group Limited and the entities it controlled during the period.



KG Smith

Partner
PricewaterhouseCoopers

Sydney
26 February 2010

Annual financial report

31 DECEMBER 2009

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This financial report includes separate financial statements for QBE Insurance Group Limited ("the company") as an individual entity and the consolidated entity consisting of QBE Insurance Group Limited and its controlled entities. The financial report is presented in Australian dollars.

QBE Insurance Group Limited is a company limited by shares, incorporated and domiciled in Australia. Its registered office is located at:

Level 2, 82 Pitt Street
Sydney NSW 2000 Australia

A description of the nature of the consolidated entity's operations and its principal activities is included in the operations overview on pages 24 to 41 and in the directors' report, neither of which is part of this financial report.

The financial report was authorised for issue by the directors on 26 February 2010.

Through the use of the internet, we have ensured that our corporate reporting is timely, complete and available globally at minimum cost to the company. All material press releases, financial reports and other information are available at our QBE investor centre on our website: www.qbe.com.

Balance sheets

AS AT 31 DECEMBER 2009

	NOTE	THE COMPANY		CONSOLIDATED	
		2009 \$M	2008 \$M	2009 \$M	2008 \$M
ASSETS					
Financial assets at fair value through profit or loss					
Cash and cash equivalents	10	17	641	1,601	2,736
Investments	11	248	770	23,420	25,693
ABC financial assets pledged for funds at Lloyd's	34	-	-	-	250
Derivative financial instruments	12	21	4	150	867
Swaps relating to ABC securities	34	-	-	-	67
Trade and other receivables	13	1,236	3,092	4,300	5,041
Reinsurance and other recoveries on outstanding claims	22	-	-	3,683	5,043
Current tax assets		-	-	140	78
Other assets		3	6	42	83
Deferred insurance costs	14	-	-	1,955	1,987
Defined benefit plan surplus	29	-	-	2	2
Property, plant and equipment	15	-	-	384	505
Deferred tax assets	16	-	27	203	333
Investment properties	17	-	-	70	112
Shares in controlled entities	18	14,334	11,340	-	-
Intangible assets	19	-	-	5,014	5,586
Total assets		15,859	15,880	40,964	48,383
LIABILITIES					
Financial liabilities at fair value through profit or loss					
Derivative financial instruments	12	13	209	40	1,119
Swaps relating to ABC securities	34	-	1	-	-
Trade and other payables	20	3,023	2,682	1,314	1,994
Current tax liabilities		67	275	211	324
Unearned premium	21	-	-	6,835	7,126
ABC securities for funds at Lloyd's	34	-	-	-	312
Outstanding claims	22	-	-	18,033	21,204
Provisions	23	-	-	598	714
Defined benefit plan deficit	29	-	-	120	148
Deferred tax liabilities	16	21	-	544	531
Borrowings	24	1,833	1,907	2,971	3,666
Total liabilities		4,957	5,074	30,666	37,138
Net assets		10,902	10,806	10,298	11,245
EQUITY					
Share capital	25(A)	7,366	6,714	7,366	6,714
Share capital, fully paid yet to be issued	25(B)	-	115	-	115
Treasury shares held in trust	25(C)	-	-	(1)	(1)
Equity component of hybrid securities	25(D)	114	114	114	114
Reserves	26	61	52	(2,374)	(178)
Retained profits		3,361	3,811	5,117	4,395
Shareholders' funds		10,902	10,806	10,222	11,159
Minority interests	18(D)	-	-	76	86
Total equity		10,902	10,806	10,298	11,245

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

Income statements

FOR THE YEAR ENDED 31 DECEMBER 2009

	NOTE	THE COMPANY		CONSOLIDATED	
		2009 \$M	2008 \$M	2009 \$M	2008 \$M
REVENUE					
Premium revenue		–	–	14,074	12,853
Other revenue		1,022	1,481	1,943	2,866
Net fair value gains on financial assets		–	24	460	–
Realised gains on sale of controlled entities		–	1	8	–
Investment income – ABC financial assets pledged for funds at Lloyd's		68	96	130	222
	6	1,090	1,602	16,615	15,941
EXPENSES					
Outward reinsurance premium expense		–	–	1,925	1,766
Gross claims incurred		–	–	8,157	7,743
Other expenses	7(C)	5	31	3,695	3,494
Net fair value losses on financial assets		13	–	–	33
Net fair value losses on investment properties		–	–	21	–
Net fair value losses on owner occupied properties		–	–	29	–
Impairment of investment in controlled entities		15	2,410	–	–
Expenses – ABC securities for funds at Lloyd's		56	111	137	245
Finance costs		164	98	219	240
Profit (loss) before income tax	7	837	(1,048)	2,432	2,420
Income tax expense	8	50	22	448	554
Profit (loss) after income tax		787	(1,070)	1,984	1,866
Net profit attributable to minority interests		–	–	14	7
Net profit (loss) after income tax attributable to ordinary equity holders of the company		787	(1,070)	1,970	1,859

Earnings per share for net profit after income tax attributable to ordinary equity holders of the company	NOTE	CONSOLIDATED	
		2009 CENTS	2008 CENTS
Basic earnings per share	36	196.5	208.8
Diluted earnings per share	36	192.8	205.5

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

Statements of comprehensive income

FOR THE YEAR ENDED 31 DECEMBER 2009

	NOTE	THE COMPANY		CONSOLIDATED	
		2009 \$M	2008 \$M	2009 \$M	2008 \$M
Profit (loss) after income tax		787	(1,070)	1,984	1,866
Net movement in foreign currency translation reserve	26	-	-	(2,206)	(118)
Actuarial losses on defined benefit superannuation plans	29(C)	-	-	(13)	(118)
Cash flow hedges	26	(12)	6	(6)	18
(Losses) gains on revaluation of owner occupied properties	26	-	-	(8)	(10)
Employee share options	26	21	7	21	7
Income tax relating to components of other comprehensive income		-	-	5	36
Other comprehensive income for the year, net of tax		9	13	(2,207)	(185)
Total comprehensive income for the year		796	(1,057)	(223)	1,681
Attributable to:					
Ordinary equity holders of the company		796	(1,057)	(237)	1,674
Minority interests		-	-	14	7
		796	(1,057)	(223)	1,681

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

Statements of changes in equity

FOR THE YEAR ENDED 31 DECEMBER 2009

CONSOLIDATED	SHARE CAPITAL \$M	TREASURY SHARES HELD IN TRUST \$M	EQUITY COMPONENT OF HYBRID SECURITIES \$M	RESERVES \$M	RETAINED PROFITS \$M	SHAREHOLDERS' FUNDS \$M	MINORITY INTERESTS \$M	TOTAL EQUITY \$M
As at 1 January 2009	6,829	(1)	114	(178)	4,395	11,159	86	11,245
Profit for the year	-	-	-	-	1,970	1,970	14	1,984
Other comprehensive income	-	-	-	(2,196)	(11)	(2,207)	-	(2,207)
Total comprehensive income	-	-	-	(2,196)	1,959	(237)	14	(223)
Transactions with owners in their capacity as owners								
Purchase of shares	-	(19)	-	-	-	(19)	-	(19)
Shares vested and/or released to participants	-	19	-	-	-	19	-	19
Contributions of equity, net of transaction costs and tax	537	-	-	-	-	537	-	537
Dividends paid on ordinary shares	-	-	-	-	(1,273)	(1,273)	-	(1,273)
Dividend reinvestment under Bonus Share Plan	-	-	-	-	36	36	-	36
Minority interests movement	-	-	-	-	-	-	(24)	(24)
As at 31 December 2009	7,366	(1)	114	(2,374)	5,117	10,222	76	10,298

CONSOLIDATED	SHARE CAPITAL \$M	TREASURY SHARES HELD IN TRUST \$M	EQUITY COMPONENT OF HYBRID SECURITIES \$M	RESERVES \$M	RETAINED PROFITS \$M	SHAREHOLDERS' FUNDS \$M	MINORITY INTERESTS \$M	TOTAL EQUITY \$M
As at 1 January 2008	4,737	(16)	114	(75)	3,719	8,479	64	8,543
Profit for the year	-	-	-	-	1,859	1,859	7	1,866
Other comprehensive income	-	-	-	(103)	(82)	(185)	-	(185)
Total comprehensive income	-	-	-	(103)	1,777	1,674	7	1,681
Transactions with owners in their capacity as owners								
Purchase of shares	-	(10)	-	-	-	(10)	-	(10)
Shares vested and/or released to participants	-	25	-	-	-	25	-	25
Contributions of equity, net of transaction costs and tax	2,092	-	-	-	-	2,092	-	2,092
Dividends paid on ordinary shares	-	-	-	-	(1,118)	(1,118)	-	(1,118)
Dividend reinvestment under Bonus Share Plan	-	-	-	-	55	55	-	55
Deferred tax adjustment	-	-	-	-	(38)	(38)	-	(38)
Minority interests movement	-	-	-	-	-	-	15	15
As at 31 December 2008	6,829	(1)	114	(178)	4,395	11,159	86	11,245

Statements of changes in equity

FOR THE YEAR ENDED 31 DECEMBER 2009

COMPANY	SHARE CAPITAL \$M	EQUITY COMPONENT OF HYBRID SECURITIES \$M	RESERVES \$M	RETAINED PROFITS \$M	SHAREHOLDERS' FUNDS \$M	MINORITY INTERESTS \$M	TOTAL EQUITY \$M
As at 1 January 2009	6,829	114	52	3,811	10,806	-	10,806
Profit for the year	-	-	-	787	787	-	787
Other comprehensive income	-	-	9	-	9	-	9
Total comprehensive income	-	-	9	787	796	-	796
Transactions with owners in their capacity as owners							
Contributions of equity, net of transaction costs and tax	537	-	-	-	537	-	537
Dividends paid on ordinary shares	-	-	-	(1,273)	(1,273)	-	(1,273)
Dividend reinvestment under Bonus Share Plan	-	-	-	36	36	-	36
As at 31 December 2009	7,366	114	61	3,361	10,902	-	10,902

COMPANY	SHARE CAPITAL \$M	EQUITY COMPONENT OF HYBRID SECURITIES \$M	RESERVES \$M	RETAINED PROFITS \$M	SHAREHOLDERS' FUNDS \$M	MINORITY INTERESTS \$M	TOTAL EQUITY \$M
As at 1 January 2008	4,737	114	39	5,944	10,834	-	10,834
Loss for the year	-	-	-	(1,070)	(1,070)	-	(1,070)
Other comprehensive income	-	-	13	-	13	-	13
Total comprehensive income	-	-	13	(1,070)	(1,057)	-	(1,057)
Transactions with owners in their capacity as owners							
Contributions of equity, net of transaction costs and tax	2,092	-	-	-	2,092	-	2,092
Dividends paid on ordinary shares	-	-	-	(1,118)	(1,118)	-	(1,118)
Dividend reinvestment under Bonus Share Plan	-	-	-	55	55	-	55
As at 31 December 2008	6,829	114	52	3,811	10,806	-	10,806

Statements of cash flows

FOR THE YEAR ENDED 31 DECEMBER 2009

	NOTE	THE COMPANY		CONSOLIDATED	
		2009 \$M	2008 \$M	2009 \$M	2008 \$M
OPERATING ACTIVITIES					
Premium received		-	-	14,333	13,098
Reinsurance and other recoveries received		-	-	1,405	1,396
Outward reinsurance paid		-	-	(1,977)	(1,691)
Claims paid		-	-	(8,434)	(7,651)
Insurance costs paid		-	-	(2,617)	(2,700)
Other underwriting costs		-	-	(907)	(928)
Interest received		11	57	673	1,133
Dividends received		-	-	51	66
Other operating income		-	249	30	14
Other operating payments		(463)	-	(125)	(58)
Interest paid		(107)	(116)	(155)	(161)
Income taxes paid		(40)	(64)	(369)	(267)
Net cash flows from operating activities	38	(599)	126	1,908	2,251
INVESTING ACTIVITIES					
Proceeds on sale of equity investments		-	-	977	1,015
Proceeds on sale of investment property		-	-	-	2
Proceeds on sale of property, plant and equipment		-	-	8	7
Payments for purchase of equity investments		-	-	(993)	(1,408)
(Payments for) proceeds from foreign exchange transactions		-	-	(790)	(493)
(Payments for) proceeds from purchase of other financial assets		(200)	(4)	(867)	1,734
Payments for purchase of controlled entities and businesses acquired ⁽¹⁾		-	-	(120)	(2,371)
Proceeds on disposal of controlled entities		-	1	14	-
Payments for purchase of investment property		-	-	(1)	-
Payments for purchase of property, plant and equipment		-	-	(69)	(71)
Net cash flows from investing activities		(200)	(3)	(1,841)	(1,585)
FINANCING ACTIVITIES					
Proceeds from (payments to) controlled entities		977	(825)	-	-
Proceeds from issue of shares		-	2,115	-	2,115
(Refund of) proceeds from over-subscribed portion of share issue		(112)	112	(112)	112
Payments for purchase of treasury shares		-	-	(19)	(10)
Share issue expenses		(4)	(32)	(4)	(32)
Proceeds from settlement of staff share loans		-	-	14	11
Proceeds from borrowings		1,001	400	1,200	400
Repayment of borrowings		(833)	(200)	(1,125)	(222)
Repayment of ABC securities		-	-	-	(656)
Dividends paid		(847)	(1,063)	(854)	(1,068)
Net cash flows from financing activities		182	507	(900)	650
NET MOVEMENT IN CASH AND CASH EQUIVALENTS					
Cash and cash equivalents at the beginning of the financial year		641	11	2,736	988
Effect of exchange rate changes		(7)	-	(302)	432
Cash and cash equivalents at the end of the financial year	10	17	641	1,601	2,736

(1) Net of cash acquired.

The above statements of cash flows should be read in conjunction with the accompanying notes.

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Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies adopted in the preparation of the financial report are set out below. These policies have been consistently applied to all the years presented unless otherwise stated. The financial report includes separate financial statements for QBE Insurance Group Limited ("the company") as an individual entity and the consolidated financial statements for the company and its controlled entities ("the consolidated entity").

(A) Basis of preparation

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

Compliance with IFRS

The financial report also complies with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board.

Historical cost convention

These financial statements have been prepared under the historical cost convention, as modified by certain exceptions noted in the financial report, with the principal exceptions for the consolidated entity being the measurement of financial assets at fair value and the measurement of the outstanding claims liability and related reinsurance and other recoveries at present value.

(B) Principles of consolidation

The consolidated financial statements incorporate the assets and liabilities of all entities controlled by the company as at 31 December 2009 and the results of all controlled entities for the financial year then ended. The effects of all transactions between entities in the consolidated entity are eliminated in full. Minority interest in the results and equity of controlled entities is shown separately in the consolidated income statement and balance sheet.

Where control of an entity commences during a financial year, its results are included in the consolidated income statement from the date on which the control commences. Where control of an entity ceases during a financial year, its results are included for that part of the year during which the control existed.

The purchase method of accounting is used to account for the acquisition of controlled entities by the consolidated entity. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the consolidated entity's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the controlled entity acquired, the difference is recognised directly in the income statement.

(C) Premium revenue

Premium comprises amounts charged to policyholders, excluding taxes collected on behalf of third parties. The earned portion of premium received and receivable, including unclosed business, is recognised as revenue. Premium on unclosed business is brought to account based upon the pattern of booking of renewals and new business.

(D) Unearned premium

Unearned premium is calculated based on the term of the risk which closely approximates the pattern of risks underwritten using either the daily pro-rata method or the 24ths method.

At each balance sheet date, the adequacy of the unearned premium liability is assessed on a net of reinsurance basis against the present value of the expected future cash flows relating to potential future claims in respect of the relevant insurance contracts, plus an additional risk margin to reflect the inherent uncertainty of the central estimate. The assessment is carried out at the divisional business segment level, being a portfolio of contracts that are broadly similar and managed together as a single portfolio. If the unearned premium liability, less related intangible assets and deferred acquisition costs, is deficient, then the resulting deficiency is recognised in the income statement of the consolidated entity.

(E) Outward reinsurance

Premium ceded to reinsurers is recognised as an expense in accordance with the pattern of reinsurance service received. Accordingly, a portion of outward reinsurance premium is treated as a prepayment at the balance sheet date.

(F) Claims

The provision for outstanding claims is measured as the central estimate of the present value of expected future claims payments plus a risk margin. The expected future payments include those in relation to claims reported but not yet paid; claims incurred but not reported ("IBNR"); claims incurred but not enough reported ("IBNER"); and estimated claims handling costs. Claims expense represents claim payments adjusted for the movement in the outstanding claims liability.

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

A risk margin is applied to the central estimate, net of reinsurance and other recoveries, to reflect the inherent uncertainty in the central estimate.

(G) Reinsurance and other recoveries

Reinsurance and other recoveries on paid claims, reported claims not yet paid, IBNR and IBNER are recognised as revenue.

Amounts recoverable are assessed in a manner similar to the assessment of outstanding claims. Recoveries are measured as the present value of the expected future receipts, calculated on the same basis as the provision for outstanding claims.

(H) Acquisition costs

A portion of acquisition costs relating to unearned premium is deferred in recognition that it represents a future benefit. Deferred acquisition costs are measured at the lower of cost and recoverable amount. Deferred acquisition costs are amortised on a straight line basis over the financial years expected to benefit from the expenditure.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

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SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

(I) Investment income

Interest income is recognised on an accruals basis. Dividends are recognised when the right to receive payment is established. Investment income includes realised and unrealised gains or losses on financial assets which are reported on a combined basis as fair value gains or losses on financial assets.

Investment income on ABC financial assets pledged for funds at Lloyd's and expenses relating to ABC securities for funds at Lloyd's, both of which are separately identified, include fair value gains and losses on the ABC swaps.

(J) Taxation

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

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

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

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

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

The company and all of its Australian wholly-owned controlled entities ("Australian entities") have implemented the tax consolidation legislation. The company is the head entity in a tax-consolidated group comprising the company and the Australian entities. All entities in the tax-consolidated group continue to account for their own current and deferred tax amounts. These tax amounts are measured as if each entity continues to be a stand-alone tax payer in its own right. In addition to its own current and deferred tax amounts, the company also recognises any current tax or deferred tax arising from unused tax losses and unused tax credits assumed from controlled entities in the tax-consolidated group. Details of the tax funding agreement are included in note 8 to the financial statements.

(K) Policyholders' and shareholders' funds

Policyholders' funds are those financial assets which are held to fund the insurance provisions of the consolidated entity. The remaining financial assets and investment properties (refer note 1(S))

represent shareholders' funds. Insurance profit is derived by adding investment income on policyholders' funds to the underwriting result.

(L) Cash and cash equivalents

Cash and cash equivalents includes cash at bank and on hand and deposits at call which are readily convertible to cash on hand and which are used in the cash management function on a day to day basis.

(M) Investments

All investments are designated as fair value through profit or loss on initial recognition. They are initially recorded at fair value and are subsequently remeasured to fair value at each reporting date. The policy of management is to designate a group of financial assets or financial liabilities as fair value through profit or loss when that group is both managed and its performance evaluated on a fair value basis for both internal and external reporting in accordance with the consolidated entity's documented investment strategy.

For securities traded in an active market, the fair value is determined by reference to published closing bid price quotations. For securities that are not traded and securities that are traded in a market that is not active, fair value is determined using valuation techniques generally by reference to the fair value of recent arm's length transactions involving the same or similar instruments. Fixed and floating rate securities are valued using independently sourced valuations that do not involve the exercise of judgment by management. Discounted cash flow analysis or option pricing models are used for a small number of investments.

All purchases and sales of investments that require delivery of the asset within the time frame established by regulation or market convention ("regular way" transactions) are recognised at trade date, being the date on which the consolidated entity commits to buy or sell the asset.

Investments are derecognised when the right to receive future cash flows from the asset has expired or has been transferred and the consolidated entity has transferred substantially all the risks and rewards of ownership.

(N) Derivative financial instruments

The consolidated entity is subject to currency, interest rate, price, credit and liquidity risks. Derivative financial instruments ("derivatives") are used to manage these risks. The consolidated entity does not enter into, issue or hold derivatives for speculative trading purposes.

Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently remeasured to their fair value. The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument and the nature of the item being hedged. Derivatives which are not part of a hedging relationship are valued at fair value through profit or loss. Derivatives which are part of a hedging relationship are accounted for as set out in note 1(O).

For derivatives traded in an active market, the fair value of derivatives presented as assets is determined by reference to published closing bid price quotations and the fair value of derivatives presented as liabilities is determined by reference to published closing ask price quotations. For derivatives that are not traded or which are traded in a market that is not sufficiently active, fair value is determined using generally accepted valuation techniques, including the use of forward exchange rates for the valuation of forward foreign exchange contracts.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

(O) Hedging transactions

Derivatives held for risk management purposes which meet the criteria specified in AASB 139: Financial Instruments: Recognition and Measurement ("AASB 139") are accounted for by the consolidated entity using fair value hedge accounting, cash flow hedge accounting or hedging of a net investment in a foreign operation as appropriate to the risks being hedged.

When a financial instrument is designated as a hedge, the consolidated entity formally documents the relationship between the hedging instrument and hedged item as well as its risk management objectives and its strategy for undertaking the various hedging transactions. The consolidated entity also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used for hedging are highly effective in offsetting changes in fair values or cash flows of hedged items.

Hedge accounting is discontinued when:

- it is determined that a derivative is not, or has ceased to be, highly effective as a hedge;
- the derivative expires or is sold, terminated or exercised; or
- the hedged item matures, is sold or repaid.

(i) Fair value hedge accounting

Changes in the fair value of derivatives that qualify and are designated as fair value hedges are recorded in the income statement, together with changes in the fair value of the hedged asset or liability that are attributable to the hedged risk. If the hedge no longer meets the criteria for hedge accounting, the fair value hedging adjustment cumulatively made to the carrying value of the hedged item is, for items carried at amortised cost, amortised over the period to maturity of the previously designated hedge relationship using the effective interest method. If the hedged item is sold or repaid, the unamortised fair value adjustment is recognised immediately in the income statement.

(ii) Cash flow hedge accounting

For qualifying cash flow hedges, the fair value gain or loss associated with the effective portion of the cash flow hedge is recognised initially directly in shareholders' equity and transferred to the income statement in the period when the hedged item will affect profit or loss. The gain or loss on any ineffective portion of the hedging instrument is recognised in the income statement immediately. When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the hedged item affects the income statement. When a transaction is no longer expected to occur, the cumulative gain or loss that was recognised in equity is immediately transferred to the income statement.

(iii) Hedges of net investments in foreign operations

Hedges of net investments in foreign operations are accounted for in a manner similar to cash flow hedges. The gain or loss on the effective portion of the hedging instrument is recognised directly in equity and the gain or loss on the ineffective portion is recognised immediately in the income statement. The cumulative gain or loss previously recognised in equity is recognised in the income statement on the disposal or partial disposal of the foreign operation.

(P) Receivables

Receivables are measured at fair value through profit or loss. A provision for impairment is established when there is objective evidence that the consolidated entity will not be able to collect all

amounts due according to the original term of the receivable. Any increase or decrease in the provision for impairment is recognised in the income statement within underwriting expenses. When a receivable is uncollectible, it is written off against the provision for impairment account. Subsequent recoveries of amounts previously written off are credited against underwriting expenses in the income statement.

(Q) Borrowings

Borrowings are initially measured at fair value and are subsequently measured at amortised cost. Any difference between the proceeds and the redemption amount is recognised in the income statement over the period of the financial liability using the effective interest method.

On issue of hybrid securities, the fair value of the liability component, being the obligation to make future payments of principal and interest to investors, is calculated using a market interest rate for an equivalent non-convertible note. The residual amount, representing the fair value of the conversion option, is included in equity with no recognition of any change in the value of the option in subsequent periods. The liability is included in borrowings and carried on an amortised cost basis with interest on the securities recognised as financing costs using the effective interest method until the liability is extinguished on conversion or maturity of the securities.

(R) Asset Backed Capital ("ABC") transactions

(i) ABC financial assets pledged for funds at Lloyd's

ABC financial assets pledged for funds at Lloyd's are managed and performance is evaluated on a fair value basis for both internal and external reporting in accordance with the consolidated entity's documented investment strategy. ABC financial assets are initially recorded at fair value and are subsequently remeasured to fair value at each reporting date.

(ii) ABC securities for funds at Lloyd's

ABC securities are initially measured at fair value and are subsequently measured at amortised cost. Any difference between the proceeds and the redemption amount is recognised in the income statement over the period of the financial liability using the effective interest method.

(iii) Swaps relating to ABC securities

Swaps relating to ABC securities are initially recognised at fair value on the date the agreements are entered into and are subsequently remeasured to their fair value. The method of recognising the resulting gain or loss depends on whether the swap is designated as a hedging instrument and the nature of the item being hedged. Swaps which are not part of a hedging relationship are valued at fair value through profit or loss. Swaps which are part of a hedging relationship are accounted for as set out in note 1(O).

(S) Investment properties

Investment properties are valued by reference to external market valuations at fair value through profit or loss.

(T) Property, plant and equipment

Owner occupied properties are measured at fair value by reference to external market valuations. When a revaluation increases the carrying value of a property, the increase is credited to the revaluation reserve in equity. To the extent that the increase reverses

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

1

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

a decrease previously recognised in the income statement, the increase is first recognised in the income statement. When an asset's carrying amount is decreased as a result of a revaluation, the decrease is recognised in the income statement. To the extent that the decrease reverses an increase previously recognised in equity, the decrease is first recognised in equity.

All other plant and equipment is stated at historical cost less accumulated depreciation.

Leasehold improvements, office equipment, fixtures and fittings and motor vehicles are depreciated using the straight line method over the estimated useful life to the consolidated entity of each class of asset. Estimated useful lives are between three and 10 years for all classes.

An asset's carrying amount is written down to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. Refer note 1(V).

(U) Intangible assets

(i) Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the consolidated entity's share of the net identifiable assets acquired. Goodwill acquired in a business combination is tested for impairment and is not subject to amortisation.

(ii) Intangible assets

Intangible assets are measured at cost. Those with a finite useful life are amortised using the straight line method over the estimated useful life. Estimated useful lives are between four and 21 years. Intangible assets with an indefinite useful life are not subject to amortisation but are tested for impairment annually or more often if there is an indication of impairment.

(V) Impairment of assets

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

(W) Foreign currency translation

(i) Functional and presentation currency

Items included in the financial statements of controlled entities are measured using the currency of the primary economic environment in which the entity operates ("the functional currency"). The consolidated entity's financial statements are presented in Australian dollars, being the functional and presentation currency of the company.

(ii) Translation of foreign currency transactions and balances

Foreign currency transactions are translated into functional currencies at the rates of exchange at the dates of the transactions. At the balance sheet date, monetary assets and liabilities denominated in foreign currencies are translated at the rates

of exchange prevailing at that date. Resulting exchange gains and losses are included in the income statement.

(iii) Translation of overseas controlled entities

The results and balance sheets of all overseas controlled entities that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- assets and liabilities are translated at the closing balance sheet date rates of exchange;
- income and expenses are translated at cumulative average rates of exchange; and
- all resulting exchange differences are recognised as a separate component of equity.

On consolidation, exchange differences arising from the translation of the net investment in overseas controlled entities, and of financial liabilities and other instruments designated as hedges of such investments, are taken to shareholders' equity. When an overseas controlled entity is sold, these exchange differences are recognised in the income statement as part of the gain or loss on sale.

(iv) Hedging transactions

Derivatives are used to hedge the foreign exchange risk relating to certain transactions. Refer to note 1(O).

(X) Equity

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction from the proceeds, net of tax. Incremental costs directly attributable to the issue of new shares or options, or for the acquisition of a business, are included in the cost of acquisition as part of the purchase consideration.

The equity component of hybrid securities is calculated and disclosed as set out in note 1(Q).

(Y) Earnings per share

(i) Basic earnings per share

Basic earnings per share is determined by dividing net profit after income tax attributable to members of the company, adjusted for the cost of servicing equity other than ordinary shares, by the weighted average number of ordinary shares outstanding during the financial year, adjusted for bonus elements in ordinary shares issued during the year.

(ii) Diluted earnings per share

Diluted earnings per share adjusts the earnings figure used in the determination of basic earnings per share to exclude the after income tax effect of interest and other financing costs associated with dilutive potential ordinary shares and the weighted average number of shares assumed to have been issued for no consideration. It also adjusts the weighted average number of shares to include dilutive potential ordinary shares and instruments with a mandatory conversion feature.

(Z) Dividends

Provision is made for dividends which are declared, being appropriately authorised and no longer at the discretion of the entity, on or before the end of the financial year but not distributed at the balance sheet date.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

1

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

(AA) Employee benefits

(i) Superannuation

The consolidated entity participates in a number of superannuation plans and contributes to these plans in accordance with plan rules and actuarial recommendations, which are designed to ensure that each plan's funding provides sufficient assets to meet its liabilities.

Defined contribution plans

Contributions to defined contribution plans are expensed as incurred.

Defined benefit plans

The liability recognised in the balance sheet in respect of defined benefit superannuation plans is the present value of the defined benefit obligation at the balance sheet date less the fair value of plan assets, adjusted for any unrecognised past service costs. The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of high quality corporate or government bonds that are denominated in the currency in which the benefits will be paid, and that have a term to maturity approximating the term of the related superannuation liability. Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are recognised directly in equity. Past service costs are recognised immediately in the income statement, unless the changes to the superannuation plan are conditional on the employees remaining in service for a specified period of time (the vesting period) in which case the past service costs are amortised on a straight line basis over the vesting period.

(ii) Share based payments

The consolidated entity operates an equity settled, share based compensation plan. The fair value of the employee services received in exchange for the grant of those instruments is recognised as an expense. The total amount to be expensed over the vesting period is determined by reference to the fair value of the instruments granted, excluding the impact of any non-market vesting conditions. The fair value at grant date of the options and conditional rights is calculated using a binomial model. The fair value of each instrument is expensed evenly over the period between grant and vesting dates. Non-market vesting conditions are included in assumptions about the number of instruments that are expected to become exercisable.

At each balance sheet date, the consolidated entity revises its estimates of the number of options that are expected to become exercisable. The consolidated entity recognises the impact of the revision of original estimates, if any, in the income statement with a corresponding adjustment to equity.

(iii) Profit sharing and bonus plans

The consolidated entity recognises a liability and an expense for bonuses and profit sharing based on a formula that takes into consideration the profit attributable to the company's shareholders.

(iv) Termination benefits

Termination benefits are payable when employment is terminated before the normal retirement date or when an employee accepts voluntary redundancy in exchange for these benefits. The consolidated entity recognises termination benefits when it has demonstrably committed to either:

- terminating the employment of current employees according to a detailed formal plan without possibility of withdrawal; or
- providing termination benefits as a result of an offer made to encourage voluntary redundancy.

(v) Long service leave

The provision for long service leave is measured as the present value of expected future payments to be made in respect of services provided by employees up to the reporting date using the projected unit credit method. Benefits due more than 12 months after the balance sheet date are discounted to present value.

(AB) Treasury shares held in trust

The assets, liabilities and results of share based remuneration trusts are included in the balance sheet and results of the consolidated entity. These trusts may hold shares in the company to satisfy the company's obligations under the Employee Share and Option Plan ("the Plan"). Any shares in the company held by a trust are measured at cost (including any attributable acquisition costs). No gain or loss is recognised in the income statement on the sale, cancellation or reissue of these shares. On consolidation, these shares are presented on the balance sheet as treasury shares held in trust and represent a reduction in equity.

(AC) Leases

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight line basis over the period of the lease.

(AD) Rounding of amounts

The company is of a kind referred to in the ASIC class order 98/0100 dated 10 July 1998 (as amended by class order 04/667 dated 15 July 2004) relating to the "rounding off" of amounts in the financial statements. Amounts have been rounded off in the financial statements to the nearest million dollars or, in certain cases, to the nearest thousand dollars in accordance with that class order.

(AE) Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the board of directors, Group operations executive and Group head office management being the management bodies responsible for the consolidated entity's strategy and operations.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

2 NEW ACCOUNTING STANDARDS AND INTERPRETATIONS

TITLE	OPERATIVE DATE	
2008-3	Amendments to Australian Accounting Standards arising from AASB 3 and AASB 127 [AASBs 1, 2, 4, 5, 7, 101, 107, 112, 114, 116, 121, 128, 131, 132, 133, 134, 136, 137, 138 & 139 and Interpretations 9 & 107]	1 January 2010
2008-6	Further Amendments to Australian Accounting Standards arising from the Annual Improvements Project [AASB 1 & AASB 5]	1 January 2010
2008-8	Amendments to Australian Accounting Standards – Eligible Hedged Items [AASB 139]	1 January 2010
Interpretation 17	Distributions of Non-cash Assets to Owners	1 January 2010
2008-13	Amendments to Australian Accounting Standards arising from AASB Interpretation 17 – Distributions of Non-cash Assets to Owners [AASB 5 & AASB 110]	1 January 2010
AASB 3	Revision to Australian Accounting Standard – Business Combinations [AASB 3]	1 January 2010
2009-4	Amendments to Australian Accounting Standards arising from the Annual Improvements Project [AASB 2 & AASB 138 and Interpretations 9 & 16]	1 January 2010
2009-5	Further Amendments to Australian Accounting Standards arising from the Annual Improvements Project [AASB 5, 8, 101, 107, 117, 118, 136 & 139]	1 January 2010
2009-7	Amendments to Australian Accounting Standards [AASB 5, 7, 107, 136 & 139 and Interpretation 17]	1 January 2010
2009-10	Amendments to Australian Accounting Standards – Classification of Rights Issues [AASB 132]	1 January 2011
2009-11	Amendments to Australian Accounting Standards arising from AASB 9 [AASB 1, 3, 4, 5, 7, 101, 102, 108, 112, 118, 121, 127, 128, 131, 132, 136, 139, 1023 & 1038 and Interpretations 10 & 12]	1 January 2013
2009-12	Amendments to Australian Accounting Standards [AASBs 5, 8, 108, 110, 112, 119, 133, 137, 139, 1023 & 1031 and Interpretations 2, 4, 16, 1039 & 1052]	1 January 2011
2009-13	Amendments to Australian Accounting Standards arising from Interpretation 19 [AASB 1]	1 January 2011
2009-14	Amendments to Australian Accounting Interpretation – Prepayments of a Minimum Funding Requirement [AASB Interpretation 14]	1 January 2011
AASB 9	Financial Instruments	1 January 2013

The Australian accounting standards, interpretations and amendments detailed in the table above are not mandatory for the company or the consolidated entity until the operative dates stated; however, early adoption is permitted.

The consolidated entity and the company will apply the amendments detailed above for the reporting periods beginning on the operative dates set out above. The application of these standards is not expected to have a material impact on either the consolidated entity's or the company's financial statements.

3 CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

The consolidated entity is an international general insurance and reinsurance group underwriting most major commercial and personal lines classes of business through operations in 47 countries. The class of business mix and an analysis of the consolidated entity's gross written and net earned premium from insurance and reinsurance business is shown on page 13. The head office function is located in Australia and exists to support the activities of divisional operations as follows:

- Australian operations, which writes general insurance throughout Australia providing all major lines of insurance for commercial and personal risks;
- Asia Pacific operations, which comprises general insurance operations in 15 countries;
- European operations, which comprises general insurance business written in the UK and throughout mainland Europe; both general insurance and reinsurance business written through Lloyd's of London; and reinsurance business written in Ireland; and
- QBE the Americas, which comprises general insurance and reinsurance operations in the US and a number of Latin American countries.

In view of the geographic and product diversity, the consolidated entity has developed a strong, centralised risk management and policy framework designed to ensure consistency of approach across a number of operational activities, subject to the specific requirements of local markets, legislation and regulation. Such operational activities include underwriting, claims management, actuarial assessment of the claims provision and investment management. In addition, assessment of the risk margin undertaken at a divisional level is subject to detailed head office review and the consolidated entity's probability of adequacy is determined by the Group's chief actuarial officer.

Given the centralised approach to many of its activities and the product and geographic diversification, sensitivity analyses in respect of critical accounting estimates and judgments are presented at the consolidated entity level in order to provide a level of analysis which is more meaningful, relevant, reliable and comparable year on year. It is considered that disclosure at business segment or product level would not provide a meaningful overview given the complex interrelationships between the variables underpinning the consolidated entity's operations.

The consolidated entity makes estimates and judgments in respect of the reported amounts of certain assets and liabilities. These estimates and judgments are determined by qualified and experienced employees with reference to historical data and reasoned expectations of future events, and are continually updated. The key areas in which critical estimates and judgments are applied are described as follows.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

3

CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS CONTINUED

(A) Ultimate liability arising from claims made under insurance contracts

Provision is made for the estimated cost of claims incurred but not settled at the balance sheet date. This provision consists of estimates of both the expected ultimate cost of claims notified to the consolidated entity as well as the expected ultimate cost of claims incurred but not reported to the consolidated entity ("IBNR"). The estimated cost of claims includes direct expenses that are expected to be incurred in settling those claims.

The estimation of IBNR is generally subject to a greater degree of uncertainty than the estimation of the cost of settling claims already notified to the consolidated entity, where more information about the claims is generally available. Liability and other long tail classes of business, where claims settlement may not happen for many years after the event giving rise to the claim, typically display greater variability between initial estimates and final settlement due to delays in reporting claims, uncertainty in respect of court awards and future claims inflation. Claims in respect of property and other short tail classes are typically reported and settled sooner after the claim event, giving rise to more certainty. The estimation techniques and assumptions used in determining the outstanding claims provision and the associated reinsurance and other recoveries are described below.

(i) Insurance risk assumptions

The consolidated entity's process for establishing the outstanding claims provision involves extensive consultation with internal and external actuaries, claims managers, underwriters and other senior management. This process includes quarterly internal claims review meetings attended by senior divisional and Group management and detailed review by external actuaries at least annually. The risk management procedures related to the actuarial function are explained further in note 4.

The determination of the amounts that the consolidated entity will ultimately pay for claims arising under insurance and reinsurance contracts involves a number of critical assumptions. Some of the uncertainties impacting these assumptions are as follows:

- changes in patterns of claims incidence, reporting and payment;
- volatility in the estimation of future costs for long tail insurance classes due to the longer period of time that elapses before a definitive determination of the ultimate claims cost can be made;
- incidence of catastrophic events close to the balance sheet date;
- changes in the legal environment, including the interpretation of liability laws and the quantum of damages; and
- social and economic trends, for example price and wage inflation and interest rates.

The potential impact of changes in key assumptions on the consolidated entity's income statement and balance sheet are summarised in note 3(A)(vii).

(ii) Central estimates

The outstanding claims provision comprises the central estimate and a risk margin which is added to the central estimate to achieve a desired probability of adequacy. The outstanding claims provision is discounted at risk-free rates of return to reflect the time value of money.

A central estimate is an estimate of the level of claims provision that is intended to contain no intentional under or over estimation. As the consolidated entity requires a higher probability that estimates will be adequate over time, a risk margin is added to the central estimate of outstanding claims.

Central estimates for each class of business are determined by reference to a variety of estimation techniques, generally based on a statistical analysis of historical experience which assumes an underlying pattern of claims development and payment. The final selected central estimates are based on a judgmental consideration of the results of each method and qualitative information, for example, the class of business, the maturity of the portfolio and the expected term to settlement of the class. Projections are based on both historical experience and external benchmarks where relevant.

Central estimates are calculated gross of any reinsurance recoveries. A separate estimate is made of the amounts recoverable from reinsurers based on the gross outstanding claims provision.

(iii) Risk margin

The determination of the appropriate level of risk margin takes into account the uncertainty or variability of each class of business and the diversification benefits achieved by writing a number of classes of business in a number of geographic locations.

The measurement of variability by class of business uses techniques similar to those used in determining the central estimate. These techniques determine a range of possible outcomes of ultimate payments and assign a likelihood to outcomes at different levels. The use of a range of outcomes allows a determination of the risk margin required to provide an estimate at a given probability of adequacy, e.g. nine times in 10 (a 90% probability of adequacy). These techniques use standard statistical distributions, and the measure of variability is referred to as the standard deviation or the coefficient of variation.

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 the risk margins for the individual classes. This reflects the benefit of diversification in general insurance. The statistical measure used to determine diversification is called the correlation. The higher the correlation between two classes of business, the more likely it is that a negative outcome in one class will correspond to a negative outcome in the other class. For example, high correlation exists in classes of business affected by court cases involving bodily injury claims such as motor third party liability (CTP), workers' compensation and public liability.

Whilst there are estimation techniques for determining correlations, they are difficult to apply. The correlations adopted by the consolidated entity are normally derived from industry analysis, the consolidated entity's historical experience and the judgment of experienced and qualified actuaries.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

3 CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS CONTINUED

The risk margin for the consolidated entity is determined by analysing the variability of each class of business and the correlation between classes of business and divisions. Correlations are determined for aggregations of classes of business, where appropriate, at the divisional level. Applying correlations between divisions results in a further diversification benefit to the consolidated entity with a consequent impact on the consolidated entity's risk margin.

The potential impact of changes in the coefficient of variation assumptions on the consolidated entity's income statement and balance sheet is summarised in note 3(A)(vii).

(iv) Assets arising from contracts with reinsurers

Assets arising from contracts with the consolidated entity's reinsurers are determined using the same methods described above. In addition, the recoverability of these assets is assessed at each balance sheet date to ensure that the balances properly reflect the amounts that will ultimately be received, taking into account counterparty and credit risk. Counterparty and credit risk in relation to reinsurance assets are considered in note 4.

(v) Expected present value of future cash flows for future claims

The expected present value of future cash flows for future claims and risk margin used in the liability adequacy test (refer note 21(D)) are determined using the same methods described above.

(vi) Financial assumptions used to determine the outstanding claims provisions

The outstanding claims provision is discounted to net present value using a risk-free rate of return. Details of risk-free rates used to discount the outstanding claims provision are summarised below.

	2009 %		2008 %	
	SUCCEEDING YEAR	SUBSEQUENT YEARS	SUCCEEDING YEAR	SUBSEQUENT YEARS
Australia	1.19 – 6.00	1.19 – 6.00	2.80 – 3.30	2.75 – 4.15
Asia Pacific	0.95 – 7.56	0.95 – 7.56	0.27 – 11.22	0.27 – 11.22
European operations	1.00 – 5.30	1.00 – 5.30	1.50 – 2.40	1.50 – 2.40
the Americas	2.30	2.30	1.50	1.50
Equator Re	0.95 – 7.56	0.95 – 7.56	1.50 – 3.60	1.50 – 3.60

The potential impact of a change in discount rates on the consolidated entity's income statement and balance sheet is summarised in note 3(A)(vii).

(vii) Impact of changes in key variables on the outstanding claims provision

The impact of changes in key outstanding claims variables is summarised in the table below. Each change has been calculated in isolation from the other changes and each change shows the after tax impact on profit and equity assuming that there is no change to:

- Any of the other variables – This is considered unlikely as, for example, an increase in interest rates is normally accompanied by an increase in the rate of inflation. As can be seen from the table below, the impact of a change in discount rates is largely offset by the impact of a change in the rate of inflation. The impact on financial assets of a change in interest rates is shown in note 5(A)(ii).
- The probability of adequacy – It is likely that if, for example, the central estimate was to increase by 5%, at least part of the increase would result in a decrease in the probability of adequacy, which is currently estimated to be 88.1%. Likewise, if the coefficient of variation were to increase by 1%, it is likely that the probability of adequacy would reduce from its current level and that the change would therefore impact the amount of risk margins held rather than net profit after income tax or equity.

	MOVEMENT IN VARIABLE %	FINANCIAL IMPACT ⁽¹⁾			
		PROFIT (LOSS)	EQUITY	PROFIT (LOSS)	EQUITY
		2009 \$M	2009 \$M	2008 \$M	2008 \$M
Central estimate	+5	(463)	(463)	(524)	(524)
	-5	463	463	524	524
Inflation rate	+1	(259)	(259)	(283)	(283)
	-1	246	246	268	268
Discount rate	+1	250	250	265	265
	-1	(269)	(269)	(284)	(284)
Coefficient of variation	+1	(112)	(112)	(115)	(115)
	-1	112	112	113	113
Weighted average term to settlement	+10	85	85	68	68
	-10	(86)	(86)	(68)	(68)

(1) Determined at the consolidated entity level net of reinsurance and taxation at the prima facie rate of 30%.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

3 CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS CONTINUED

AASB 1023: General Insurance Contracts requires that the outstanding claims provision shall be discounted for the time value of money using risk-free rates that are based on current observable, objective rates that relate to the nature, structure and terms of the future obligations. The standard also states that government bond rates may be an appropriate starting point in determining a risk-free rate.

The consolidated entity has adopted government bond rates appropriate to the mean term and currency of the outstanding claims provision. This has resulted in a probability of adequacy of 88.1%.

(B) Retirement benefit obligations

The present value of the obligations arising from the consolidated entity's defined benefit superannuation plans is determined by external actuaries based on discount rate, inflation rate, mortality rate, salary growth and investment return assumptions.

The discount rate applied to the various plans is the interest rate on high quality corporate bonds where there is a sufficiently deep market or the appropriate government bond rate.

Mortality assumptions are affected by experience which indicates increasing longevity, particularly for certain age groups of the population. The consolidated entity has considered the consensus of professional opinions from a number of external actuaries in respect of the appropriateness of the mortality tables selected for use in the valuation of the superannuation obligations for each of the consolidated entity's plans.

The potential impact of a change in the most sensitive assumptions on the consolidated entity's income statement and balance sheet is summarised below.

	MOVEMENT IN VARIABLE %	FINANCIAL IMPACT ⁽¹⁾			
		PROFIT (LOSS) 2009 \$M	EQUITY 2009 \$M	PROFIT (LOSS) 2008 \$M	EQUITY 2008 \$M
Discount rate	+1	-	27	-	28
	-1	-	(97)	-	(80)
Inflation rate	+1	-	(57)	-	(38)
	-1	-	14	-	11

(1) Determined at the consolidated entity level net of taxation at the prima facie rate of 30%.

(C) Intangible assets

Goodwill and intangible assets with an indefinite useful life are tested annually for impairment or more frequently when changes in circumstances indicate that the carrying amount may not be recoverable. Intangible assets subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying value may not be recoverable. The impairment review is based on the net present value of estimated future cash flows of the relevant cash generating unit which is determined by reference to, amongst other factors, the estimated combined operating ratio in the business plan.

If the discount rate applied in these calculations was increased by 1% over the rates applied at 31 December 2009, the consolidated entity would be required to reflect an impairment of \$122 million.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

4 RISK MANAGEMENT

An overview of the consolidated entity's risk management framework is provided in the risk management statement on pages 16 to 18 and in the risk management section of the corporate governance statement on pages 47 and 48.

The consolidated entity's risk management policy, strategy and framework are embedded in the Group head office and in each of the divisional operations, ensuring a consistent approach to managing risk across the organisation. The board annually approves a comprehensive risk management strategy ("RMS") and a reinsurance management strategy ("REMS"), both of which are lodged with the Australian Prudential Regulation Authority ("APRA").

The consolidated entity's risk management objectives are to:

- adequately price risk;
- avoid unwelcome surprises by reducing uncertainty and volatility;
- achieve competitive advantage through better understanding the risk environment in which the consolidated entity operates;
- optimise risk and more effectively allocate capital and resources by assessing the balance of risk and reward;
- comply with laws and internal procedures; and
- improve resilience to external events.

A fundamental part of the consolidated entity's overall risk management strategy is the effective governance and management of the risks that impact the amount, timing and uncertainty of cash flows from insurance contracts. The Group has established internal controls to manage risk in the key areas of exposure relevant to its business. The broad risk categories discussed below are:

- insurance risk;
- reinsurance counterparty risk;
- acquisition risk;
- operational risk; and
- capital and regulatory risk.

Financial risks are considered in note 5. Within each of these categories, risks are evaluated before consideration of the impact of mitigating controls. The existence and effectiveness of such mitigating controls are then measured to ensure that residual risks are managed within risk tolerance.

(A) Insurance risk

The risks inherent in any single insurance contract are the possibility of the insured event occurring and the uncertainty of the amount of the resulting claim. By the very nature of an insurance contract, these risks are random and unpredictable. In relation to the pricing of individual insurance contracts and the determination of the level of the outstanding claims provision in relation to a portfolio of insurance contracts, the principal risk is that the ultimate claims payments will exceed the carrying amount of the provision established.

Experience shows that the larger the portfolio of similar insurance contracts, the smaller the relative variability around the expected outcome will be. In addition, a more diversified insurance and reinsurance group is less likely to be affected by a change in any one specific portfolio. The consolidated entity has developed its underwriting strategy to diversify the type of insurance risks accepted and, within each of these categories, to achieve a sufficiently large population of risks to reduce the variability of the expected outcome.

The consolidated entity has established the following protocols to manage its insurance risk across the underwriting, claims and actuarial disciplines.

(i) Underwriting risks

Selection and pricing of risks

Underwriting authority is delegated to experienced underwriters for the forthcoming year following a detailed retrospective and prospective analysis of each class of business as part of the consolidated entity's annual business planning process. Delegated authorities reflect the level of risk which the consolidated entity is prepared to take. The authorities include reference to some combination of:

- gross written premium;
- premium per contract;
- sum insured per contract;
- aggregate exposures per zone;
- probable maximum loss and realistic disaster scenarios ("RDSs");
- levels and quality of reinsurance protection;
- geographic exposures; and/or
- classes of business and types of product that may be written.

Limits in respect of each of the above are set at a portfolio, divisional and consolidated entity level and are included within business plans for individual classes of business. They are adjusted at a local level to reflect a risk factor in respect of each controlled entity depending on previous underwriting results, the economic environment and other potential drivers of volatility.

Insurance and reinsurance policies are written in accordance with local management practices and regulations within each jurisdiction taking into account the consolidated entity's risk tolerance and underwriting standards. Non-standard and long-term policies may only be written if expressly included in the delegated authorities. No individual long-term or non-standard policy is material to the consolidated entity.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

4 RISK MANAGEMENT CONTINUED

Pricing of risks is controlled by the use of in-house pricing models relevant to specific portfolios and the markets in which the consolidated entity operates. Experienced underwriters and actuaries maintain historical pricing and claims analysis for each portfolio and this is combined with a detailed knowledge of the current developments in the respective markets and classes of business.

Concentration risk

The consolidated entity's exposure to concentrations of insurance risk is mitigated by a portfolio diversified across 47 countries and hundreds of classes of business. Product diversification is achieved through a strategy of developing strong underwriting skills in a wide variety of classes of business. A combination of core and speciality products under the control of employees skilled in underwriting such products allows the consolidated entity to lead underwrite in many of the markets in which it operates.

The table below demonstrates the diversity of the consolidated entity's operations.

GROSS EARNED PREMIUM	2009 \$M	2008 \$M
Property	4,149	3,519
Motor and motor casualty	2,720	2,518
Liability	2,120	2,154
Marine, energy and aviation	1,386	1,285
Workers' compensation	1,044	1,186
Professional indemnity	963	885
Accident and health	492	490
Other	496	317
Financial and credit	464	276
Bloodstock	240	223
	14,074	12,853

The consolidated entity has potential exposure to catastrophe losses that may impact more than one operating division. Each year, the consolidated entity sets its tolerance to concentration risk. RDSs, using industry standard and QBE determined probable maximum losses and various catastrophe models, are calculated for each portfolio as part of the business planning process. These RDSs are aggregated across all portfolios and divisions to determine the consolidated entity's maximum event retention ("MER") which is the estimated maximum net claim from a major natural catastrophe with an approximate return period of 250 years. The MER must be less than the consolidated entity's concentration risk tolerance, otherwise steps such as the purchase of additional reinsurance are taken to limit the exposure.

In 2009, the net cost to the consolidated entity of weather-related catastrophic events above \$2.5 million was \$260 million before income tax (2008 \$424 million before income tax).

(ii) Claims management and claims provisioning risks

The consolidated entity's approach to determining the outstanding claims provision and the related sensitivities are set out in note 3. The consolidated entity seeks to ensure the adequacy of its outstanding claims provision by reference to the following controls:

- experienced claims managers work with underwriters on coverage issues and operate within the levels of authority delegated to them in respect of the settlement of claims;
- processes exist to ensure that all claims advices are captured and updated on a timely basis and with a realistic assessment of the ultimate claims cost;
- initial IBNR estimates are set by experienced internal actuaries in conjunction with the local product managers and underwriters for each class of business in each business unit;
- the aggregate outstanding claims provision for each controlled entity is assessed in a series of quarterly internal claims review meetings, which are attended by senior divisional management and one or both of the Group chief risk officer and Group chief actuarial officer in order to ensure consistency of provisioning practices across all divisions; and
- approximately 90% of the consolidated entity's outstanding claims provision is reviewed by external actuaries at least annually.

Despite the rigour involved in the establishment and review of the outstanding claims provision, the provision is subject to significant uncertainty for the reasons set out in note 3.

(B) Reinsurance counterparty risk

The consolidated entity reinsures a portion of risks underwritten to control exposure to insurance losses, reduce volatility and protect capital. The consolidated entity's strategy in respect of the selection, approval and monitoring of reinsurance arrangements is addressed by the following protocols:

- treaty or facultative reinsurance is placed in accordance with the requirements of the consolidated entity's REMS and Group security committee guidelines;
- reinsurance arrangements are regularly reassessed to determine their effectiveness based on current exposures, historical losses and potential future losses based on RDSs and the consolidated entity's MER; and
- exposure to reinsurance counterparties and the credit quality of those counterparties is actively monitored.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

4 RISK MANAGEMENT CONTINUED

Strict controls are maintained over reinsurance counterparty exposures. Reinsurance is placed with counterparties that have a strong credit rating and concentration of risk is managed by adherence to counterparty limits. Counterparty limits are reviewed by management on a regular basis. Credit risk exposures are calculated regularly and compared with authorised credit limits. In certain cases, the consolidated entity requires letters of credit or other collateral arrangements to be provided to guarantee the recoverability of the amount involved. The credit rating analysis below includes the impact of such security arrangements. In some cases, further security has been obtained in the form of trust arrangements, reinsurer default protection and other potential offsets. This additional security has not been included in the credit rating analysis set out below.

The following table provides information about the quality of the consolidated entity's credit risk exposure in respect of reinsurance and other recoveries on outstanding claims at the balance sheet date. The analysis classifies the assets according to Standard & Poor's counterparty credit ratings. AAA is the highest possible rating. Rated assets falling outside the range of AAA to BBB are classified as speculative grade.

		CREDIT RATING						TOTAL \$M
		AAA \$M	AA \$M	A \$M	BBB \$M	SPECULATIVE GRADE \$M	NOT RATED \$M	
Reinsurance and other recoveries on outstanding claims	2009	157	1,398	1,830	26	78	194	3,683
	2008	231	2,739	1,756	35	113	169	5,043
Reinsurance and other recoveries on paid claims	2009	19	132	206	3	12	36	408
	2008	15	164	130	6	16	44	375

The following table provides further information regarding the ageing of reinsurance and other recoveries on paid claims at the balance sheet date.

		PAST DUE BUT NOT IMPAIRED					TOTAL \$M
		NEITHER PAST DUE NOR IMPAIRED \$M	0 TO 3 MTHS \$M	3 TO 6 MTHS \$M	6 MTHS TO 1 YEAR \$M	GREATER THAN 1 YEAR \$M	
Reinsurance and other recoveries on paid claims	2009	131	163	46	20	48	408
	2008	72	164	52	24	63	375

(C) Acquisition risk

The consolidated entity's strategy of growth by acquisition exposes it to additional risks. Acquisition risks are principally managed by the consolidated entity's controls over the selection of potential acquisitions, due diligence, negotiation of warranties and indemnities and subsequent integration processes. The consolidated entity has experienced due diligence teams in each of the divisions and has documented minimum requirements for carrying out due diligence.

(D) Operational risk

Operational risk is the risk of loss arising from system failure or inadequacies, human error or external events that does not relate to insurance, acquisition, capital and regulatory or financial risks. The consolidated entity manages operational risk within the same robust control framework as its other risks. One of the cornerstones of the consolidated entity's risk management framework is the recruitment and retention of high quality people who are entrusted with appropriate levels of autonomy within the parameters of disciplined risk management practices. The consolidated entity operates a system of delegated authorities based on expertise and proven performance, and compliance is closely monitored. Other controls include effective segregation of duties, access controls and authorisation and reconciliation procedures.

(E) Capital and regulatory risk

Australian and overseas controlled entities are subject to extensive prudential and other forms of regulation in the jurisdictions in which they conduct business. Prudential regulation is generally designed to protect policyholders. Regulation covers a number of areas including solvency, change in control and capital movement limitations. The regulatory environment in Australia and overseas continues to evolve in response to economic, political and industry developments. The consolidated entity works closely with regulators and monitors regulatory developments across its global operations to assess their potential impact on its ability to meet solvency and other requirements. Refer to note 25(G).

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

5 FINANCIAL RISK

The operating activities of the consolidated entity expose it to financial risks such as market risk, credit risk and liquidity risk. The consolidated entity's risk management framework recognises the unpredictability of financial markets and seeks to minimise potential adverse effects on its financial performance. The key objective of the consolidated entity's asset and liability management strategy is to ensure sufficient liquidity is maintained at all times to meet the consolidated entity's obligations, including its settlement of insurance liabilities and, within these parameters, to optimise investment returns for policyholders and shareholders.

(A) Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market factors. Market risk comprises three types of risk: currency risk (due to fluctuations in foreign exchange rates), interest rate risk (due to fluctuations in market interest rates) and price risk (due to fluctuations in market prices).

(i) Currency risk

Operational currency risk

The consolidated entity is exposed to currency risk in respect of its operational net foreign currency exposures within each of its controlled entities. This risk is managed as follows:

- as far as is practicable, each controlled entity manages the volatility arising from changes in foreign exchange rates by matching liabilities with assets of the same currency, thus ensuring that any exposures to foreign currencies are minimised; and
- where possible, forward foreign exchange contracts are used to protect residual currency positions. These forward foreign exchange contracts are accounted for in accordance with the derivatives accounting policy set out in note 1(N).

Foreign exchange gains or losses arising from operational foreign currency exposures are included in the income statement with the gains or losses from the related forward foreign exchange contracts. The risk management process covering the use of forward foreign exchange contracts involves close senior management scrutiny, including regular board and other management reporting. All forward foreign exchange contracts are subject to delegated authority levels provided to management, and the levels of exposure are reviewed on an ongoing basis.

The consolidated entity's policy is to mitigate, where possible, its operational foreign currency exposures at a controlled entity level. Residual foreign currency exposures at the controlled entity level are managed to be within an absolute local currency unit limit.

The analysis below demonstrates the impact on profit after income tax and equity of a movement in foreign currency exchange rates against the Australian dollar on our major operational currency exposures. The basis for the sensitivity calculation is the residual controlled entity foreign currency exposures at the balance sheet date.

	RESIDUAL EXPOSURE AT 31 DEC 2009 \$M	MOVEMENT IN VARIABLE AGAINST A\$ %	FINANCIAL IMPACT ⁽¹⁾		RESIDUAL EXPOSURE AT 31 DEC 2008 \$M	MOVEMENT IN VARIABLE AGAINST A\$ %	FINANCIAL IMPACT ⁽¹⁾	
			PROFIT (LOSS) 2009 \$M	EQUITY 2009 \$M			PROFIT (LOSS) 2008 \$M	EQUITY 2008 \$M
CONSOLIDATED								
US dollar	208	+10	15	15	65	+10	5	5
		-10	(15)	(15)		-10	(5)	(5)
Sterling	(878)	+10	(61)	(61)	48	+10	3	3
		-10	61	61		-10	(3)	(3)
Euro	(47)	+10	(3)	(3)	168	+10	12	12
		-10	3	3		-10	(12)	(12)

(1) Determined at the consolidated entity level net of taxation at the prima facie rate of 30%.

COMPANY	RESIDUAL EXPOSURE AT 31 DEC 2009 \$M	MOVEMENT IN VARIABLE AGAINST A\$ %	FINANCIAL IMPACT ⁽¹⁾		RESIDUAL EXPOSURE AT 31 DEC 2008 \$M	MOVEMENT IN VARIABLE AGAINST A\$ %	FINANCIAL IMPACT ⁽¹⁾	
			PROFIT (LOSS) 2009 \$M	EQUITY 2009 \$M			PROFIT (LOSS) 2008 \$M	EQUITY 2008 \$M
US dollar	(261)	+10	(18)	(18)	(6)	+10	-	-
		-10	18	18		-10	-	-
Sterling	(992)	+10	(69)	(69)	46	+10	3	3
		-10	69	69		-10	(3)	(3)

(1) Net of taxation at the prima facie rate of 30%.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

5

FINANCIAL RISK CONTINUED

Currency risk in relation to net investment in foreign operations

The consolidated entity is exposed to currency risk in relation to the translation of its net investment in foreign operations to Australian dollars. Currently, the consolidated entity does not hedge the net exposure to foreign currency risk in relation to the net investment in foreign operations in tradeable currencies. This practice provides greater stability of capital adequacy levels because the consolidated entity's shareholders' funds move in line with changes in assets and liabilities on translation to Australian dollars.

During 2008, the consolidated entity's practice was to actively manage all exposure to foreign currency risk in relation to the net investment in foreign operations, where practicable, with residual currency exposures managed so that they did not exceed 5% of consolidated shareholders' funds.

To the extent that currency risk in relation to net investment in foreign operations is hedged, this is done using either foreign currency borrowings or forward foreign exchange contracts designated as hedging instruments. Those arrangements which meet the hedging criteria set out in AASB 139 are accounted for in accordance with the accounting policy set out in note 1(O). The effectiveness of the currency management processes and the related use of derivatives is actively monitored by the Group chief financial officer. The risk management process covering forward foreign exchange contracts and hedges involves close senior management scrutiny, including regular board and other management reporting. All forward foreign exchange contracts and hedge transactions are subject to delegated authority levels provided to management, and the levels of exposure are reviewed on an ongoing basis.

All instruments that are designated as hedges in accordance with AASB 139 are tested for effectiveness on both a prospective and a retrospective basis. These tests are performed at least quarterly.

The analysis below demonstrates the impact on profit after income tax and equity of a movement in foreign currency exchange rates on our major currency exposures arising on the translation of net investments in foreign operations to Australian dollars. The basis for the sensitivity calculation is the consolidated entity's actual residual exposure at the balance sheet date.

	RESIDUAL EXPOSURE AT 31 DEC 2009 \$M	MOVEMENT IN VARIABLE AGAINST A\$ %	FINANCIAL IMPACT ⁽¹⁾		RESIDUAL EXPOSURE AT 31 DEC 2008 \$M	MOVEMENT IN VARIABLE AGAINST A\$ %	FINANCIAL IMPACT ⁽¹⁾	
			PROFIT (LOSS) 2009 \$M	EQUITY 2009 \$M			PROFIT (LOSS) 2008 \$M	EQUITY 2008 \$M
US dollar	5,032	+10	-	503	60	+10	-	6
		-10	-	(503)		-10	-	(6)
Sterling	365	+10	-	36	38	+10	-	4
		-10	-	(36)		-10	-	(4)
Singapore dollar	78	+10	-	8	-	-	-	-
		-10	-	(8)		-	-	-
New Zealand dollar	71	+10	-	7	-	-	-	-
		-10	-	(7)		-	-	-
Colombian Peso	57	+10	-	6	-	-	-	-
		-10	-	(6)		-	-	-
Euro	41	+10	-	4	-	-	-	-
		-10	-	(4)		-	-	-

(1) Determined at the consolidated entity level.

(ii) Interest rate risk

Financial instruments with floating rate interest expose the consolidated entity to cash flow interest rate risk, whereas fixed interest rate instruments expose the consolidated entity to fair value interest rate risk.

The consolidated entity's risk management approach is to minimise interest rate risk by actively managing investment portfolios to achieve a balance between cash flow interest rate risk and fair value interest rate risk. The consolidated entity invests in high quality, liquid fixed interest securities and cash and actively manages the duration of the fixed interest portfolio.

Interest-bearing borrowings are valued at amortised cost and therefore do not expose the consolidated entity to fair value interest rate risk. In addition, the majority of these interest-bearing borrowings are at fixed interest rates and so do not expose the entity to cash flow interest rate risk; however, Eurobonds and ABC securities for funds at Lloyd's issued at variable interest rates are subject to cash flow interest rate risk. The consolidated entity manages this interest rate risk and other financial risk associated with the Eurobonds and ABC securities for funds at Lloyd's by using derivative financial instruments. For further details refer to notes 12(D) and 34 respectively.

The contractual maturity profile of the consolidated entity's interest-bearing financial assets and hence its exposure to interest rate risk, and the effective weighted average interest rate for interest-bearing financial assets (excluding ABC financial assets pledged for funds at Lloyd's) is analysed on the following page. The table includes investments at the maturity date of the security; however, many of the longer-dated securities have call dates of relatively short duration. The maturity of ABC financial assets pledged for funds at Lloyd's is shown in note 34(C).

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

5 FINANCIAL RISK CONTINUED

	FLOATING INTEREST RATE ⁽¹⁾	FIXED INTEREST RATE MATURING IN						TOTAL	
		1 YEAR OR LESS ⁽²⁾	1 TO 2 YEARS	2 TO 3 YEARS	3 TO 4 YEARS	4 TO 5 YEARS	OVER 5 YEARS ⁽³⁾		
At 31 December 2009									
Interest-bearing financial assets	\$M	7,938	12,395	1,787	815	95	18	474	23,522
Weighted average interest rate	%	1.9	1.9	3.5	5.1	5.9	4.4	6.2	2.2
At 31 December 2008									
Interest-bearing financial assets	\$M	5,820	18,011	1,087	899	618	56	349	26,840
Weighted average interest rate	%	4.7	2.5	3.7	5.3	2.5	5.5	6.9	3.2

(1) Includes \$17 million (2008 \$641 million) of cash and cash equivalents and \$3 million (2008 \$nil) of short-term money relating to the company.

(2) Includes \$245 million (2008 \$52 million) of short-term money relating to the company.

(3) Interest-bearing investments owned by the company of \$nil (2008 \$718 million) have a maturity of greater than five years. These were eliminated on consolidation.

The consolidated entity's sensitivity to movements in interest rates in relation to the value of interest-bearing financial assets is shown in the table below.

	MOVEMENT IN VARIABLE %	FINANCIAL IMPACT ⁽¹⁾		MOVEMENT IN VARIABLE %	FINANCIAL IMPACT ⁽¹⁾	
		PROFIT (LOSS) 2009 \$M	EQUITY 2009 \$M		PROFIT (LOSS) 2008 \$M	EQUITY 2008 \$M
Interest rate movement – interest-bearing financial assets	+1.5	(113)	(113)	+1.5	(141)	(141)
	-1.5	113	113	-1.5	141	141

(1) Determined at the consolidated entity level net of taxation at the prima facie rate of 30%.

The effect of interest rate movements on the consolidated entity's provision for outstanding claims is included in note 3(A)(vii).

(iii) Price risk

Price risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market prices (other than those arising from interest rate or currency risk), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting all similar financial instruments traded on the market.

The consolidated entity is exposed to price risk on its investment in equities and uses derivative financial instruments to manage this exposure. The risk management processes over these derivative financial instruments are the same as those explained in note 5(A)(i) in respect of forward foreign exchange contracts. Exposure is also managed by diversification across worldwide markets and currencies.

At 31 December 2009, 5.9% (2008 5.3%) of the consolidated entity's investments and cash was held in listed equities, of which the majority were publicly traded in the major financial markets.

The potential impact of movements in the market value of listed equities on the consolidated entity's income statement and balance sheet is shown in the sensitivity analysis in the table below. The calculation assumes that exposures are unhedged although in practice the consolidated entity may purchase derivatives to manage this exposure. The price risk in relation to unlisted securities is immaterial in terms of the possible impact on profit or loss and has not been included in the sensitivity analysis.

	EXPOSURE AT 31 DEC 2009 \$M	MOVEMENT IN VARIABLE %	FINANCIAL IMPACT ⁽¹⁾		EXPOSURE AT 31 DEC 2008 \$M	MOVEMENT IN VARIABLE %	FINANCIAL IMPACT ⁽¹⁾	
			PROFIT (LOSS) 2009 \$M	EQUITY 2009 \$M			PROFIT (LOSS) 2008 \$M	EQUITY 2008 \$M
ASX 200	676	+20	94	94	566	+20	77	77
		-20	(94)	(94)		-20	(77)	(77)
FTSE 100	198	+20	28	28	265	+20	34	34
		-20	(28)	(28)		-20	(34)	(34)
EURO STOXX	102	+20	15	15	110	+20	15	15
		-20	(15)	(15)		-20	(15)	(15)
S&P 500	514	+20	72	72	543	+20	70	70
		-20	(72)	(72)		-20	(70)	(70)

(1) Determined at the consolidated entity level net of taxation at the prima facie rate of 30%.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

5 FINANCIAL RISK CONTINUED

(B) Credit risk

Credit risk is the risk that one party to a financial instrument will cause financial loss to the other party by failing to discharge an obligation. The following policies and procedures are in place to mitigate the consolidated entity's exposure to credit risk:

- a Group-wide investment credit risk policy is in place which defines what constitutes credit risk for the consolidated entity and establishes tolerance levels. Compliance with the policy is monitored and exposures and breaches are reported to the Group investment committee;
- net exposure limits are set for each counterparty or group of counterparties in relation to investments, cash deposits and forward foreign exchange exposures. The policy also sets out minimum credit ratings for investments;
- the consolidated entity has strict guidelines covering the limits and terms of net open derivative positions and the counterparties with which the consolidated entity may transact. The consolidated entity does not expect any investment counterparties to fail to meet their obligations given their strong credit ratings and therefore does not require collateral or other security to support derivatives. The consolidated entity only uses derivatives in highly liquid markets; and
- credit risk in respect of premium debtors and reinsurance receivables is actively monitored. Strict controls are maintained over counterparty exposures. Business is transacted with counterparties that have a strong credit rating and concentration of risk is avoided by adherence to counterparty limits. The provision for impairment is formally assessed by management at least four times a year.

The following tables provide information regarding the aggregate credit risk exposure of the consolidated entity and the company at the balance sheet date in respect of the major classes of financial assets. The analysis classifies the assets according to Moody's counterparty credit ratings. Aaa is the highest possible rating. Rated assets falling outside the range of Aaa to Baa are classified as speculative grade.

As at 31 December 2009

CONSOLIDATED	CREDIT RATING					NOT RATED \$M	TOTAL \$M
	Aaa \$M	Aa \$M	A \$M	Baa \$M	SPECULATIVE GRADE \$M		
Cash and cash equivalents	276	447	727	27	84	40	1,601
Interest-bearing investments	7,001	12,407	1,925	340	217	31	21,921
Derivative financial instruments	–	35	115	–	–	–	150

As at 31 December 2009

COMPANY	CREDIT RATING					NOT RATED \$M	TOTAL \$M
	Aaa \$M	Aa \$M	A \$M	Baa \$M	SPECULATIVE GRADE \$M		
Cash and cash equivalents	–	15	2	–	–	–	17
Interest-bearing investments	8	239	1	–	–	–	248
Derivative financial instruments	–	14	7	–	–	–	21
Amounts due from controlled entities	–	39	67	–	–	1,127	1,233

As at 31 December 2008

CONSOLIDATED	CREDIT RATING					NOT RATED \$M	TOTAL \$M
	Aaa \$M	Aa \$M	A \$M	Baa \$M	SPECULATIVE GRADE \$M		
Cash and cash equivalents	334	1,837	404	9	102	50	2,736
Interest-bearing investments	5,753	17,182	916	101	132	20	24,104
ABC financial assets pledged for funds at Lloyd's	–	191	59	–	–	–	250
Derivative financial instruments	33	704	130	–	–	–	867

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

5 FINANCIAL RISK CONTINUED

As at 31 December 2008

COMPANY	CREDIT RATING						TOTAL \$M
	Aaa \$M	Aa \$M	A \$M	Baa \$M	SPECULATIVE GRADE \$M	NOT RATED \$M	
Cash and cash equivalents	–	641	–	–	–	–	641
Interest-bearing investments	–	52	–	718	–	–	770
Derivative financial instruments	2	2	–	–	–	–	4
Amounts due from controlled entities	–	6	138	–	–	2,919	3,063

Details of credit risk in respect of reinsurance recoveries on outstanding claims are set out in note 4(B).

The carrying amount of the relevant asset classes in the balance sheet represents the maximum amount of credit exposure. The fair value of derivatives shown on the balance sheet represents the current risk exposure but not the maximum risk exposure that could arise in the future as a result of changing values. Further details are provided in note 12.

The following tables provide information regarding the ageing of the consolidated entity's and the company's financial assets that are past due but not impaired at the balance sheet date.

As at 31 December 2009

CONSOLIDATED	NEITHER PAST DUE NOR IMPAIRED ⁽¹⁾ \$M	PAST DUE BUT NOT IMPAIRED				TOTAL \$M
		0 TO 3 MTHS \$M	3 TO 6 MTHS \$M	6 MTHS TO 1 YEAR \$M	GREATER THAN 1 YEAR \$M	
Premium receivable	1,487	557	102	27	14	2,187
Other debtors	452	3	1	6	7	469
Treasury receivables	15	1	–	–	–	16
Investment receivables	134	4	–	–	–	138

(1) Includes \$2 million of treasury receivables relating to the company.

As at 31 December 2008

CONSOLIDATED	NEITHER PAST DUE NOR IMPAIRED ⁽¹⁾ \$M	PAST DUE BUT NOT IMPAIRED				TOTAL \$M
		0 TO 3 MTHS \$M	3 TO 6 MTHS \$M	6 MTHS TO 1 YEAR \$M	GREATER THAN 1 YEAR \$M	
Premium receivable	1,705	416	100	27	21	2,269
Other debtors	558	14	1	8	24	605
Treasury receivables	79	–	–	–	–	79
Investment receivables	275	2	2	5	–	284

(1) Includes \$9 million of treasury receivables and \$20 million of investment receivables relating to the company.

The company has amounts due from controlled entities of \$1,233 million (2008 \$3,063 million) which are neither past due nor impaired.

Details of the ageing of reinsurance and other recoveries on paid claims are set out in note 4(B).

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

5 FINANCIAL RISK CONTINUED

(C) Liquidity risk

In addition to treasury cash held for working capital requirements, and in accordance with the consolidated entity's liquidity policy, a minimum percentage of consolidated investments and cash is held in liquid, short-term money market securities to ensure that there are sufficient liquid funds available to meet insurance and investment obligations. The consolidated entity has a strong liquidity position. At 31 December 2009, the average duration of cash and fixed interest securities was 0.5 years (2008 0.5 years).

The consolidated entity limits the risk of liquidity shortfalls resulting from mismatches in the timing of claims payments and receipts of claims recoveries by negotiating cash call clauses in reinsurance contracts and seeking accelerated settlements for large claims.

The following tables summarise the contractual maturity profile of certain financial liabilities of the consolidated entity and the company based on the remaining undiscounted contractual obligations. The maturity profile of borrowings is included in note 24.

As at 31 December 2009

CONSOLIDATED	1 YEAR OR LESS ⁽¹⁾ \$M	1 TO 3 YEARS \$M	3 TO 5 YEARS \$M	OVER 5 YEARS \$M	NO TERM \$M	TOTAL \$M
Trade payables	680	40	3	3	3	729
Treasury payables	39	-	-	-	-	39
Investment payables	-	-	-	-	-	-

(1) Includes \$33 million of treasury payables relating to the company.

As at 31 December 2008

CONSOLIDATED	1 YEAR OR LESS ⁽¹⁾ \$M	1 TO 3 YEARS \$M	3 TO 5 YEARS \$M	OVER 5 YEARS \$M	NO TERM \$M	TOTAL \$M
Trade payables	856	54	2	1	9	922
Treasury payables	26	-	-	-	-	26
Investment payables	42	-	-	-	-	42

(1) Includes \$9 million of treasury payables relating to the company.

The company has amounts due to controlled entities of \$2,979 million (2008 \$2,528 million) which are repayable in one year or less.

The consolidated entity and the company have no significant concentration of liquidity risk.

The maturity profile of the consolidated entity's net outstanding claims provision is analysed in note 22. For the maturity profile of derivative financial instruments refer to note 12. For the maturity profile of ABC securities for funds at Lloyd's and the swaps relating to the ABC securities refer to note 34.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

6 REVENUE

	THE COMPANY		CONSOLIDATED	
	2009 \$M	2008 \$M	2009 \$M	2008 \$M
Premium revenue				
Direct and facultative	–	–	12,595	11,117
Inward reinsurance	–	–	1,479	1,736
	–	–	14,074	12,853
Other revenue				
Reinsurance and other recoveries	–	–	829	1,355
Interest and dividend income	996	1,481	749	1,102
Foreign exchange gains	26	–	365	409
	1,022	1,481	1,943	2,866
Net fair value gains on financial assets	–	24	460	–
Realised gains on sale of controlled entities	–	1	8	–
Investment income – ABC financial assets pledged for funds at Lloyd's	68	96	130	222
Revenue	1,090	1,602	16,615	15,941

7 PROFIT BEFORE INCOME TAX

(A) Profit before income tax (consolidated)

	NOTE	2009 \$M	2008 \$M
Gross written premium		14,455	13,142
Unearned premium movement		(381)	(289)
Gross earned premium		14,074	12,853
Outward reinsurance premium		(2,071)	(1,692)
Deferred reinsurance premium movement		146	(74)
Outward reinsurance premium expense		(1,925)	(1,766)
Net earned premium		12,149	11,087
Gross claims incurred		(8,157)	(7,743)
Reinsurance and other recoveries		829	1,355
Net claims incurred	9	(7,328)	(6,388)
Net commission		(1,972)	(1,909)
Other acquisition costs		(707)	(607)
Underwriting and other expenses ⁽¹⁾		(880)	(908)
		(10,887)	(9,812)
Underwriting profit		1,262	1,275
Investment income on policyholders' funds		802	908
Insurance profit		2,064	2,183
Investment income on shareholders' funds		435	269
Amortisation of intangibles and impairment of goodwill/intangibles		(67)	(32)
Profit before income tax		2,432	2,420

(1) Includes \$302 million (2008 \$104 million) of agency income earned by the consolidated entity's agency operations which is treated as a recovery of the consolidated entity's underwriting expenses.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

7 PROFIT BEFORE INCOME TAX CONTINUED

(B) Net investment and other income

	THE COMPANY		CONSOLIDATED	
	2009 \$M	2008 \$M	2009 \$M	2008 \$M
Dividends from controlled entities	935	1,427	–	–
Dividends from non-related entities	–	–	51	64
Interest received or receivable from controlled entities	14	42	–	–
Interest received or receivable from non-related entities	36	12	688	1,038
Other investment income	11	–	10	–
Investment and dividend income	996	1,481	749	1,102
Investment income – ABC financial assets pledged for funds at Lloyd's	68	96	130	222
Net realised (losses) gains – equities and investment properties	–	–	(366)	39
Net realised gains – fixed interest and other	2	2	280	205
Net unrealised gains (losses) – equities and investment properties	–	–	442	(593)
Net unrealised (losses) gains – fixed interest and other	(22)	22	13	13
Net unrealised losses on owner occupied properties	–	–	(29)	–
Realised gains on sale of controlled entities	–	1	8	–
Gain on sale of capital securities	7	–	–	–
Gain on repurchase of debt securities ⁽¹⁾	–	–	70	303
Foreign exchange gains ^(2,3)	26	–	365	409
Investment and other income	1,077	1,602	1,662	1,700
Expenses – ABC securities for funds at Lloyd's	(56)	(111)	(137)	(245)
Finance costs paid or payable to controlled entities	(34)	(36)	–	–
Finance costs paid or payable to non-related entities	(130)	(62)	(219)	(240)
Investment expenses	(5)	(1)	(69)	(38)
Impairment of investment in controlled entities ⁽⁴⁾	(15)	(2,410)	–	–
Foreign exchange losses	–	(30)	–	–
Net investment and other income	837	(1,048)	1,237	1,177
Investment income on policyholders' funds			802	908
Investment income on shareholders' funds			435	269
Net investment and other income			1,237	1,177

(1) Gains arose on the repurchase of capital securities and other QBE debt securities. Details are provided in note 24.

(2) 2009 realised foreign exchange gains include \$246 million arising following a change in the consolidated entity's approach to hedging its net investment in foreign operations.

(3) 2008 realised foreign exchange gains include \$380 million arising from forward foreign exchange contracts entered into to protect the consolidated entity's cash position against foreign currency volatility on the acquisition of QBE Lenders' Mortgage Insurance (Holdings) Pty Limited. This entity was acquired in October 2008 and the purchase price was payable in US dollars.

(4) These amounts arose due to Group restructuring in 2009 and 2008.

(C) Other expenses

	THE COMPANY		CONSOLIDATED	
	2009 \$M	2008 \$M	2009 \$M	2008 \$M
Commission	–	–	1,972	1,909
Other acquisition costs	–	–	707	607
Underwriting and other expenses	–	–	880	908
Investment expenses	5	1	69	38
Amortisation of intangibles and impairment of goodwill/intangibles	–	–	67	32
Foreign exchange losses	–	30	–	–
Other expenses	5	31	3,695	3,494

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

7 PROFIT BEFORE INCOME TAX CONTINUED

(D) Specific items

	THE COMPANY		CONSOLIDATED	
	2009 \$M	2008 \$M	2009 \$M	2008 \$M
Defined contribution superannuation plan expense	-	-	41	39
Payments on operating leases	-	-	93	101
Depreciation of property, plant and equipment	-	-	71	63

8 INCOME TAX

(A) Reconciliation of prima facie tax to income tax expense

	THE COMPANY		CONSOLIDATED	
	2009 \$M	2008 \$M	2009 \$M	2008 \$M
Profit (loss) before income tax	837	(1,048)	2,432	2,420
Prima facie tax payable (receivable) at 30%	251	(314)	730	726
Tax effect of permanent differences:				
Untaxed dividends	(281)	(429)	(11)	(14)
Differences in tax rates	-	1	(163)	(126)
Impairment of investment in controlled entities	5	720	-	-
Other, including non-allowable expenses and non-taxable income	20	8	(110)	(51)
Prima facie tax adjusted for permanent differences	(5)	(14)	446	535
Deferred tax asset no longer recognised	11	20	49	20
Underprovision (overprovision) in prior years	44	16	(47)	(1)
Income tax expense	50	22	448	554
Analysed as follows:				
Current tax	(38)	86	372	502
Deferred tax	44	(80)	123	53
Underprovision (overprovision) in prior years	44	16	(47)	(1)
	50	22	448	554
Deferred tax (credit) expense comprises ⁽¹⁾ :				
Deferred tax assets (credited) charged to income statement	(28)	(3)	57	(45)
Deferred tax liabilities charged (credited) to income statement	72	(77)	66	98
	44	(80)	123	53

(1) Consolidated deferred tax expense includes \$3 million (2008 \$1 million) credited to the income statement as a result of changes in income tax rates.

(B) Tax consolidation legislation

The accounting policy in relation to this legislation is set out in note 1(J).

On adoption of the tax consolidation legislation, the directors of the company and its Australian entities entered into a tax sharing and tax funding agreement that requires the Australian entities to fully compensate the company for current tax liabilities and to be fully compensated by the company for any current tax or deferred tax assets in respect of tax losses arising from external transactions occurring after the date of implementation of the tax consolidation legislation. The contributions are allocated by reference to the notional taxable income of each Australian entity.

Details of franking credits available to shareholders are shown in note 25(F).

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

9 CLAIMS INCURRED (CONSOLIDATED)

(A) Claims analysis

	2009 \$M	2008 \$M
Gross claims incurred and related expenses		
Direct and facultative	7,537	7,276
Inward reinsurance	620	467
	8,157	7,743
Reinsurance and other recoveries		
Direct and facultative	707	1,226
Inward reinsurance	122	129
	829	1,355
Net claims incurred	7,328	6,388

(B) Claims development

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

	2009			2008		
	CURRENT YEAR \$M	PRIOR YEARS \$M	TOTAL \$M	CURRENT YEAR \$M	PRIOR YEARS \$M	TOTAL \$M
Gross claims incurred and related expenses						
Undiscounted	8,784	(276)	8,508	9,284	(2,517)	6,767
Discount	(406)	55	(351)	(474)	1,450	976
	8,378	(221)	8,157	8,810	(1,067)	7,743
Reinsurance and other recoveries						
Undiscounted	742	58	800	1,859	(733)	1,126
Discount	(30)	59	29	(102)	331	229
	712	117	829	1,757	(402)	1,355
Net claims incurred						
Undiscounted	8,042	(334)	7,708	7,425	(1,784)	5,641
Discount	(376)	(4)	(380)	(372)	1,119	747
	7,666	(338)	7,328	7,053	(665)	6,388

The development of the net undiscounted central estimate of outstanding claims for the nine most recent accident years is shown in note 22(D). Note 9(C) is a reconciliation of the amounts included in the table above and the current financial year movements in the claims development table.

(C) Reconciliation of net claims incurred to claims development table

	2009			2008		
	CURRENT YEAR \$M	PRIOR YEARS \$M	TOTAL \$M	CURRENT YEAR \$M	PRIOR YEARS \$M	TOTAL \$M
Net undiscounted claims development – central estimate (note 22)	7,354	(79)	7,275	7,173	(371)	6,802
Acquisitions – central estimate	(94)	–	(94)	(282)	–	(282)
Foreign exchange	41	75	116	(218)	(163)	(381)
Movement in claims settlement costs	312	18	330	312	70	382
Movement in discount ⁽¹⁾	(376)	(4)	(380)	(372)	1,119	747
Movement in risk margin ⁽¹⁾	440	(402)	38	440	(1,272)	(832)
Other movements	(11)	54	43	–	(48)	(48)
Net claims incurred – discounted	7,666	(338)	7,328	7,053	(665)	6,388

(1) The 2008 prior accident year discount movement reflects the impact of the significant reduction in discount rates during the year on the consolidated entity's outstanding claims provision. \$819 million of discount unwind is offset by an equal and opposite movement in prior accident year risk margins.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

10 CASH AND CASH EQUIVALENTS

	THE COMPANY		CONSOLIDATED	
	2009 \$M	2008 \$M	2009 \$M	2008 \$M
Cash at bank and on hand	2	233	650	816
Overnight money	15	408	291	726
Cash management trusts	-	-	408	297
Term deposits	-	-	252	896
Commercial paper	-	-	-	1
	17	641	1,601	2,736

Cash and cash equivalents includes balances readily convertible to cash. All balances are held to service normal operational requirements. Included in cash and cash equivalents are amounts totalling \$264 million (2008 \$193 million) which are held in Lloyd's syndicate trust funds. Under Lloyd's bye-laws, these amounts can only be used to pay claims and allowable expenses of the syndicate and cannot be withdrawn from the trust funds until distributed as profit.

Amounts in cash and cash equivalents are the same as those included in the cash flow statement.

11 INVESTMENTS

	THE COMPANY		CONSOLIDATED	
	2009 \$M	2008 \$M	2009 \$M	2008 \$M
Interest-bearing				
Short-term money	248	52	11,548	16,885
Government bonds	-	-	1,417	1,992
Corporate bonds	-	718	2,978	1,823
Floating rate notes	-	-	5,846	3,245
Fixed interest trusts	-	-	132	159
	248	770	21,921	24,104
Equities				
Listed	-	-	1,492	1,523
Unlisted	-	-	52	66
Exchange traded equity derivatives	-	-	(45)	-
	-	-	1,499	1,589
Total investments	248	770	23,420	25,693
Amounts maturing within 12 months	248	52	13,728	18,071
Amounts maturing in greater than 12 months	-	718	9,692	7,622
Total investments	248	770	23,420	25,693

(A) Exchange traded equity derivatives

Contractual amounts for forward contracts at the balance sheet date were \$45 million payable (2008 \$nil). The credit risk arising from equity derivatives is \$nil (2008 \$nil). There were no amounts outstanding for purchased or written options (2008 \$nil).

(B) Charges over investments and other assets

A controlled entity has given fixed and floating charges over certain of its investments and other assets in order to secure the obligations of the consolidated entity's corporate members at Lloyd's of London as described in note 31. Details of the fixed and floating charges over ABC financial assets pledged for funds at Lloyd's are provided in note 34.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

11 INVESTMENTS CONTINUED

(C) Valuation of investments

All investments are initially recorded at fair value and are subsequently remeasured to fair value at each reporting date. Investments traded in an active market are valued with reference to the closing bid price. The significant majority of other investments, being fixed and floating rate securities, are valued using independently sourced valuations that do not involve the exercise of judgment by management. Less than 1% of investments are valued using accepted valuation practices such as discounted cash flow analysis and option pricing tools. Any reasonable changes in the inputs used to value these investments would not have a significant impact on the balance sheet.

The investments in the company and the consolidated entity are disclosed in the table below using a fair value hierarchy which reflects the significance of inputs into the determination of fair value as follows:

Fair value hierarchy

Level 1: valuation is based on quoted prices in active markets for the same instruments;

Level 2: valuation is based on quoted prices in active markets for similar assets or liabilities or other valuation techniques for which all significant inputs are based on observable market data (consensus price using broker quotes and valuation model with observable inputs); and

Level 3: valuation techniques are applied in which any significant input is not based on observable market data.

	LEVEL 1 \$M	LEVEL 2 \$M	LEVEL 3 \$M	2009 TOTAL \$M
Short-term money	961	10,587	–	11,548
Government bonds	350	1,067	–	1,417
Corporate bonds	–	2,944	34	2,978
Floating rate notes	–	5,816	30	5,846
Fixed interest trusts	30	102	–	132
Equities – listed	1,492	–	–	1,492
Equities – unlisted	–	–	52	52
Exchange traded equity derivatives	(45)	–	–	(45)
Total investments	2,788	20,516	116	23,420

Short-term money in the company of \$248 million meets the level 1 valuation criteria.

(D) Movements in level 3 investments

The following table provides an analysis of investments valued with reference to level 3 inputs.

	2009 \$M
LEVEL 3	
At 1 January	106
Purchases	29
Unrealised losses in income statement	(5)
Foreign exchange	(14)
At 31 December	116

(E) Restrictions on use

Included in short-term money are amounts totalling \$2,081 million (2008 \$3,651 million) which are held in Lloyd's syndicate trust funds. Under Lloyd's bye-laws, these amounts can only be used to pay claims and allowable expenses of the syndicate and cannot be withdrawn from the trust funds until distributed as profit.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

12 DERIVATIVE FINANCIAL INSTRUMENTS

(A) Fair value

	THE COMPANY		CONSOLIDATED	
	2009 \$M	2008 \$M	2009 \$M	2008 \$M
Assets maturing within 12 months				
Forward foreign exchange contracts	21	4	47	762
Eurobond swaps	-	-	103	-
Assets maturing in greater than 12 months				
Forward foreign exchange contracts	-	-	-	3
Eurobond swaps	-	-	-	102
	21	4	150	867
Liabilities maturing within 12 months				
Forward foreign exchange contracts	(13)	(209)	(40)	(1,119)
	8	(205)	110	(252)

Swaps relating to ABC securities are included in note 34 and equity derivatives are included in note 11(A).

All derivative positions entered into by the consolidated entity are for economic hedging purposes but do not, in all cases, meet the criteria for hedge accounting.

(B) Credit risk

Credit risk arises from the potential failure of counterparties to meet their obligations under the respective contracts at maturity. This arises on derivative financial instruments with unrealised gains. In the consolidated entity, \$150 million (2008 \$867 million) is receivable from forward foreign exchange contracts and Eurobond swaps at the balance sheet date.

(C) Forward foreign exchange contracts

Forward foreign exchange contracts are entered into by the consolidated entity for the purpose of managing residual foreign currency exposures. The consolidated entity's policy for managing such exposures is explained in note 5(A). In the consolidated entity, undiscounted contractual amounts to purchase \$4,824 million (2008 \$27,483 million) were outstanding at the balance sheet date. The maturity profile of these contracts is set out in the table below.

	THE COMPANY		CONSOLIDATED	
	2009 \$M	2008 \$M	2009 \$M	2008 \$M
Less than one year	2,053	1,823	4,824	27,471
More than one year but less than five years	-	-	-	12
	2,053	1,823	4,824	27,483

(D) Eurobond swaps

A controlled entity is exposed to cash flow interest rate and currency risk in respect of its three Eurobond financing arrangements. Accordingly, the consolidated entity has entered into swap agreements which result in the consolidated entity's Eurobond borrowings being fixed at sterling amounts until 2010, at which point the consolidated entity will be liable for the original Australian dollar and Euro amounts in the underlying financing arrangements. The facility can be extended for a further 10 years to 2020. Under the swap agreements, the variable interest rates of between 1.8% and 2.0% above the wholesale interbank rate are swapped to fixed rates of between 8.4% and 8.6% payable quarterly until 2010. The timing of the payments under the swap agreements matches the dates on which interest is payable on the underlying debt. The contracts are settled on a net basis.

The underlying borrowings are measured at amortised cost in original currency and translated to Australian dollars at the closing rate of exchange. The swaps are measured at fair value. The swaps are designated as cash flow hedges and have satisfied the relevant hedge effectiveness tests throughout the year and at the balance sheet date. The gain or loss on the cash flow hedges is recognised directly in equity. Any ineffectiveness in the cash flow hedges is recognised directly in the income statement. Each financial year end, until the close out of the swap agreements in 2010, an amount is transferred from equity to the income statement to offset:

- the differential between the fixed and variable interest payments; and
- the movement in the spot rate on the borrowings.

During the year, a gain of \$15 million (2008 \$82 million) was recognised in equity relating to the movements in the fair value of the swaps. During the year, a gain of \$9 million (2008 \$70 million) was transferred from equity and included in the income statement.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

12 DERIVATIVE FINANCIAL INSTRUMENTS CONTINUED

(E) Determination of fair value and fair value hierarchy

The consolidated entity's accounting policy in relation to the valuation of derivatives is set out in note 1(N). Derivatives are analysed in the table below using a fair value hierarchy which reflects the significance of inputs into the determination of fair value. The hierarchy is explained in more detail in note 11(C).

	LEVEL 1 \$M	LEVEL 2 \$M	LEVEL 3 \$M	2009 TOTAL \$M
Forward foreign exchange contracts	39	(32)	–	7
Eurobond swaps	–	103	–	103
Total	39	71	–	110

(F) Hedging arrangements

The following derivatives have been designated as hedges and meet the relevant requirements of AASB 139:

TYPE OF HEDGE	DESCRIPTION OF INSTRUMENT	NATURE OF RISKS	FAIR VALUE	
			2009 \$M	2008 \$M
Cash flow	Cross currency interest rate swaps – Eurobonds	Variability of functional currency cash flows due to interest rate and currency risk	103	102
Cash flow	Cross currency interest rate swaps – ABC securities (due 2009)	Variability of functional currency cash flows due to interest rate and currency risk	–	67
Net investments in foreign operations	Forward foreign exchange contracts	Currency risk	–	258

At the balance sheet date, \$825 million of borrowings were designated as hedges of net investments in foreign operations (2008 \$nil).

13 TRADE AND OTHER RECEIVABLES

	THE COMPANY		CONSOLIDATED	
	2009 \$M	2008 \$M	2009 \$M	2008 \$M
Trade debtors				
Premium receivable ⁽¹⁾	–	–	2,187	2,269
Reinsurance and other recoveries ⁽¹⁾	–	–	408	375
Unclosed premium	–	–	1,082	1,429
	–	–	3,677	4,073
Other debtors	1	–	469	605
Treasury receivables	2	9	16	79
Investment receivables	–	20	138	284
Amounts due from controlled entities	1,233	3,063	–	–
Trade and other receivables	1,236	3,092	4,300	5,041
Receivable within 12 months	1,236	3,060	4,222	4,972
Receivable in greater than 12 months	–	32	78	69
Trade and other receivables	1,236	3,092	4,300	5,041

(1) Net of a provision for impairment.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

13 TRADE AND OTHER RECEIVABLES CONTINUED

(A) Provision for impairment (consolidated)

	2009 \$M	2008 \$M
At 1 January	160	146
(Credit) charge for the year	(2)	5
Other movements	(12)	–
Foreign exchange	(24)	9
At 31 December	122	160

(B) Fair value

Due to the short-term nature of these receivables, their carrying value is assumed to approximate their fair value.

(C) Risk

The maximum exposure to credit risk at the reporting date is the fair value of each class of receivables. No receivables are pledged by the consolidated entity as collateral for liabilities or contingent liabilities. Information on the ageing and credit rating of balances in the table above, where relevant, is included in note 5. Note 5 also provides more information on the risk management policy of the consolidated entity.

14 DEFERRED INSURANCE COSTS (CONSOLIDATED)

	2009 \$M	2008 \$M
Deferred reinsurance premium	639	550
Deferred net commission	987	1,066
Deferred acquisition costs	329	371
Deferred insurance costs	1,955	1,987
To be expensed within 12 months	1,683	1,599
To be expensed in greater than 12 months	272	388
Deferred insurance costs	1,955	1,987

	DEFERRED NET COMMISSION		DEFERRED ACQUISITION COSTS	
	2009 \$M	2008 \$M	2009 \$M	2008 \$M
At 1 January	1,066	915	371	271
Acquisitions	18	10	11	54
Costs deferred in financial year	962	925	289	248
Reclassification	13	–	(13)	–
Amortisation of costs deferred in previous financial years	(951)	(822)	(293)	(209)
Foreign exchange	(121)	38	(36)	7
At 31 December	987	1,066	329	371

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

15 PROPERTY, PLANT AND EQUIPMENT (CONSOLIDATED)

	FREEHOLD BUILDINGS \$M	LEASEHOLD IMPROVEMENTS \$M	OFFICE EQUIPMENT/ FIXTURES & FITTINGS \$M	MOTOR VEHICLES \$M	TOTAL \$M
2009					
Cost or valuation					
At 1 January	284	112	310	14	720
Additions	3	14	50	2	69
Revaluations	(38)	-	-	-	(38)
Disposals	(5)	(4)	(18)	(3)	(30)
Foreign exchange	(45)	(10)	(53)	(2)	(110)
At 31 December	199	112	289	11	611
Accumulated depreciation and impairment losses					
At 1 January	-	31	178	6	215
Disposals	-	(3)	(16)	(3)	(22)
Depreciation charge for the year	-	12	56	3	71
Foreign exchange	-	(4)	(32)	(1)	(37)
At 31 December	-	36	186	5	227
Carrying amount					
At 31 December	199	76	103	6	384

	FREEHOLD BUILDINGS \$M	LEASEHOLD IMPROVEMENTS \$M	OFFICE EQUIPMENT/ FIXTURES & FITTINGS \$M	MOTOR VEHICLES \$M	TOTAL \$M
2008					
Cost or valuation					
At 1 January	245	113	270	13	641
Acquisitions	4	3	21	1	29
Additions	6	21	49	3	79
Revaluations	(8)	-	-	-	(8)
Disposals	(5)	(27)	(47)	(4)	(83)
Foreign exchange	42	2	17	1	62
At 31 December	284	112	310	14	720
Accumulated depreciation and impairment losses					
At 1 January	-	46	154	6	206
Disposals	-	(25)	(36)	(3)	(64)
Depreciation charge for the year	-	9	52	2	63
Foreign exchange	-	1	8	1	10
At 31 December	-	31	178	6	215
Carrying amount					
At 31 December	284	81	132	8	505

Principal owner occupied properties are valued annually by the directors effective 31 December based on independent valuations.

All owner occupied properties were valued on the basis of capitalisation of net market rentals allowing for costs of reletting, having regard to comparable on-market sales and discounted future cash flows.

In accordance with the consolidated entity's accounting policy, freehold buildings are measured at fair value. The cost of freehold buildings at 31 December 2009 was \$223 million (2008 \$271 million).

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

16 DEFERRED INCOME TAX

	THE COMPANY		CONSOLIDATED	
	2009 \$M	2008 \$M	2009 \$M	2008 \$M
Deferred tax assets	–	27	203	333
Deferred tax liabilities	(21)	–	(544)	(531)
	(21)	27	(341)	(198)

(A) Deferred tax assets – maturing in greater than 12 months

(i) The balance comprises temporary differences attributable to:

	THE COMPANY		CONSOLIDATED	
	2009 \$M	2008 \$M	2009 \$M	2008 \$M
Amounts recognised in the income statement				
Financial assets – fair value movements	–	–	53	150
Provision for impairment	–	–	14	16
Employee benefits	–	–	75	68
Defined benefit plans	–	–	8	9
Insurance provisions	–	–	455	443
Deferred tax losses recognised	55	24	162	221
Other	–	3	125	161
	55	27	892	1,068
Amounts recognised directly in equity				
Cash flow hedges	–	–	–	5
Capitalised expenses	10	14	7	11
Defined benefit plans	–	–	32	58
Employee share options	–	–	5	1
	10	14	44	75
	65	41	936	1,143
Set-off of deferred tax liabilities	(65)	(14)	(733)	(810)
	–	27	203	333

(ii) Movements:

	THE COMPANY		CONSOLIDATED	
	2009 \$M	2008 \$M	2009 \$M	2008 \$M
Balance at 1 January	41	27	1,143	740
Credited (charged) to the income statement	28	3	(57)	45
(Charged) credited to equity	(4)	11	(18)	44
Acquisitions	–	–	2	183
Foreign exchange	–	–	(134)	131
Balance at 31 December	65	41	936	1,143

(B) Tax losses

The consolidated entity has not brought to account \$80 million (2008 \$24 million) of tax losses, which includes the benefit arising from tax losses in overseas countries. This benefit will only be brought to account when the directors believe it is probable that it will be realised. This benefit of tax losses will only be obtained if:

- the consolidated entity derives future assessable income of a nature and an amount sufficient to enable the benefit from the deductions for the losses to be realised;
- the consolidated entity continues to comply with the conditions for deductibility imposed by tax legislation; and
- no changes in tax legislation adversely affect the consolidated entity in realising the benefit from the deductions for the losses.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

16 DEFERRED INCOME TAX CONTINUED

(C) Deferred tax liabilities – maturing in greater than 12 months

(i) The balance comprises temporary differences attributable to:

	THE COMPANY		CONSOLIDATED	
	2009 \$M	2008 \$M	2009 \$M	2008 \$M
Amounts recognised in the income statement				
Intangibles	–	–	(202)	(229)
Insurance provisions	–	–	(580)	(621)
Foreign currency monetary items	(85)	(6)	(86)	(21)
Financial assets – fair value movements	–	(7)	(118)	(163)
Other provisions	–	–	(82)	(104)
Other items	(1)	(1)	(186)	(180)
	(86)	(14)	(1,254)	(1,318)
Amounts recognised directly in equity				
Owner occupied property	–	–	(17)	(19)
Other	–	–	(6)	(4)
	(86)	(14)	(1,277)	(1,341)
Set-off of deferred tax assets	65	14	733	810
	(21)	–	(544)	(531)

(ii) Movements:

	THE COMPANY		CONSOLIDATED	
	2009 \$M	2008 \$M	2009 \$M	2008 \$M
Balance at 1 January	(14)	(91)	(1,341)	(997)
(Charged) credited to the income statement	(72)	77	(66)	(98)
Acquisitions	–	–	(10)	(194)
Foreign exchange	–	–	140	(52)
Balance at 31 December	(86)	(14)	(1,277)	(1,341)

17 INVESTMENT PROPERTIES (CONSOLIDATED)

	2009 \$M	2008 \$M
At 1 January	112	93
Additions	1	–
Disposals	–	(3)
Fair value (losses) gains	(21)	1
Foreign exchange	(22)	21
At 31 December	70	112

Investment properties are valued annually by the directors based on independent valuations.

All investment properties were valued on the basis of capitalisation of net market rentals allowing for costs of reletting, having regard to comparable on-market sales and discounted future cash flows. Investment properties are not expected to be realised within 12 months.

Rental income from investment properties was \$10 million (2008 \$9 million).

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

18 INVESTMENTS IN CONTROLLED ENTITIES

	COUNTRY OF INCORPORATION/ FORMATION	EQUITY HOLDING	
		2009 %	2008 %
(A) Parent entity			
QBE Insurance Group Limited	Australia		
(B) Controlled entities⁽¹⁾			
Affinity Insurance Services	US	100.00	100.00
ALS Green Slip Group Pty Limited	Australia	100.00	100.00
Anex Jenni & Partner AG	Switzerland	100.00	100.00
Atlasz Real Estate and Management Company Limited	Hungary	100.00	100.00
Austral Mercantile Collections Pty Limited	Australia	100.00	100.00
Australian Aviation Underwriting Pool Pty Limited	Australia	100.00	100.00
BCO Insurance Management Services Inc	US	100.00	100.00
BCO Surplus Lines Inc	US	100.00	100.00
Blue Ridge Indemnity Company	US	100.00	100.00
Blue Ridge Insurance Company	US	100.00	100.00
British Marine Holdings SA	Luxembourg	100.00	100.00
British Marine Holdings II SA	Luxembourg	100.00	100.00
British Marine Luxembourg SA	Luxembourg	100.00	100.00
British Marine Managers Limited	UK	100.00	100.00
BRO Enterprises LLC	US	100.00	100.00
Burnett & Company Inc	US	100.00	100.00
Burnett Holdings Inc	US	100.00	100.00
Burnett Insurance Agency	US	100.00	100.00
Capital City Insurance Company Inc	US	100.00	100.00
CHU Underwriting Agencies (UK) Limited	UK	100.00	100.00
CHU Underwriting Agencies Pty Limited	Australia	100.00	100.00
Community Association Underwriters of America Inc	US	100.00	100.00
Corporate Underwriting Agencies Pty Limited	Australia	100.00	100.00
Davis Garvin Agency Inc	US	100.00	100.00
Deep South of California Inc	US	100.00	100.00
Deep South Surplus Inc	US	100.00	100.00
Deep South Surplus of Texas Management LLC	US	100.00	100.00
Deep South Surplus of Texas LP ⁽²⁾	US	–	–
Elders Insurance (Underwriting Agency) Pty Limited	Australia	75.00	–
Elders Insurance Agencies Pty Limited	Australia	100.00	–
Elders Insurance Limited	Australia	100.00	–
Ensign Dedicated No.1 Limited	UK	100.00	100.00
Ensign Holdings Limited	UK	100.00	100.00
Equator Re (Australia) Limited	Bermuda	100.00	100.00
Equator Reinsurances Limited	Bermuda	100.00	100.00
FAI Insurances (Fiji) Limited	Fiji	100.00	100.00
General Casualty Company of Wisconsin	US	100.00	100.00
General Casualty Insurance Company	US	100.00	100.00
Greenhill Baia Underwriting GmbH	Germany	100.00	100.00
Greenhill International Insurance Holdings Limited	UK	100.00	100.00
Greenhill Sturge Underwriting Limited	UK	100.00	100.00
Greenhill Underwriting Espana Limited	UK	100.00	100.00
Hoosier Insurance Company	US	100.00	100.00
HP Jenni & Partner AG	Switzerland	100.00	100.00
Hyfield Company Limited ⁽²⁾	Thailand	49.00	49.00

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

18 INVESTMENTS IN CONTROLLED ENTITIES CONTINUED

	COUNTRY OF INCORPORATION/ FORMATION	EQUITY HOLDING	
		2009 %	2008 %
Invivo Medical Pty Limited	Australia	50.00	50.00
Iron Trades Management Services Limited	UK	100.00	100.00
Lifeco Re Limited	UK	100.00	–
Lifeco SRO	Czech Republic	100.00	–
Limit Corporate Members Limited	UK	100.00	100.00
Limit Holdings Limited	UK	100.00	100.00
Limit No 1 Limited	UK	100.00	100.00
Limit No 2 Limited	UK	100.00	100.00
Limit No 3 Limited	UK	100.00	100.00
Limit No 4 Limited	UK	100.00	100.00
Limit No 5 Limited	UK	100.00	100.00
Limit No 6 Limited	UK	100.00	100.00
Limit No 7 Limited	UK	100.00	100.00
Limit No 10 Limited	UK	100.00	100.00
Limit Properties Limited	UK	100.00	100.00
Mantis Reef II Limited ⁽⁹⁾	Cayman Is	–	–
Mantis Reef II Pledge Limited ⁽⁹⁾	Cayman Is	–	–
MBP Holdings Limited	UK	100.00	100.00
Minster Court Asset Management (UK) Limited	UK	100.00	100.00
Minster Court Asset Management Pty Limited	Australia	100.00	100.00
MMIA Pty Limited	Australia	100.00	100.00
MMWC Pty Limited	Australia	100.00	100.00
National Credit Insurance (Brokers) NZ Limited	NZ	100.00	100.00
National Credit Insurance (Brokers) Pty Limited	Australia	100.00	100.00
National Farmers Union Property and Casualty Company	US	100.00	100.00
North Pointe Casualty Insurance Company	US	100.00	100.00
North Pointe Financial Services Inc	US	100.00	100.00
North Pointe Insurance Company	US	100.00	100.00
NP Capital Trust 1 ⁽⁹⁾	US	–	–
Permanent LMI Pty Limited	Australia	50.10	50.10
Pitt Nominees Pty Limited	Australia	100.00	100.00
Praetorian Financial Group Inc	US	100.00	100.00
Praetorian Insurance Company	US	100.00	100.00
Praetorian Specialty Insurance Company	US	–	100.00
PT Asuransi QBE Pool Indonesia	Indonesia	60.00	60.00
QBE (PNG) Limited	PNG	100.00	100.00
QBE (Singapore) Pte Ltd	Singapore	100.00	100.00
QBE (Stafford) Limited	UK	100.00	100.00
QBE Americas Inc	US	100.00	–
QBE AS	Slovakia	100.00	100.00
QBE Aseguradora de Riesgos del Trabajo SA	Argentina	100.00	100.00
QBE Atlantic LLC	US	100.00	–
QBE Atlasz Ingatlankezelő zrt	Hungary	100.00	100.00
QBE Brasil Seguros SA	Brazil	99.90	100.00
QBE Capital Funding LP ⁽⁹⁾	Jersey	–	–
QBE Capital Funding LP II ⁽⁹⁾	Jersey	–	–
QBE Corporate Limited	UK	100.00	100.00
QBE de Mexico Compania de Seguros SA de CV	Mexico	100.00	100.00

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

18 INVESTMENTS IN CONTROLLED ENTITIES CONTINUED

	COUNTRY OF INCORPORATION/ FORMATION	EQUITY HOLDING	
		2009 %	2008 %
QBE Employee Share Trust ⁽³⁾	Australia	–	–
QBE Equities Pty Limited (in liquidation)	Australia	100.00	100.00
QBE European Underwriting Services (Australia) Pty Limited	Australia	100.00	100.00
QBE Europe Holdings Services Agent de Asigurare SRL	Romania	100.00	–
QBE Funding Limited	Jersey	100.00	100.00
QBE Funding II Limited	Jersey	100.00	100.00
QBE Funding III Limited	Jersey	100.00	100.00
QBE Funding IV Limited	Jersey	100.00	100.00
QBE Funding Trust ⁽³⁾	US	–	–
QBE Funding Trust II ⁽³⁾	US	–	–
QBE Funding Trust III ⁽³⁾	US	–	–
QBE Funding Trust IV ⁽³⁾	US	–	–
QBE Holdings (AAP) Pty Limited	Australia	100.00	100.00
QBE Holdings (Americas) Pty Limited	Australia	100.00	100.00
QBE Holdings (EO) Limited	UK	100.00	100.00
QBE Holdings (Europe) Limited	UK	100.00	100.00
QBE Holdings (UK) Limited	UK	100.00	100.00
QBE Holdings Inc	US	100.00	100.00
QBE Hongkong & Shanghai Insurance Limited	Hong Kong	74.47	74.47
QBE Hu KFT	Hungary	100.00	–
QBE Insurance (Australia) Limited	Australia	100.00	100.00
QBE Insurance (Europe) Limited	UK	100.00	100.00
QBE Insurance (Fiji) Limited	Fiji	100.00	100.00
QBE Insurance (International) Limited	Australia	100.00	100.00
QBE Insurance (Malaysia) Berhad	Malaysia	51.00	51.00
QBE Insurance (Philippines) Inc	Philippines	59.00	59.00
QBE Insurance (PNG) Limited	PNG	100.00	100.00
QBE Insurance (Thailand) Co Limited ⁽²⁾	Thailand		
Thai resident entities		23.67	23.67
Non-Thai resident entities		24.87	24.87
QBE Insurance (Vanuatu) Limited	Vanuatu	100.00	100.00
QBE Insurance (Vietnam) Company Limited	Vietnam	100.00	100.00
QBE Insurance Company (UK) Limited	UK	100.00	100.00
QBE Insurance Corporation	US	100.00	100.00
QBE International Holdings (UK) plc	UK	100.00	100.00
QBE International Holdings Limited	Hong Kong	100.00	100.00
QBE Investments (Australia) Pty Limited	Australia	100.00	100.00
QBE Investments (North America) Inc	US	100.00	100.00
QBE Investments (UK) Limited	NZ	100.00	100.00
QBE Investments Pty Ltd (in liquidation)	Australia	100.00	100.00
QBE Irish Share Incentive Plan ⁽³⁾	Ireland	–	–
QBE IT Services Pty Limited (in liquidation)	Australia	100.00	100.00
QBE (Jersey) GP Limited	Jersey	100.00	100.00
QBE (Jersey) GP II Limited	Jersey	100.00	100.00
QBE Kindlustuse Eesti AS (in liquidation)	Estonia	100.00	100.00
QBE Latin America Insurance Holdings SL	Spain	100.00	100.00
QBE Lenders' Mortgage Insurance (Holdings) Pty Limited	Australia	100.00	100.00
QBE Lenders' Mortgage Insurance Limited	Australia	100.00	100.00

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FOR THE YEAR ENDED 31 DECEMBER 2009

18 INVESTMENTS IN CONTROLLED ENTITIES CONTINUED

	COUNTRY OF INCORPORATION/ FORMATION	EQUITY HOLDING	
		2009 %	2008 %
QBE Makedonija ⁽⁴⁾	Macedonia	65.23	65.23
QBE Management (Ireland) Limited	Ireland	100.00	100.00
QBE Management Company (Bermuda) Limited	Bermuda	100.00	100.00
QBE Management Inc	US	100.00	100.00
QBE Management Services (Philippines) Pty Limited	Australia	100.00	100.00
QBE Management Services (UK) Limited	UK	100.00	100.00
QBE Management Services Pty Limited	Australia	100.00	100.00
QBE Marine and Energy Services Pte Limited	Singapore	100.00	100.00
QBE Marine Underwriting Agency Pte Limited	Singapore	70.00	70.00
QBE Mortgage Insurance (Asia) Limited	Hong Kong	100.00	100.00
QBE Nordic Aviation Insurance A/S	Denmark	100.00	100.00
QBE PL Sp ZOO	Poland	100.00	–
QBE Re Services Pty Limited	Australia	100.00	100.00
QBE Regional Companies (NA) Inc	US	100.00	100.00
QBE Reinsurance (Bermuda) Limited	Bermuda	100.00	100.00
QBE Reinsurance (Europe) Limited	Ireland	100.00	100.00
QBE Reinsurance (UK) Limited	UK	100.00	100.00
QBE Reinsurance Corporation	US	100.00	100.00
QBE Seguros SA	Colombia	97.58	97.55
QBE Services Inc	Canada	100.00	100.00
QBE SK SRO	Slovakia	100.00	–
QBE Specialty Insurance Company	US	100.00	100.00
QBE SRO	Czech Republic	100.00	–
QBE UK Finance I Limited	UK	100.00	100.00
QBE UK Finance II Limited	UK	100.00	100.00
QBE UK Finance III Limited	UK	100.00	–
QBE UK Finance IV Limited	UK	100.00	–
QBE UK Share Incentive Plan ⁽³⁾	UK	–	–
QBE Ukraine ⁽²⁾	Ukraine	50.00	50.00
QBE Underwriting Limited	UK	100.00	100.00
QBE Underwriting Services (Ireland) Limited	Ireland	100.00	100.00
QBE Underwriting Services (UK) Limited	UK	100.00	100.00
QBE Underwriting Services Limited	UK	100.00	100.00
QBE US Agencies Inc	US	100.00	100.00
QBE Workers Compensation (NSW) Limited	Australia	100.00	100.00
QBE Workers Compensation (SA) Limited	Australia	100.00	100.00
QBE Workers Compensation (VIC) Limited	Australia	100.00	100.00
QBEMM Pty Limited	Australia	100.00	100.00
Queensland Insurance (Investments) Limited	Fiji	100.00	100.00
Redland Insurance Company	US	100.00	100.00
Regent Insurance Company	US	100.00	100.00
Ridgwell Fox & Partners (Underwriting Management) Limited	UK	100.00	100.00
Sinkaonamahasarn Company Limited ⁽²⁾	Thailand	49.00	49.00
SIU LLC	US	100.00	100.00
SLG Benefits and Insurance LLC	US	100.00	–
Southern Fire & Casualty Company	US	100.00	100.00
Southern Guaranty Insurance Company	US	100.00	100.00
Southern Pilot Insurance Company	US	100.00	100.00
Southern National Risk Management Inc	US	100.00	100.00
SRL Underwriting Limited	UK	100.00	100.00

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FOR THE YEAR ENDED 31 DECEMBER 2009

18 INVESTMENTS IN CONTROLLED ENTITIES CONTINUED

	COUNTRY OF INCORPORATION/ FORMATION	EQUITY HOLDING	
		2009 %	2008 %
Stahl Intermediaries Inc	US	100.00	100.00
Standfast Corporate Underwriters Limited	UK	100.00	100.00
Star Trust ⁽⁹⁾	Cayman Is	–	–
Strakh-Consult (in liquidation)	Ukraine	100.00	100.00
The MiniBus & Coach Club Limited	UK	100.00	100.00
Torch Dedicated Corporate Member Limited	UK	100.00	100.00
Travelon Pty Limited	Australia	100.00	100.00
Underwriting Agencies of Australia (Holdings) Pty Limited	Australia	90.00	90.00
Underwriting Agencies of Australia Pty Limited	Australia	90.00	90.00
Unigard Indemnity Company	US	100.00	100.00
Unigard Insurance Company	US	100.00	100.00
United Security Insurance Company	US	100.00	100.00
Universal Underwriting Agencies Pty Limited	Australia	100.00	100.00
Visionex 2000 Limited	UK	100.00	100.00
Westwood Insurance Agency	US	100.00	100.00
ZC Real Estate Tax Solutions Limited	US	100.00	100.00
ZC Sterling Corporation	US	100.00	100.00
ZC Sterling Insurance Agency Inc	US	100.00	100.00

(1) All controlled entities have a 31 December year end.

(2) The following special conditions exist with respect to the consolidated entity's equity holdings:

- For accounting purposes, the consolidated entity has management control of QBE Insurance (Thailand) Co Limited and QBE Ukraine.
- The issued share capital of Hyfield Company Limited and Sinkaonamahasarn Company Limited owned by the consolidated entity is held by various controlled entities. Other controlled entities have the right to acquire the remaining share capital.

(3) Deep South Surplus of Texas LP, Mantis Reef II Limited, Mantis Reef II Pledge Limited, NP Capital Trust 1, QBE Employee Share Trust, QBE Irish Share Incentive Plan, QBE UK Share Incentive Plan, Star Trust, the QBE Funding Trusts, QBE Capital Funding LP and QBE Capital Funding LP II have been included in the consolidated financial statements as these entities are special purpose entities that exist for the benefit of the consolidated entity.

(4) The shareholding in QBE Makedonija equates to 73.50% (2008 73.50%) of the voting rights.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

18 INVESTMENTS IN CONTROLLED ENTITIES CONTINUED

(C) Change of name

CONTROLLED ENTITY	FORMER NAME
QBE AS	QBE Poistovna AS
QBE Atlasz Ingatlankezelo zrt	Stefania Biztosito zrt
QBE Hu KFT	Carlife KFT
QBE SK SRO	Carlife SK SRO
QBE SRO	Carlife Direct SRO
QBE Europe Holdings Services Agent de Asigurare SRL	Carlife SRL
QBE PL Sp ZOO	Carlife Sp ZOO
Stefania Biztosito zrt	QBE Atlasz Biztosito zrt

(D) Minority interest in controlled entities (consolidated)

	2009 \$M	2008 \$M
Ordinary share capital	53	52
Reserves	(15)	1
Retained profits	38	33
	76	86

(E) Equity

All equity in controlled entities is held in the form of shares or through contractual arrangements.

(F) Acquisitions

The following entities were acquired during the financial year:

On 28 February 2009, a wholly-owned entity acquired the entire share capital of Lifeco SRO which owns the Carlife group of companies in Eastern Europe. The purchase price was \$11 million including contingent consideration of \$4 million, for net tangible liabilities of \$2 million.

On 1 July 2009, a wholly-owned entity acquired the entire share capital of SLG Benefits and Insurance LLC, an underwriting agency in the US. The purchase price was \$US29 million including contingent consideration of \$US10.8 million, for net tangible assets of US\$1.5 million.

On 30 September 2009, a wholly-owned entity acquired the entire share capital of Elders Insurance Group and 75% of Elders Insurance (Underwriting Agency) Pty Limited, a joint venture company between QBE and Elders Limited. The purchase price was \$270 million for net tangible assets of \$85 million.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

18 INVESTMENTS IN CONTROLLED ENTITIES CONTINUED

The fair value of assets and liabilities arising from acquisitions in the year ended 31 December 2009 and final fair values of assets and liabilities arising from acquisitions in the year ended 31 December 2008 are as follows:

	2009			2008 ⁽¹⁾		
	ELDERS \$M	OTHERS \$M	TOTAL \$M	ZCS \$M	LMI \$M	DEEP SOUTH \$M
Cash and cash equivalents	204	9	213	306	27	38
Investments	–	–	–	–	1,529	–
Trade and other receivables	237	3	240	85	90	21
Reinsurance and other recoveries on outstanding claims	83	–	83	–	–	–
Current tax assets	4	–	4	7	22	–
Other assets	–	–	–	9	–	–
Deferred insurance costs	139	–	139	–	54	–
Property, plant and equipment	–	–	–	16	3	3
Deferred tax assets	2	–	2	–	160	–
Intangible assets	34	–	34	314	32	50
Total assets	703	12	715	737	1,917	112
Trade and other payables	110	11	121	391	94	77
Unearned premium	251	–	251	–	693	–
Outstanding claims	212	–	212	–	518	–
Provisions	1	1	2	–	1	–
Deferred tax liabilities	10	–	10	153	–	1
Borrowings	–	–	–	145	–	–
Total liabilities	584	12	596	689	1,306	78
Net assets acquired	119	–	119	48	611	34

	2009			2008 ⁽¹⁾		
	ELDERS \$M	OTHERS \$M	TOTAL \$M	ZCS \$M	LMI \$M	DEEP SOUTH \$M
Purchase consideration						
Cash	270	29	299	899	1,115	160
Contingent and deferred consideration	–	18	18	264	252	–
Direct costs relating to the acquisition	–	–	–	–	7	–
Total purchase consideration	270	47	317	1,163	1,374	160
Fair value of net assets acquired	119	–	119	48	611	34
Minority interest in net assets acquired	–	–	–	–	(7)	–
Goodwill acquired	151	47	198	1,115	770	126

(1) Information relates to the final assessment of the fair value of net assets acquired in respect of 2008 acquisitions declared provisional at the 2008 balance date.

The above information is presented at the exchange rates prevailing at the date of the acquisitions.

The goodwill is attributable to the future profitability of the acquisitions and the synergies expected to arise within the consolidated entity.

The acquired businesses contributed premium revenue of \$129 million and net profit after income tax of \$19 million to the consolidated entity for the period from acquisition to 31 December 2009.

If the acquisitions had occurred on 1 January 2009, consolidated gross earned premium and consolidated net profit after income tax for the year ended 31 December 2009 would have been \$14,397 million and \$1,974 million respectively.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

18 INVESTMENTS IN CONTROLLED ENTITIES CONTINUED

The fair value of assets and liabilities arising from acquisitions in the year ended 31 December 2008 are as follows:

2008	ZCS \$M	LMI \$M	NORTH POINTE \$M	DEEP SOUTH \$M	OTHER \$M	TOTAL \$M
Cash and cash equivalents	306	27	47	38	56	474
Investments	–	1,529	235	–	111	1,875
Trade and other receivables	76	90	45	42	97	350
Reinsurance and other recoveries on outstanding claims	–	–	59	–	–	59
Current tax assets	–	22	10	–	–	32
Other assets	18	–	–	–	2	20
Deferred insurance costs	–	54	19	–	4	77
Property, plant and equipment	16	3	5	3	2	29
Deferred tax assets	–	166	15	–	2	183
Intangible assets	314	32	17	50	42	455
Total assets	730	1,923	452	133	316	3,554
Trade and other payables	386	94	40	77	69	666
Current tax liabilities	–	–	–	–	12	12
Unearned premium	–	693	67	–	31	791
Outstanding claims	–	518	242	–	13	773
Provisions	–	1	–	–	1	2
Deferred tax liabilities	170	–	–	2	22	194
Borrowings	145	–	43	–	–	188
Total liabilities	701	1,306	392	79	148	2,626
Net assets acquired	29	617	60	54	168	928

2008	ZCS \$M	LMI \$M	NORTH POINTE \$M	DEEP SOUTH \$M	OTHER \$M	TOTAL \$M
Purchase consideration						
Cash	878	1,100	151	160	368	2,657
Contingent consideration	490	–	–	54	80	624
Direct costs relating to the acquisition	–	21	1	–	1	23
Total purchase consideration	1,368	1,121	152	214	449	3,304
Fair value of net assets acquired	29	617	60	54	168	928
Minority interest in net assets acquired	–	(7)	–	–	(4)	(11)
Goodwill acquired	1,339	511	92	160	285	2,387

The above information is presented at the exchange rates prevailing at the date of the acquisitions.

(G) Joint venture

On 19 July 2007, the consolidated entity entered into a joint venture agreement with Rajan Raheja Group to form Raheja QBE General Insurance Company. The consolidated entity has a 26% ownership interest in the joint venture. The consolidated entity's share of gross premium written by this entity in 2009 was not material. No business was written by this operation in 2008.

(H) Disposal

Praetorian Specialty Insurance Company was sold on 17 February 2009, realising a gain on disposal of \$8 million.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

19 INTANGIBLE ASSETS (CONSOLIDATED)

	IDENTIFIABLE INTANGIBLES						GOODWILL	TOTAL
	LLOYD'S SYNDICATE CAPACITY \$M	RENEWAL RIGHTS/ DISTRIBUTION CHANNELS \$M	BRAND NAMES \$M	INSURANCE LICENCES \$M	SOFTWARE \$M	OTHER \$M	\$M	\$M
2009								
Cost								
At 1 January	115	710	36	69	60	18	4,648	5,656
Acquisitions	-	22	12	-	-	-	198	232
Additions/reclassifications	-	29	4	2	(4)	-	44	75
Foreign exchange	(18)	(139)	(8)	(16)	(11)	(2)	(634)	(828)
At 31 December	97	622	44	55	45	16	4,256	5,135
Amortisation								
At 1 January	-	(50)	-	-	(11)	(9)	-	(70)
Amortisation for the year	-	(53)	(1)	-	(9)	(2)	-	(65)
Impairment	-	(2)	-	-	-	-	-	(2)
Foreign exchange	-	12	-	-	3	1	-	16
At 31 December	-	(93)	(1)	-	(17)	(10)	-	(121)
Carrying amount								
At 31 December	97	529	43	55	28	6	4,256	5,014

	IDENTIFIABLE INTANGIBLES						GOODWILL	TOTAL
	LLOYD'S SYNDICATE CAPACITY \$M	RENEWAL RIGHTS/ DISTRIBUTION CHANNELS \$M	BRAND NAMES \$M	INSURANCE LICENCES \$M	SOFTWARE \$M	OTHER \$M	\$M	\$M
2008								
Cost								
At 1 January	127	233	24	48	23	13	2,056	2,524
Acquisitions	-	405	6	7	32	5	2,387	2,842
Additions/reclassifications	-	25	-	-	-	-	(3)	22
Foreign exchange	(12)	47	6	14	5	-	208	268
At 31 December	115	710	36	69	60	18	4,648	5,656
Amortisation								
At 1 January	-	(20)	-	-	(3)	(8)	-	(31)
Amortisation for the year	-	(25)	-	-	(6)	(1)	-	(32)
Foreign exchange	-	(5)	-	-	(2)	-	-	(7)
At 31 December	-	(50)	-	-	(11)	(9)	-	(70)
Carrying amount								
At 31 December	115	660	36	69	49	9	4,648	5,586

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

19 INTANGIBLE ASSETS (CONSOLIDATED) CONTINUED

(A) Identifiable intangibles

Lloyd's syndicate capacity, insurance licences and brand names are generally considered to have an indefinite useful life and no amortisation is charged. All remaining intangible assets are amortised over their finite useful lives and the amortisation charge is included in amortisation and impairment of goodwill/intangibles in the income statement. The most significant classes of intangible assets are as follows:

(i) Lloyd's syndicate capacity

The Lloyd's syndicate capacity relates to the syndicate capacity acquired as part of the acquisition of QBE Underwriting Limited (formerly trading as Limit) in 2000 and costs incurred as a result of increasing capacity since that date. The consolidated entity has demonstrated a long-term commitment to developing its operations at Lloyd's. Since acquiring QBE Underwriting Limited, the consolidated entity has increased its share of ownership for all syndicates from 55% in 2000 to 91% for the 2009 underwriting year. The value of this asset is in the access it gives to future underwriting profits at Lloyd's. For these reasons Lloyd's syndicate capacity is deemed to have an indefinite useful life.

(ii) Renewal rights/distribution channels

This is the capitalisation of future profits relating to insurance contracts acquired and the expected renewal of those contracts. It also includes the value of the distribution network. Renewal rights and distribution channels are amortised over lives of between five and 21 years depending on the classes of business to which the rights relate.

(iii) Brand names

This asset reflects the revenue generating ability of acquired brands. Brand names are generally considered to have an indefinite useful life due to the long-term nature of this asset. When there is a contractual limit on the use of the brand name, the asset is amortised over the relevant period, being 20 years.

(iv) Insurance licences

This asset gives the consolidated entity the right to operate in certain geographic locations and to write certain classes of business with a potential to generate additional revenue. It is considered to have an indefinite useful life due to its long-term nature.

(v) Software

This is the fair value of key operating systems acquired in business combinations which will benefit the future operations of the acquired entity. Capitalised software is amortised over periods ranging from four to 15 years, reflecting the period during which the consolidated entity is expected to benefit from the use of the software.

(B) Goodwill

Goodwill is allocated to cash generating units being the lowest level at which there are separately identifiable cash flows relating to the goodwill. As the consolidated entity continues to acquire operations and reorganise the way that operations are managed, reporting structures may change giving rise to a reassessment of cash generating units.

The goodwill relating to certain acquisitions outside Australia is denominated in currencies other than the Australian dollar and so is subject to foreign exchange movements.

Goodwill is allocated to cash generating units as follows:

	2009 \$M	2008 \$M
Australian operations	892	747
QBE Insurance Europe	257	284
Lloyd's division	237	238
North American operations	2,059	2,821
QBE LMI	770	511
Other	41	47
	4,256	4,648

(C) Impairment testing of intangible assets

The consolidated entity's accounting policy in respect of impairment testing of intangible assets is set out in note 1(V). The recoverable amount of each cash generating unit is determined by reference to a value in use calculation based on the following key assumptions and estimates:

- discounted cash flow projections for a five year period are included in the calculation. This information is extracted from the latest three year business plan which has been presented to and approved by the board;
- projections for years four and five are based on the final year of the three year business plan assuming growth of 2.5% per annum;
- discount rates are pre-tax and reflect a beta and equity risk premium appropriate to the consolidated entity; and
- terminal value is calculated using a perpetuity growth formula based on the cash flow forecast for year five and an appropriate discount rate and terminal growth rate.

The discount rates used to value cash generating units at 31 December 2009 were in a range of 10.5% to 15.7% (31 December 2008 range of 10.1% to 13.2%).

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

20 TRADE AND OTHER PAYABLES

	THE COMPANY		CONSOLIDATED	
	2009 \$M	2008 \$M	2009 \$M	2008 \$M
Trade payables	-	-	729	922
Amounts due to controlled entities	2,979	2,528	-	-
Other payables and accrued expenses	11	145	546	1,004
Treasury payables	33	9	39	26
Investment payables	-	-	-	42
Trade and other payables	3,023	2,682	1,314	1,994
Payable within 12 months	3,023	2,682	1,272	1,915
Payable in greater than 12 months	-	-	42	79
Trade and other payables	3,023	2,682	1,314	1,994

21 UNEARNED PREMIUM (CONSOLIDATED)

(A) Unearned premium

	2009 \$M	2008 \$M
At 1 January	7,126	5,698
Acquisitions/disposals	220	791
Deferral of premium on contracts written in the period	6,349	6,333
Earning of premium written in previous periods	(5,889)	(6,000)
Foreign exchange	(971)	304
At 31 December	6,835	7,126
To be earned within 12 months	6,148	6,289
To be earned in greater than 12 months	687	837
Unearned premium	6,835	7,126

(B) Net premium liabilities

	NOTE	2009 \$M	2008 \$M
Unearned premium		6,835	7,126
Deferred insurance costs	14	(1,955)	(1,987)
Net premium liabilities		4,880	5,139

(C) Expected present value of future cash flows for future claims including risk margin

	2009 \$M	2008 \$M
Undiscounted central estimate	4,350	4,482
Risk margin	176	200
	4,526	4,682
Discount to present value	(461)	(308)
Expected present value of future cash flows for future claims including risk margin	4,065	4,374

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

21 UNEARNED PREMIUM (CONSOLIDATED) CONTINUED

(D) Liability adequacy test

The probability of adequacy applied in the liability adequacy test differs from the probability of adequacy adopted in determining the outstanding claims provision. The reason for the difference is that the former is a benchmark used only to test the sufficiency of net premium liabilities whereas the latter is a measure of the adequacy of the outstanding claims provision actually carried by the consolidated entity.

AASB 1023 requires the inclusion of a risk margin in insurance liabilities, but does not prescribe a minimum level of margin. Whilst there is established practice in the calculation of the probability of adequacy of the outstanding claims provision, no such guidance exists in respect of the level of risk margin to be used in determining the adequacy of net premium liabilities. The consolidated entity has adopted a risk margin for the purpose of the liability adequacy test to produce a 75% probability of adequacy in respect of total insurance liabilities. The 75% basis is a recognised industry benchmark in Australia, being the minimum probability of adequacy required for Australian licensed insurers by APRA.

The application of the liability adequacy test in respect of the net premium liabilities identified a surplus at 31 December 2009 and 2008.

(E) Risk margin

The process used to determine the risk margin is explained in note 3(A)(iii).

The risk margin in expected future cash flows for future claims as a percentage of the central estimate is 4.5% (2008 4.8%). This is the risk margin required to give a probability of adequacy of 75% for total insurance liabilities.

22 OUTSTANDING CLAIMS (CONSOLIDATED)

(A) Net outstanding claims

	2009 \$M	2008 \$M
Gross outstanding claims	19,153	22,059
Claims settlement costs	461	531
	19,614	22,590
Discount to present value	(1,581)	(1,386)
Gross outstanding claims provision	18,033	21,204
Less than 12 months	6,258	7,240
Greater than 12 months	11,775	13,964
Gross outstanding claims provision	18,033	21,204
Reinsurance and other recoveries on outstanding claims ⁽¹⁾	3,942	5,394
Discount to present value	(259)	(351)
Reinsurance and other recoveries on outstanding claims	3,683	5,043
Less than 12 months	1,503	1,713
Greater than 12 months	2,180	3,330
Reinsurance and other recoveries on outstanding claims	3,683	5,043
Net outstanding claims	14,350	16,161
Central estimate	13,216	14,962
Risk margin	1,134	1,199
Net outstanding claims	14,350	16,161

(1) Reinsurance and other recoveries on outstanding claims is shown net of a provision for impairment of \$48 million (2008 \$64 million).

The expected maturity of the consolidated entity's discounted net outstanding claims provision is analysed below.

		1 YEAR OR LESS	1 TO 2 YEARS	2 TO 3 YEARS	3 TO 4 YEARS	4 TO 5 YEARS	OVER 5 YEARS	TOTAL
At 31 December 2009	\$M	4,755	3,080	1,971	1,380	940	2,224	14,350
At 31 December 2008	\$M	5,527	3,480	2,239	1,567	1,029	2,319	16,161

The weighted average term to settlement of the consolidated entity's net outstanding claims provision at the balance sheet date is 2.8 years (2008 2.7 years).

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

22 OUTSTANDING CLAIMS CONTINUED

(B) Risk margin

The process used to determine the risk margin is explained in note 3(A)(iii) and details of the risk-free discount rates adopted are set out in note 3(A)(vi).

The probability of adequacy at 31 December 2009 is 88.1% (2008 86.1%) which is well above APRA's 75% benchmark. The risk margin included in net outstanding claims is 8.6% (2008 8.0%) of the central estimate.

(C) Reconciliation of movement in discounted outstanding claims provision

	2009			2008		
	GROSS \$M	REINSURANCE \$M	NET \$M	GROSS \$M	REINSURANCE \$M	NET \$M
At 1 January	21,204	(5,043)	16,161	18,231	(4,360)	13,871
Increase in net claims incurred in current accident year	8,378	(712)	7,666	8,810	(1,757)	7,053
Movement in prior year claims provision	(221)	(117)	(338)	(1,067)	402	(665)
Incurred claims recognised in the income statement	8,157	(829)	7,328	7,743	(1,355)	6,388
Acquisitions/disposals	79	50	129	773	(59)	714
Claim payments	(8,434)	1,405	(7,029)	(7,651)	1,396	(6,255)
Foreign exchange	(2,973)	734	(2,239)	2,108	(665)	1,443
At 31 December	18,033	(3,683)	14,350	21,204	(5,043)	16,161

(D) Claims development – undiscounted net central estimate

	2000 & PRIOR \$M	2001 \$M	2002 \$M	2003 \$M	2004 \$M	2005 \$M	2006 \$M	2007 \$M	2008 \$M	2009 \$M	TOTAL \$M
Net claims cost – central estimate:											
At end of accident year	3,133	2,659	2,829	3,898	4,435	3,910	7,782	7,373	7,354		
One year later	3,181	2,588	2,628	3,650	4,493	3,858	7,530	7,397			
Two years later	3,279	2,591	2,482	3,463	4,205	3,783	7,621				
Three years later	3,386	2,605	2,433	3,443	4,207	3,743					
Four years later	3,476	2,602	2,350	3,302	4,215						
Five years later	3,374	2,590	2,357	3,288							
Six years later	3,420	2,617	2,359								
Seven years later	3,434	2,593									
Eight years later	3,323										
Current central estimate cost for the nine most recent accident years	3,323	2,593	2,359	3,288	4,215	3,743	7,621	7,397	7,354		
Cumulative net claims payments to date	(3,060)	(2,345)	(2,128)	(2,710)	(3,507)	(2,768)	(4,931)	(4,341)	(2,235)		
Net undiscounted central estimate	1,070	263	248	231	578	708	975	2,690	3,056	5,119	14,938
Foreign exchange											(926)
Net undiscounted central estimate at 31 December 2009											14,012
Discount to present value											(1,322)
Risk margin											1,134
Claims settlement costs											461
Other											65
Net outstanding claims at 31 December 2009											14,350
Net central estimate development											
Increase (decrease) in the year – current year minus prior year	(15)	(111)	(24)	2	(14)	8	(40)	91	24	7,354	7,275

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

22 OUTSTANDING CLAIMS (CONSOLIDATED) CONTINUED

A reconciliation of the net central estimate development in the previous table to the net incurred claims in the income statement, analysed between current and prior accident years, is included in note 9(C).

The consolidated entity writes business in currencies other than the Australian dollar in its overseas operations. The translation of outstanding claims denominated in foreign currencies gives rise to foreign exchange movements which have no direct bearing on the development of the underlying claims. To eliminate this distortion, claims liabilities have been translated to the functional currencies of our overseas operations at constant rates of exchange. All estimates of net central estimate claims cost and cumulative claims payments for the nine most recent accident years reported in functional currencies other than Australian dollars have been translated to Australian dollars using the 2009 cumulative average rate of exchange.

The central estimate claims development table is presented net of reinsurance. With operations in 47 countries, hundreds of products, various reinsurance arrangements and with the consolidated entity's risk tolerance managed on a consolidated net basis, it is not considered meaningful or practicable to provide this information other than on a consolidated net accident year basis.

Outstanding claims in respect of acquisitions are included in the net central estimate claims cost in the accident year in which the acquisition was made. The exception is increased participation in Lloyd's syndicates where the increased share of the central estimate of the outstanding claims provision is allocated to the original accident year.

23 PROVISIONS (CONSOLIDATED)

	PROVISION FOR LONG SERVICE LEAVE \$M	AMOUNTS PAYABLE UNDER ACQUISITION AGREEMENTS \$M	OTHER PROVISIONS \$M	TOTAL PROVISIONS \$M
2009				
At 1 January	28	613	73	714
Cash payments	–	(11)	(3)	(14)
Amounts charged (credited) to the income statement	2	–	1	3
Other movement	–	1	(21)	(20)
Acquisitions/disposals	1	18	1	20
Foreign exchange	–	(100)	(5)	(105)
At 31 December	31	521	46	598
Payable within 12 months	24	170	8	202
Payable in greater than 12 months	7	351	38	396
At 31 December	31	521	46	598

	PROVISION FOR LONG SERVICE LEAVE \$M	AMOUNTS PAYABLE UNDER ACQUISITION AGREEMENTS \$M	OTHER PROVISIONS \$M	TOTAL PROVISIONS \$M
2008				
At 1 January	22	12	33	67
Amounts charged to the income statement	4	–	–	4
Other movement	2	–	35	37
Acquisitions	–	624	2	626
Disposals	–	–	(2)	(2)
Foreign exchange	–	(23)	5	(18)
At 31 December	28	613	73	714
Payable within 12 months	17	–	25	42
Payable in greater than 12 months	11	613	48	672
At 31 December	28	613	73	714

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

24 BORROWINGS

(A) Analysis of borrowings

		THE COMPANY		CONSOLIDATED	
		2009	2008	2009	2008
		\$M	\$M	\$M	\$M
Repayable as follows:					
Bank loans	Principal amount				
13 March 2009	A\$100 million	–	100	–	100
24 March 2009	A\$200 million	–	200	–	200
1 April 2009	US\$21 million	–	–	–	28
22 April 2009	A\$200 million	–	200	–	200
30 April 2009	US\$50 million	–	–	–	70
17 June 2009	US\$2 million	–	–	–	3
30 June 2011	US\$2.5 million	–	–	2	3
15 March 2036	US\$20 million	–	–	22	28
		–	500	24	632
Senior debt					
28 September 2009	£nil (2008 £175 million)	–	363	–	363
14 March 2014	US\$211 million	233	298	233	298
14 March 2014	£191 million	340	394	340	394
28 September 2015	£550 million	985	–	985	–
		1,558	1,055	1,558	1,055
Eurobonds^(1,2)					
2 August 2020	A\$150 million/£58 million	–	–	150	150
2 August 2020	A\$20 million/£8 million	–	–	20	20
2 August 2020	€98 million/£60 million (2008 €115 million/£70 million)	–	–	156	229
		–	–	326	399
Hybrid securities⁽³⁾					
21 September 2024	US\$nil (2008 US\$165 million)	–	–	–	156
16 May 2027 ⁽⁴⁾	£258 million	–	–	535	579
		–	–	535	735
Subordinated debt					
1 July 2023 ⁽⁵⁾	US\$220 million (2008 US\$250 million)	275	352	242	352
31 December 2035	US\$80 million	–	–	87	111
		275	352	329	463
Capital securities					
No fixed date	US\$151 million (2008 US\$249 million)	–	–	167	350
No fixed date	£18 million	–	–	32	32
		–	–	199	382
Total borrowings		1,833	1,907	2,971	3,666
Payable within 12 months		–	863	861	1,120
Payable in greater than 12 months		1,833	1,044	2,110	2,546
Total borrowings		1,833	1,907	2,971	3,666

(1) The consolidated entity may elect to redeem the Eurobond on or after 3 August 2010 subject to providing not less than 60 days and not more than 90 days notice of its intention to do so.

(2) During 2009, a controlled entity repurchased €17 million of Eurobonds at a discount giving rise to a profit of \$8 million on consolidation.

(3) Hybrid securities are shown net of the equity conversion option. The US dollar principal amounts shown are the outstanding amounts payable at the end of the 20 year term.

(4) The consolidated entity may elect to redeem the hybrid securities due 2027 any time after 16 May 2010. Redemption terms are set out in note 24 (D)(i).

(5) During 2009, a controlled entity repurchased US\$30 million of subordinated debt at a discount giving rise to a net profit of \$13 million on consolidation.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

24 BORROWINGS CONTINUED

(B) Finance costs

\$8 million (2008 \$5 million) of finance costs have been capitalised in the year.

(C) Security and facility arrangements

In the normal course of business, bank loans are made to controlled entities and secured by guarantees or letters of comfort given by the company.

The Eurobonds were issued by a controlled entity in July 2000 and secured by guarantees given by the company and another controlled entity. The US\$250 million subordinated debt was issued by the company in June 2003. The claims of bondholders pursuant to both of these borrowings will be subordinated in right of payment to the claims of all senior creditors, including policyholders, of the relevant controlled entity.

The hybrid securities are guaranteed by the company and a controlled entity. The claims of investors under these guarantees in general will rank equally with all existing and future unsecured and unsubordinated indebtedness of the company and the controlled entity.

The performance of the obligations of the controlled entity under the capital securities is guaranteed by the company to the extent that the controlled entity has funds. The guarantee is an unsecured and subordinated obligation of the company. The guarantee ranks senior to the claims of the holders of ordinary shares of the company, equally with equally ranked securities and instruments of the company and junior to the claims of creditors of the company.

(D) Hybrid securities

(i) Hybrid securities due 2027

In 2007, a controlled entity issued £258 million of 20 year hybrid securities. Investors can request repurchase at the end of years three, five, seven, 10 or 15 from the date of issue. The company can redeem the securities at any time after three years from the date of issue. Investors have the option to convert the security if:

- the company calls for their redemption;
- the market value of the security is less than the market value of the underlying shares in the company for five consecutive trading days; or
- on certain corporate transactions occurring (e.g. change in control).

In the event of conversion, up to 11 million shares will be issued. In the event of early redemption, up to 21 million shares will be issued based on the share price at 31 December 2009.

(ii) Hybrid securities due 2024

During the year, 9.8 million shares were issued as a result of the conversion of the hybrid securities due 2024. In 2008, no shares were issued as a result of the conversion of the hybrid securities. All hybrid securities due 2024 have now been converted to ordinary shares in the company.

(E) Capital securities

In 2007, a controlled entity issued US\$550 million of capital securities. In 2006, a controlled entity issued £300 million of capital securities. The securities have no fixed redemption date and may not be called for redemption or conversion by the investors.

Both issues of capital securities are subordinated. Distributions are deferrable and not cumulative. If a distribution or principal amount is not paid by the controlled entity, and the company does not pay the amount under the guarantee, then the capital securities are to be redeemed for QBE preference shares. For so long as the distributions or principal amounts are outstanding, no payments (including distributions or principal amounts) are to be made on the company's shares or other instruments ranking junior to the securities. Payment of distributions or principal amounts on equal ranking securities may be paid proportionally.

In 2009, US\$98 million (2008 US\$301 million) and £nil million (2008 £282 million) of capital securities were repurchased by the consolidated entity at a discount giving rise to a profit of \$48 million (2008 \$303 million) on consolidation. These securities continue to be held by the consolidated entity. The repurchases of capital securities during 2009 were cash transactions. The repurchase of capital securities during 2008 was funded by the senior notes due 2014.

(F) Senior notes due 2014

In 2008, the company issued US\$211 million and £191 million of senior notes maturing on 14 March 2014. The notes are unsecured and unsubordinated obligations of the consolidated entity and will rank equally amongst themselves and, subject to certain exceptions in relation to ranking, with all other unsecured existing and future senior indebtedness of the consolidated entity. Interest of 9.75% per annum is payable half-yearly on the US dollar notes and interest of 10.00% per annum is payable half-yearly on the sterling notes.

(G) Senior notes due 2015

In 2009, the company issued £550 million of senior notes maturing on 28 September 2015. The notes are unsecured and unsubordinated obligations of the consolidated entity and will rank equally among themselves and, subject to certain exceptions in relation to ranking, with all other unsecured existing and future senior indebtedness of the consolidated entity. Interest of 6.125% is payable half-yearly in arrears.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

24 BORROWINGS CONTINUED

(H) Fair value of borrowings

	THE COMPANY		CONSOLIDATED	
	2009 \$M	2008 \$M	2009 \$M	2008 \$M
Bank loans	-	500	24	632
Senior debt due 2009	-	365	-	365
Senior notes due 2014	677	697	677	697
Senior notes due 2015	1,021	-	1,021	-
Eurobonds	-	-	318	318
Hybrid securities	-	-	547	788
Subordinated debt	260	319	320	434
Capital securities	-	-	147	294
	1,958	1,881	3,054	3,528

There has been no active trading of borrowings during 2009. The fair value has been estimated using valuation techniques based on market available data for similar debt instruments.

At 31 December 2008, hybrid securities due 2024, which were converted to ordinary shares of the Company during 2009, have been valued with reference to the underlying market value of shares in the consolidated entity.

25 CONTRIBUTED EQUITY

(A) Share capital (company and consolidated)

	2009 \$M	2008 \$M
Issued ordinary shares, fully paid	7,366	6,714

	NUMBER OF SHARES 000	\$M
Issued and fully paid at 1 January 2009	981,795	6,714
Shares issued under the Employee Share and Option Plan	377	4
Employee options exercised	488	8
Shares issued under the Share Purchase Plan	5,593	115
Shares issued under Dividend Reinvestment Plan	20,133	388
Shares issued under Bonus Share Plan	1,996	-
Shares issued to holders of hybrid securities	9,852	136
Share issue expenses net of tax	-	1
Issued and fully paid at 31 December 2009	1,020,234	7,366
Shares notified to the Australian Securities Exchange	1,024,672	7,402
Less: Plan shares subject to non-recourse loans, derecognised under Australian GAAP	(4,438)	(36)
Issued and fully paid at 31 December 2009	1,020,234	7,366

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

25 CONTRIBUTED EQUITY CONTINUED

	NUMBER OF SHARES 000	\$M
Issued and fully paid at 1 January 2008	880,788	4,737
Shares issued under the Employee Share and Option Plan	541	5
Employee options exercised	435	6
Share placement	97,561	2,000
Shares issued under Bonus Share Plan	2,467	–
Shares issued under Deferred Compensation Plan on vesting of conditional rights	3	–
Share issue expenses net of tax	–	(34)
Issued and fully paid at 31 December 2008	981,795	6,714
Shares notified to the Australian Securities Exchange	986,609	6,754
Less: Plan shares subject to non-recourse loans, derecognised under Australian GAAP	(4,814)	(40)
Issued and fully paid at 31 December 2008	981,795	6,714

Ordinary shares in the company have no par value and entitle the holder to participate in dividends and the proceeds on winding up of the company in proportion to the number of shares held. Ordinary shareholders rank after all creditors and are entitled to any residual proceeds.

(B) Share capital, fully paid yet to be issued

5,592,597 ordinary shares in the company were paid for at 31 December 2008 (\$115 million). These shares were issued on 20 January 2009.

(C) Treasury shares held in trust (consolidated)

	2009 \$M	2008 \$M
At 1 January	1	16
Purchase of shares	19	10
Shares vested and/or released to participants	(19)	(25)
At 31 December	1	1

Shares in the company may be bought on-market to satisfy future obligations of the company under the various employee share based remuneration plans. Any such shares are held in trust. On consolidation, these shares are recognised as treasury shares held in trust. The balance of the treasury shares held in trust at the balance sheet date represents the cumulative cost of acquiring shares in the company that have not yet been distributed to employees as share based remuneration.

(D) Equity component of hybrid securities

	THE COMPANY		CONSOLIDATED	
	2009 \$M	2008 \$M	2009 \$M	2008 \$M
At 1 January	114	114	114	114
Movement during the period	–	–	–	–
At 31 December	114	114	114	114

(E) Dividend Reinvestment and Bonus Share Plans

The company operates a Dividend Reinvestment Plan (“DRP”) and a Bonus Share Plan (“BSP”) which allow equity holders to receive their dividend entitlement in the form of QBE ordinary shares.

The last date of receipt of election notices applicable to the DRP and BSP is 10 March 2010.

(F) Dividend (company and consolidated)

	2009 \$M	2008 \$M
Previous year final dividend paid on ordinary shares		
Franked at 20% – 13.0 cents (2008 32.5 cents, 50% franked)	129	288
Unfranked – 52.0 cents (2008 32.5 cents)	516	288
	645	576
Interim dividend paid on ordinary shares		
Franked at 20% – 12.4 cents (2008 12.2 cents, 20% franked)	126	108
Unfranked – 49.6 cents (2008 48.8 cents)	502	434
	628	542
Dividend reinvestment under Bonus Share Plan	(36)	(55)
Total dividend paid	1,237	1,063

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

25 CONTRIBUTED EQUITY CONTINUED

The interim dividend of \$628 million was paid on 22 September 2009. On 26 February 2010, the directors declared a 20% franked final dividend of 66.0 cents per share (2008 65.0 cents per share, 20% franked). The final dividend payout is \$678 million (2008 \$645 million).

The franking account balance on a tax paid basis at 31 December 2009 was a surplus of \$30 million (2008 \$223 million). After taking into account the impact of franking on the final dividend recommended by the directors since year end, but not recognised as a liability at year end, the franking account balance will be a deficit of \$28 million (2008 surplus of \$223 million).

Following the introduction of the conduit foreign income ("CFI") rules effective for the consolidated entity from 1 January 2006, shareholders not resident in Australia will receive CFI unfranked dividends for the unfranked portion of the final 2009 dividend exempt from Australian tax and not subject to Australian withholding tax.

(G) Capital risk management

The company's and the consolidated entity's objectives when managing capital are to maintain an optimal capital structure to reduce the cost of capital whilst meeting capital adequacy requirements, providing security for policyholders and continuing to provide returns to shareholders. Where appropriate, adjustments are made to capital levels in light of changes in economic conditions and risk characteristics of the consolidated entity's activities. In order to maintain or adjust the capital structure, the consolidated entity has the option to adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or debt securities with capital characteristics or sell assets to reduce debt.

The controlled entities which are insurance companies are subject to, and are in compliance with, externally imposed capital requirements set and monitored by regulatory bodies. These requirements are in place to ensure sufficient solvency margins for the protection of policyholders. In addition, the consolidated entity aims to maintain a strong credit rating and robust capital ratios in order to support its business objectives and maximise shareholder wealth.

QBE uses a Group-wide Economic Capital Model ("ECM") to assess the level of capital required for the underwriting, claims provisioning, credit, market, liquidity and operational risks that QBE is exposed to. The economic capital is determined as the level of capital that QBE needs to ensure that it can, with a pre-specified probability, satisfy its obligations in relation to all policies issued on or before the end of the plan year, with all risks run-off to ultimate. The ECM is used by management to help determine the strategic capital allocation, business planning, underwriting performance, pricing, reinsurance and aggregate management, as well as assisting in determining regulatory capital and reviews by third parties.

Capital is allocated to business units, divisions and ultimately to underwriting portfolios according to the associated risk. The minimum target risk adjusted return on capital is 15%. The business plans include net asset projections, dividends, issued share projections and solvency projections as well as the impact of potential acquisitions. Should there be a significant change in the consolidated entity's risk profile, the ECM will be recalculated, reviewed and, if appropriate, the results reported to the QBE board.

QBE maintains an ongoing review of the company's and consolidated entity's structure to ensure flexibility in the allocation of capital whilst minimising the cost of capital. Active management of the business and its capital has enabled QBE to maintain its financial strength and credit rating and has afforded QBE with good access to capital markets when needed.

Management monitors the company's and the consolidated entity's capital levels on an ongoing basis, with particular focus on the following:

- The consolidated entity is subject to APRA Level 2 minimum capital requirements. Management actively manages the components of capital in order to achieve an optimal capital adequacy multiple of around 1.5 times APRA's minimum requirement for Level 2 groups. The multiple at 31 December 2009 is 1.6 times (2008 1.7 times).
- All regulated wholly-owned entities are subject to local prudential standards requiring that a minimum level of capital is maintained to meet obligations to policyholders. It is the consolidated entity's policy that each regulated entity maintains a capital base appropriate to its size, business mix, complexity and risk profile which meets local regulatory requirements.
- The consolidated entity aims to maintain the ratio of borrowings to shareholders' funds at around 40%. The ratio of borrowings to shareholders' funds at 31 December 2009 is 29.1% (2008 32.9%).
- The consolidated entity believes that insurer financial strength ratings provided by the major rating agencies are an important factor in demonstrating the financial strength and claims paying ability of our regulated wholly-owned entities. The consolidated entity's policy is to maintain ratings that optimise the balance between providing security to policyholders whilst providing appropriate returns to shareholders. All of our regulated wholly-owned entities are rated Standard & Poor's "A" rating or higher (or equivalent rating from other recognised rating agencies) at 31 December 2009.

In addition to the management reporting and planning processes, QBE has dedicated staff in all business units and divisions responsible for understanding the regulatory capital requirements for each of our operations. The quality of assets (particularly investments and reinsurance recoveries) is monitored on an ongoing basis to ensure issues are identified early and remedial action, where necessary, is taken to restore effective capital performance and levels.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

26 OTHER RESERVES

	THE COMPANY		CONSOLIDATED	
	2009 \$M	2008 \$M	2009 \$M	2008 \$M
Owner occupied property revaluation reserve⁽¹⁾				
At 1 January	-	-	15	22
Valuation decrease	-	-	(8)	(10)
Deferred tax	-	-	3	3
At 31 December	-	-	10	15
Cash flow hedges reserve⁽²⁾				
At 1 January	12	6	-	(15)
Fair value (loss) gain	(79)	96	(64)	178
Transfer of (loss) gain to income statement	67	(90)	58	(160)
Taxation	-	-	(2)	(3)
At 31 December	-	12	(8)	-
Foreign currency translation reserve⁽³⁾				
At 1 January	-	-	(305)	(187)
(Losses) gains on translation	-	-	(1,788)	436
Losses on forward foreign exchange contracts	-	-	(418)	(554)
At 31 December	-	-	(2,511)	(305)
Options reserve⁽⁴⁾				
At 1 January	40	33	101	94
Options and conditional rights expense	40	33	40	33
Transfers from reserve on vesting of options and conditional rights	(19)	(26)	(19)	(26)
Taxation	-	-	2	-
At 31 December	61	40	124	101
General reserve⁽⁵⁾				
At 1 January	-	-	5	5
Movement in the year	-	-	-	-
At 31 December	-	-	5	5
Realised capital profits reserve⁽⁶⁾				
At 1 January	-	-	6	6
Movement in the year	-	-	-	-
At 31 December	-	-	6	6
Total reserves at 31 December	61	52	(2,374)	(178)

(1) Used to recognise fair value movements in the carrying value of owner occupied property. Refer note 1(T).

(2) Used to record gains or losses on a hedging instrument in a cash flow hedge that are recognised directly in equity. Refer note 1(O)(ii).

(3) Exchange gains and losses arising on translation of a foreign controlled entity and related hedging instruments are taken to the foreign currency translation reserve. Refer note 1(W). In the event of the disposal of a relevant net investment, the movement in the reserve is recognised in the income statement.

(4) Used to recognise the fair value of instruments issued as share based payments.

(5) Established prior to 1989 for general purposes.

(6) Realised capital profits arising prior to the introduction of capital gains tax in Australia.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

27 SHARE BASED PAYMENTS

(A) Employee Share and Option Plan

The company, at its 1981 AGM, approved the issue of shares from time to time under an Employee Share and Option Plan ("the Plan"), up to 5% of the issued ordinary shares in the capital of the company. Any full-time or part-time employee of the consolidated entity or equally owned joint venture who is offered shares or options pursuant to the offer document of the Plan is eligible to participate in the Plan.

Under the Plan, ordinary shares of the company are offered at the weighted average market price during the five trading days up to the date of the offer. Likewise, the exercise price for options offered under the Plan is the weighted average market price during the five trading days up to the date of the offer.

In accordance with the terms of the Plan, for awards made up to and including March 2009 interest-free loans were granted to employees to subscribe for shares issued under the Plan. Prior to 20 June 2005, the terms of the loans were either personal recourse or non-recourse. With effect from 20 June 2005, only personal recourse loans were granted to employees to subscribe for shares under the Plan. The loans are repayable in certain circumstances as set out in the Plan such as termination of employment or breach of condition. The award of options and interest free loans was discontinued for awards made after March 2009.

Currently there are three schemes operating within the Plan:

(i) Deferred Compensation Plan

Shareholder approval of the DCP was given at the 2006 AGM for the purpose of ASX Listing Rule 7.2, sections 200B and 200E of the *Corporations Act 2001* and for all other purposes.

Operative from 1 January 2009 and applicable to awards in March 2010

Senior management are invited to participate in the Deferred Compensation Plan ("DCP"). Under the DCP, the directors can issue conditional rights to shares to senior management who have already achieved predetermined performance criteria. The terms of the DCP may vary to take into account the requirements and market conditions of the locations of senior management, but the general terms of the DCP conditional rights are as follows:

- Conditional rights to the value of 50% of the DCP award will be converted to shares after three years.
- Conditional rights to the value of 50% of the DCP award will be converted to shares after five years.
- Further shares are issued in relation to the conditional rights to reflect dividends paid on ordinary shares of the company in the period commencing from the date of the grant of the conditional rights.
- The shares issued pursuant to the conditional rights are issued without payment being made by senior management (i.e. at a nil exercise price).

The shares issued pursuant to the conditional rights will only vest if the individual has remained in the company's service throughout the vesting period. The remuneration committee has the discretion to pay cash in lieu of shares in certain circumstances such as death, disability, redundancy or retirement if the individual is not subject to disciplinary proceedings or notice on that date. The ultimate vesting of the conditional rights is also contingent on there being no material subsequent deterioration of the consolidated entity's return on equity during the vesting period.

Operative until 31 December 2008 and applicable to awards in March 2009 and prior

For DCP awards made in March 2009 and prior, the directors were able to issue conditional rights to shares and options to subscribe for shares to senior management who have already achieved predetermined performance criteria. The terms of the DCP varied to take into account the requirements and market conditions of the locations of senior management, but the general terms of the DCP conditional rights and options were as follows:

- The conditional rights entitled relevant employees to receive shares on the third anniversary of the grant of the rights. Further shares were issued in relation to the conditional rights to reflect dividends paid on ordinary shares of the company in the period commencing from the date of the grant of the conditional rights.
- The shares issued pursuant to the conditional rights were issued without payment being made by senior management (i.e. at a nil exercise price).
- The options were subject to the terms and conditions of the Plan. Options issued in 2004 and prior could be exercised after three years, whilst any options issued in 2005 and thereafter will generally be exercisable after five years. They must be exercised within a 12 month period after vesting. Interest-free personal recourse loans were granted on the terms permitted by the Plan as described above to persons who hold options to fund the exercise of options.

The shares issued pursuant to the conditional rights and the options will only vest if the individual has remained in the company's service throughout the vesting period. The remuneration committee has the discretion to pay cash in lieu of shares in certain circumstances such as death, disability, redundancy or retirement if the individual is not subject to disciplinary proceedings or notice on that date.

(ii) Share Incentive Plan

Generally, all full-time or part-time employees of the consolidated entity in Australia, Ireland, New Zealand, the UK and the US with a minimum of one year's service are invited to participate in the Share Incentive Plan ("the SIP"). Under the SIP, the directors can provide shares up to \$1,000 to employees without payment being made by employees. The allocation of shares is based on the period of service. The shares are purchased on-market and held in trust for the employee for a minimum of three years or until cessation of employment, whichever is earlier. Further details are provided in note 27(E).

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

27 SHARE BASED PAYMENTS CONTINUED

(iii) Group Executive Restricted Share Plan

Key management personnel were eligible to participate in the Group Executive Restricted Share Plan ("GERSP") which came into effect from 1 January 2008. Under the GERSP, eligible executives have the opportunity to acquire additional equity in the form of conditional rights if the consolidated entity exceeds a return on equity target.

The conditional rights entitle relevant executives to receive fully paid QBE shares on the third anniversary of the grant of the conditional rights. Further shares are issued in relation to the conditional rights to reflect dividends paid on ordinary shares of the company in the period commencing from the date of the grant of the conditional rights. The shares issued pursuant to the conditional rights are issued without payment being made by the executive (i.e. at a nil exercise price).

The shares issued pursuant to the conditional rights will only be issued if the individual has remained in the company's service throughout the vesting period (unless leaving due to death, genuine retirement, incapacity due to total and permanent disability or redundancy) and is not subject to disciplinary proceedings or notice on that date. The ultimate vesting of the conditional rights is also contingent on there being no material subsequent deterioration of the consolidated entity's return on equity during the vesting period.

The GERSP will be replaced in 2010 by the Long-Term Incentive Plan ("LTI"). Details of the LTI are provided in the directors' report on page 65.

(B) Employee options

During the year, the company granted to 464 (2008 866) qualifying employees options over ordinary shares with a total market value of \$53 million (2008 \$54 million), being the quoted market price at the date the options were granted. The weighted average fair value of options granted during the year ended 31 December 2009 was \$2.80 (2008 \$4.61).

The market value of the options outstanding at the balance sheet date was \$299 million (2008 \$238 million), calculated by reference to the quoted market value of the underlying shares at that date.

Details of the number of employee options granted, exercised and cancelled or forfeited during 2009, including those issued under the DCP, were as follows:

2009 GRANT DATE	EXERCISE PRICE	BALANCE AT 1 JAN 2009	GRANTED IN THE YEAR	EXERCISED IN THE YEAR	CANCELLED/ FORFEITED IN THE YEAR	BALANCE AT 31 DEC 2009
3 March 2004	\$11.08	34,750	-	(7,000)	-	27,750
3 March 2005	\$8.04	135,583	-	-	-	135,583
3 March 2005	\$11.08	150,310	-	-	-	150,310
3 March 2005	\$14.85	2,103,730	-	(195,107)	(11,791)	1,896,832
8 April 2005	\$14.85	118,587	-	-	-	118,587
12 May 2005	\$14.81	60,000	-	(60,000)	-	-
2 March 2006	\$20.44	2,127,857	-	(151,265)	(42,636)	1,933,956
7 April 2006	\$20.44	94,771	-	-	-	94,771
2 March 2007	\$20.44	40,000	-	(20,000)	-	20,000
2 March 2007	\$32.68	1,739,572	-	-	(111,352)	1,628,220
4 April 2007	\$32.68	51,125	-	-	-	51,125
4 March 2008	\$20.44	40,000	-	(20,000)	-	20,000
4 March 2008	\$24.22	2,468,346	-	(19,110)	(64,917)	2,384,319
4 April 2008	\$27.00	74,257	-	-	-	74,257
6 March 2009	\$20.44	-	20,000	-	-	20,000
6 March 2009	\$17.57	-	3,201,126	(15,137)	(85,303)	3,100,686
		9,238,888	3,221,126	(487,619)	(315,999)	11,656,396
Weighted average exercise price	\$22.12		\$17.59	\$17.44	\$24.55	\$21.00

The weighted average share price at the date of exercise of options during the year was \$22.47 (2008 \$24.31). The weighted average remaining contractual life of total options outstanding at 31 December 2009 was 3.2 years (2008 3.5 years).

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

27 SHARE BASED PAYMENTS CONTINUED

Employee options outstanding at 31 December 2009 were as follows:

YEAR OF EXPIRY	FUTURE PERFORMANCE ⁽¹⁾	DCP/STI	OTHER ⁽²⁾	TOTAL OPTIONS
2010	–	218,679	–	218,679
2011	60,000	2,396,255	–	2,456,255
2012	–	2,223,366	–	2,223,366
2013	–	1,767,872	–	1,767,872
2014	–	1,905,741	–	1,905,741
2015	–	3,056,733	–	3,056,733
2024	–	–	27,750	27,750
	60,000	11,568,646	27,750	11,656,396
Vested and exercisable at 31 December 2009	–	135,304	27,750	163,054

(1) The future performance options have been issued subject to the achievement of specific performance criteria. Examples of such criteria are provided in the directors' report.

(2) Other options were issued to US and Irish employees in 2004 in lieu of shares under the Plan. The options vested immediately and are exercisable until March 2024.

Details of the number of employee options granted, exercised and cancelled or forfeited during 2008, including those issued under the DCP, were as follows:

2008 GRANT DATE	EXERCISE PRICE	BALANCE AT 1 JAN 2008	GRANTED IN THE YEAR	EXERCISED IN THE YEAR	CANCELLED/ FORFEITED IN THE YEAR	BALANCE AT 31 DEC 2008
13 March 2003	\$8.04	16,152	–	(15,752)	(400)	–
3 March 2004	\$11.08	80,509	–	(45,759)	–	34,750
3 March 2005	\$8.04	173,739	–	(38,156)	–	135,583
3 March 2005	\$11.08	186,500	–	(36,190)	–	150,310
3 March 2005	\$14.85	2,311,154	–	(201,824)	(5,600)	2,103,730
8 April 2005	\$14.85	118,587	–	–	–	118,587
12 May 2005	\$14.81	60,000	–	–	–	60,000
2 March 2006	\$20.44	2,235,673	–	(97,187)	(10,629)	2,127,857
7 April 2006	\$20.44	94,771	–	–	–	94,771
2 March 2007	\$20.44	40,000	–	–	–	40,000
2 March 2007	\$32.68	1,822,551	5,508	–	(88,487)	1,739,572
4 April 2007	\$32.68	51,125	–	–	–	51,125
4 March 2008	\$20.44	–	40,000	–	–	40,000
4 March 2008	\$24.22	–	2,529,180	–	(60,834)	2,468,346
4 April 2008	\$27.00	–	74,257	–	–	74,257
		7,190,761	2,648,945	(434,868)	(165,950)	9,238,888
Weighted average exercise price		\$21.02	\$24.26	\$14.54	\$28.13	\$22.12

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

27 SHARE BASED PAYMENTS CONTINUED

Employee options outstanding at 31 December 2008 were as follows:

YEAR OF EXPIRY	FUTURE PERFORMANCE	DCP/STI	OTHER	TOTAL OPTIONS
2009	60,000	–	–	60,000
2010	–	170,401	–	170,401
2011	80,000	2,612,096	–	2,692,096
2012	–	2,401,662	–	2,401,662
2013	–	1,860,805	–	1,860,805
2014	–	2,019,174	–	2,019,174
2024	–	–	34,750	34,750
	140,000	9,064,138	34,750	9,238,888
Vested and exercisable at 31 December 2008	20,000	–	34,750	54,750

(C) Conditional rights

Details of the number of employee entitlements to conditional rights to ordinary shares under the DCP and GERSP granted, vested and transferred to employees during the year were as follows:

2009	DATE EXERCISABLE	FAIR VALUE PER RIGHT AT GRANT DATE	BALANCE AT 1 JAN 2009	GRANTED IN THE YEAR	DIVIDENDS ATTACHING IN THE YEAR	VESTED AND TRANSFERRED TO EMPLOYEES IN THE YEAR	CANCELLED IN THE YEAR	BALANCE AT 31 DEC 2009
2 March 2006	1 March 2009	\$23.09	821,850	–	1,194	(821,004)	(2,040)	–
7 April 2006	6 April 2009	\$24.23	39,572	–	1,610	(41,182)	–	–
2 March 2007	1 March 2010	\$32.68	734,850	–	49,752	(40,394)	(10,424)	733,784
4 April 2007	3 April 2010	\$32.68	27,485	–	1,927	–	–	29,412
4 March 2008	3 March 2011	\$24.22	1,216,083	–	82,597	(63,738)	(15,989)	1,218,953
4 April 2008	4 April 2011	\$27.00	38,095	–	2,672	–	–	40,767
1 January 2009	2 January 2012	\$25.37	–	20,000	1,403	–	–	21,403
6 March 2009	5 March 2012	\$17.57	–	1,883,467	131,428	(24,218)	(45,547)	1,945,130
			2,877,935	1,903,467	272,583	(990,536)	(74,000)	3,989,449

The weighted average share price at the date of vesting of conditional rights during the year ended 31 December 2009 was \$17.90 (2008 \$21.86). The weighted average fair value of conditional rights granted during the year ended 31 December 2009 was \$17.65 (2008 \$24.32).

Details of the number of employee entitlements to conditional rights to ordinary shares under the DCP and GERSP granted, vested and transferred to employees during the prior year were as follows:

2008	DATE EXERCISABLE	FAIR VALUE PER RIGHT AT GRANT DATE	BALANCE AT 1 JAN 2008	GRANTED IN THE YEAR	DIVIDENDS ATTACHING IN THE YEAR	VESTED AND TRANSFERRED TO EMPLOYEES IN THE YEAR	CANCELLED IN THE YEAR	BALANCE AT 31 DEC 2008
3 March 2005	2 March 2008	\$15.30	72,750	–	–	(72,750)	–	–
3 March 2005	2 March 2008	\$15.86	78,095	–	–	(78,095)	–	–
3 March 2005	2 March 2008	\$16.94	276,347	–	–	(276,347)	–	–
3 March 2005	2 March 2008	\$17.51	548,274	–	–	(548,274)	–	–
3 March 2005	2 March 2008	\$17.81	100,284	–	–	(100,284)	–	–
8 April 2005	7 April 2008	\$16.94	48,656	–	1,486	(50,142)	–	–
2 March 2006	1 March 2009	\$23.09	832,896	–	45,782	(56,153)	(675)	821,850
7 April 2006	6 April 2009	\$24.23	37,425	–	2,147	–	–	39,572
2 March 2007	1 March 2010	\$32.68	751,154	2,850	41,293	(42,636)	(17,811)	734,850
4 April 2007	3 April 2010	\$32.68	25,994	–	1,491	–	–	27,485
4 March 2008	3 March 2011	\$24.22	–	1,185,127	67,369	(9,397)	(27,016)	1,216,083
4 April 2008	4 April 2011	\$27.00	–	37,128	967	–	–	38,095
			2,771,875	1,225,105	160,535	(1,234,078)	(45,502)	2,877,935

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

27 SHARE BASED PAYMENTS CONTINUED

(D) Fair value of options and conditional rights

The fair value of both options and conditional rights is determined using a binomial model. The fair value is earned evenly over the period between grant and vesting. For those options and conditional rights granted during the year to 31 December 2009, the following significant assumptions were used:

		OPTIONS		CONDITIONAL RIGHTS	
		2009	2008	2009	2008
Share price on grant date	\$	16.30	20.50 – 25.19	16.30 – 25.81	20.50 – 25.19
Fair value of instrument at grant date	\$	2.36 – 2.81	3.36 – 5.16	17.57 – 25.37	24.22 – 27.00
Risk-free interest rate	%	3.6 – 4.2	6.2 – 6.5	3.6 – 4.2	6.2 – 6.5
Expected share price volatility	%	25.0	25.0	25.0	25.0
Expected dividend yield	%	5.0	5.0	5.0	5.0
Expected life of instrument	years	3.0 – 5.0	3.0 – 5.0	3.0	3.0

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.

(E) Share Incentive Plan

The SIP was introduced during 2005 and is a reward scheme available to eligible permanent employees who have met minimum service conditions at the annual grant date. Under the terms of the SIP, eligible employees may be offered up to \$1,000 of fully paid ordinary shares in the company annually for no cash consideration. The market value of shares issued under the terms of the SIP is expensed in the period in which the shares are granted. The total number of shares issued to participating employees in the year was 243,725 (2008 193,275). The weighted average market price on the issue date was \$22.75 (2008 \$23.76).

(F) Share based payment expenses

Total expenses arising from share based payment transactions during the year included in underwriting expenses were as follows:

	CONSOLIDATED	
	2009 \$M	2008 \$M
Options provided under the DCP	11	10
Conditional rights provided under the DCP	29	23
Shares provided under the SIP	6	5
	46	38

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

28 KEY MANAGEMENT PERSONNEL (COMPANY AND CONSOLIDATED)

(A) Key management personnel – compensation

	CONSOLIDATED	
	2009 \$'000	2008 \$'000
Short-term employee benefits	28,072	29,473
Post employment benefits	1,232	1,327
Other long-term employment benefits	232	333
Share based payments	7,783	7,119
Termination benefits	–	2,902
	37,319	41,154

2008 comparatives have been updated to include all current key management personnel as disclosed in the remuneration report on pages 56 to 76 of the directors' report.

(B) Key management personnel – equity instruments

(i) Options and conditional rights provided as remuneration

For additional details of equity instruments (options and conditional rights) provided to key management personnel as remuneration and shares issued on the exercise of such instruments, together with the associated terms and conditions, refer to the remuneration report on pages 56 to 76. No equity instruments were provided to non-executive directors.

(ii) DCP option holdings

Details of the movements in the number of DCP options over ordinary shares in the company provided as remuneration to the key management personnel are provided below.

2009	BALANCE AT 1 JAN 2009	GRANTED IN THE YEAR	EXERCISED IN THE YEAR	CANCELLED/ FORFEITED IN THE YEAR	BALANCE AT 31 DEC 2009	EXERCISE COST AT 31 DEC 2009 \$'000
NUMBER OF OPTIONS						
Executive director						
FM O'Halloran	338,740	127,804	–	–	466,544	9,619
Other key management personnel						
SP Burns	411,768	125,307	–	–	537,075	10,112
NG Drabsch	177,755	51,144	–	–	228,899	4,592
D Fogarty	66,841	28,839	–	–	95,680	2,019
MJ Goodwin	23,011	29,028	–	–	52,039	991
MD ten Hove ⁽¹⁾	107,614	16,222	–	–	123,836	2,915
TW Ibbotson	83,973	40,696	–	–	124,669	2,497
V McLenaghan	156,515	63,589	–	–	220,104	4,526
BM Nicholls	97,579	25,681	–	–	123,260	2,661
DA Ramsay	94,083	29,962	–	–	124,045	2,507
J Rumpier	46,892	13,835	–	–	60,727	1,248
JM Smith	76,730	24,611	–	–	101,341	2,046
GB Thwaites	39,371	23,113	–	–	62,484	1,321

(1) Mr ten Hove had 46,799 DCP options that were vested and exercisable at 31 December 2009. All other options were unvested and not exercisable at this date.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

28 KEY MANAGEMENT PERSONNEL CONTINUED

2008	BALANCE AT 1 JAN 2008	GRANTED IN THE YEAR	EXERCISED IN THE YEAR	CANCELLED/ FORFEITED IN THE YEAR	BALANCE AT 31 DEC 2008 ⁽¹⁾	EXERCISE COST AT 31 DEC 2008 \$'000
NUMBER OF OPTIONS						
Executive director						
FM O'Halloran	264,483	74,257	–	–	338,740	7,374
Other key management personnel						
SP Burns	335,068	76,700	–	–	411,768	7,910
NG Drabsch	142,586	35,169	–	–	177,755	3,693
D Fogarty	50,236	16,605	–	–	66,841	1,512
MJ Goodwin	15,077	7,934	–	–	23,011	481
MD ten Hove	137,160	37,161	(66,707)	–	107,614	2,630
TW Ibbotson	64,786	19,187	–	–	83,973	1,782
V McLenaghan	113,680	42,835	–	–	156,515	3,409
BM Nicholls	82,054	15,525	–	–	97,579	2,210
DA Ramsay	74,211	19,872	–	–	94,083	1,980
J Rumppler	36,403	10,489	–	–	46,892	1,005
JM Smith	60,584	16,146	–	–	76,730	1,613
GB Thwaites	24,855	14,516	–	–	39,371	915

(1) None of these options were vested or exercisable at 31 December 2008.

(iii) Future performance option holdings

Details of the movements in the number of future performance options over ordinary shares in the company provided as remuneration to the key management personnel are provided below.

		BALANCE AT 1 JAN	GRANTED IN THE YEAR	EXERCISED IN THE YEAR	CANCELLED/ FORFEITED IN THE YEAR	BALANCE AT 31 DEC ⁽¹⁾	EXERCISE COST AT 31 DEC \$'000
NUMBER OF OPTIONS							
Key management personnel							
SP Burns	2009	40,000	20,000	–	–	60,000	1,226
	2008	20,000	20,000	–	–	40,000	818

(1) None of these options were vested or exercisable at 31 December 2009 or 31 December 2008.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

28 KEY MANAGEMENT PERSONNEL CONTINUED

(iv) Conditional rights holdings

Details of the movements in the number of conditional rights to ordinary shares in the company provided as remuneration to the key management personnel are provided below.

2009	BALANCE AT 1 JAN 2009	GRANTED IN THE YEAR	DIVIDENDS ATTACHING IN THE YEAR	VESTED AND TRANSFERRED IN THE YEAR	CANCELLED/ FORFEITED IN THE YEAR	BALANCE AT 31 DEC 2009 ⁽¹⁾
NUMBER OF RIGHTS						
Executive director						
FM O'Halloran	105,152	63,902	10,690	(41,182)	–	138,562
Other key management personnel						
SP Burns	166,006	132,272	17,620	(47,006)	–	268,892
NG Drabsch	53,612	29,943	4,354	(21,462)	–	66,447
D Fogarty	26,532	16,261	2,229	(11,025)	–	33,997
MJ Goodwin	6,701	20,261	1,831	(884)	–	27,909
MD ten Hove	52,494	10,706	3,037	(19,904)	–	46,333
TW Ibbotson	27,363	25,720	2,980	(10,604)	–	45,459
V McLenaghan	53,549	61,356	6,891	(16,648)	–	105,148
BM Nicholls	37,583	14,480	2,417	(17,594)	–	36,886
DA Ramsay	29,536	16,893	2,450	(11,475)	–	37,404
J Rumpier	15,468	6,917	1,161	(5,831)	–	17,715
JM Smith	24,158	13,877	1,993	(9,597)	–	30,431
GB Thwaites	15,535	13,032	1,779	(3,184)	–	27,162

(1) None of these conditional rights were vested or exercisable at 31 December 2009.

2008	BALANCE AT 1 JAN 2008	GRANTED IN THE YEAR	DIVIDENDS ATTACHING IN THE YEAR	VESTED AND TRANSFERRED IN THE YEAR	CANCELLED/ FORFEITED IN THE YEAR	BALANCE AT 31 DEC 2008 ⁽¹⁾
NUMBER OF RIGHTS						
Executive director						
FM O'Halloran	112,075	37,128	6,091	(50,142)	–	105,152
Other key management personnel						
SP Burns	144,507	80,963	9,005	(68,469)	–	166,006
NG Drabsch	61,317	17,585	2,909	(28,199)	–	53,612
D Fogarty	21,820	8,302	1,440	(5,030)	–	26,532
MJ Goodwin	6,572	3,967	363	(4,201)	–	6,701
MD ten Hove	58,995	18,581	2,848	(27,930)	–	52,494
TW Ibbotson	27,912	9,594	1,484	(11,627)	–	27,363
V McLenaghan	49,528	21,417	2,906	(20,302)	–	53,549
BM Nicholls	35,803	7,763	2,038	(8,021)	–	37,583
DA Ramsay	31,993	9,936	1,602	(13,995)	–	29,536
J Rumpier	15,756	5,245	839	(6,372)	–	15,468
JM Smith	26,081	8,073	1,312	(11,308)	–	24,158
GB Thwaites	11,128	7,258	844	(3,695)	–	15,535

(1) None of these conditional rights were vested or exercisable at 31 December 2008.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

28 KEY MANAGEMENT PERSONNEL CONTINUED

(v) Shareholdings

The movements during the year in the number of ordinary shares in the company held by the key management personnel, including their personally related parties, are provided in the table below. Prior to 20 June 2005, non-recourse loans were provided by the consolidated entity to the executive director and other key management personnel on the exercise of their options for the purchase of shares in the company. Under AIFRS, non-recourse loans and the related shares are derecognised and are instead treated as options.

2009 NUMBER OF SHARES	INTEREST IN SHARES AT 1 JAN 2009	CONDITIONAL RIGHTS VESTED	OPTIONS EXERCISED	SHARES PURCHASED (SOLD)	DIVIDENDS REINVESTED IN THE YEAR	INTEREST IN SHARES AT 31 DEC 2009	INTEREST IN SHARES AT 31 DEC 2009 SUBJECT TO NON-RECOURSE LOANS
Non-executive directors							
LF Bleasel AM	52,116	–	–	5,488	–	57,604	–
DM Boyle	5,003	–	–	3,694	–	8,697	–
EJ Cloney AM	635,377	–	–	244	–	635,621	–
IF Hudson	8,732	–	–	–	489	9,221	–
BJ Hutchinson AM	51,888	–	–	11,608	–	63,496	–
CLA Irby	15,000	–	–	–	–	15,000	–
IYL Lee	26,505	–	–	244	–	26,749	–
Executive director							
FM O'Halloran	1,116,740	41,182	–	(72,811)	73,449	1,158,560	894,972
Other key management personnel							
SP Burns	76,142	47,006	–	(75,000)	6,547	54,695	3,540
NG Drabsch	227,556	21,462	–	(79,896)	15,560	184,682	155,527
D Fogarty	35,550	11,025	–	(13)	3,265	49,827	20,209
MJ Goodwin	11,036	884	–	244	853	13,017	6,099
MD ten Hove	275,633	19,904	–	–	20,724	316,261	185,898
TW Ibbotson	20,183	10,604	–	–	–	30,787	–
V McLenaghan	185,413	16,648	–	244	–	202,305	109,809
BM Nicholls	16,097	17,594	–	244	–	33,935	8,076
DA Ramsay	215,708	11,475	–	(11,231)	–	215,952	92,318
J Rumppler	58,595	5,831	–	(5,831)	–	58,595	56,975
JM Smith	11,308	9,597	–	244	–	21,149	–
GB Thwaites	25,669	3,184	–	244	2,040	31,137	3,401

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

28 KEY MANAGEMENT PERSONNEL CONTINUED

The movements in the number of ordinary shares in the company held by key management personnel, including their personally related parties, in the prior year are provided in the table below.

2008 NUMBER OF SHARES	INTEREST IN SHARES AT 1 JAN 2008	CONDITIONAL RIGHTS VESTED	OPTIONS EXERCISED	SHARES PURCHASED (SOLD)	DIVIDENDS REINVESTED IN THE YEAR	INTEREST IN SHARES AT 31 DEC 2008	INTEREST IN SHARES AT 31 DEC 2008 SUBJECT TO NON-RECOURSE LOANS
Non-executive directors							
LF Bleasel AM	43,996	–	–	8,120	–	52,116	–
DM Boyle	5,003	–	–	–	–	5,003	–
EJ Cloney AM	635,377	–	–	–	–	635,377	–
IF Hudson	1,058	–	–	7,642	32	8,732	–
BJ Hutchinson AM	33,950	–	–	17,938	–	51,888	–
CLA Irby	15,000	–	–	–	–	15,000	–
IYL Lee	21,505	–	–	5,000	–	26,505	–
Executive director							
FM O'Halloran	1,104,569	50,142	–	(98,750)	60,779	1,116,740	875,359
Other key management personnel							
SP Burns	3,511	68,469	–	–	4,162	76,142	3,308
NG Drabsch	316,076	28,199	–	(135,732)	19,013	227,556	154,649
D Fogarty	28,573	5,030	–	–	1,947	35,550	18,885
MJ Goodwin	6,236	4,201	–	–	599	11,036	5,699
MD ten Hove	194,416	27,930	66,707	(30,000)	16,580	275,633	173,716
TW Ibbotson	8,556	11,627	–	–	–	20,183	–
V McLenaghan	165,111	20,302	–	–	–	185,413	109,809
BM Nicholls	8,076	8,021	–	–	–	16,097	8,076
DA Ramsay	201,713	13,995	–	–	–	215,708	92,318
J Rumppler	56,859	6,372	–	(6,567)	1,931	58,595	56,975
JM Smith	–	11,308	–	–	–	11,308	–
GB Thwaites	25,310	3,695	–	(5,000)	1,664	25,669	3,177

(C) Key management personnel – share loans

Details of the share loans made by the consolidated entity to the key management personnel are set out below.

(i) Personal recourse share loans

2009	BALANCE AT 1 JAN 2009 \$'000	LOANS MADE IN THE YEAR \$'000	REPAYMENTS \$'000	BALANCE AT 31 DEC 2009 \$'000	INTEREST NOT CHARGED \$'000	HIGHEST BALANCE IN THE PERIOD \$'000
Executive director						
FM O'Halloran	1,271	–	–	1,271	84	1,271
Other key management personnel						
NG Drabsch	502	–	(502)	–	14	502
MD ten Hove	991	–	–	991	63	991
V McLenaghan	157	–	(15)	142	10	157
DA Ramsay	558	–	(42)	516	36	558
J Rumppler	14	–	(1)	13	1	14
GB Thwaites	121	–	–	121	8	121

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

28 KEY MANAGEMENT PERSONNEL CONTINUED

2008	BALANCE AT 1 JAN 2008 \$'000	LOANS MADE IN THE YEAR \$'000	REPAYMENTS \$'000	BALANCE AT 31 DEC 2008 \$'000	INTEREST NOT CHARGED \$'000	HIGHEST BALANCE IN THE PERIOD \$'000
Executive director						
FM O'Halloran	1,271	–	–	1,271	112	1,271
Other key management personnel						
NG Drabsch	502	–	–	502	44	502
MD ten Hove	–	991	–	991	74	991
V McLenaghan	173	–	(16)	157	14	173
DA Ramsay	600	–	(42)	558	51	600
J Rumpler	14	–	–	14	1	14
GB Thwaites	121	–	–	121	11	121

(ii) Non-recourse share loans

Prior to 20 June 2005, non-recourse loans were provided by the consolidated entity to the executive director and other key management personnel for the purchase of shares in the company. Under AIFRS, non-recourse loans and the related shares are derecognised and are instead treated as options.

2009	BALANCE AT 1 JAN 2009 \$'000	LOANS MADE IN THE YEAR \$'000	REPAYMENTS \$'000	BALANCE AT 31 DEC 2009 \$'000	INTEREST NOT CHARGED \$'000	HIGHEST BALANCE IN THE PERIOD \$'000
Executive director						
FM O'Halloran	4,227	–	–	4,227	280	4,227
Other key management personnel						
SP Burns	22	–	–	22	1	22
NG Drabsch	2,008	–	(29)	1,979	133	2,008
D Fogarty	87	–	–	87	6	87
MJ Goodwin	35	–	–	35	2	35
MD ten Hove	2,848	–	–	2,848	182	2,848
V McLenaghan	1,021	–	(70)	951	65	1,021
BM Nicholls	170	–	(5)	165	11	170
DA Ramsay	993	–	(58)	935	64	993
J Rumpler	397	–	(16)	381	26	397
GB Thwaites	43	–	–	43	3	43

(D) Other transactions with key management personnel and their personally related parties

FM O'Halloran – retirement benefits

Mr O'Halloran joined QBE in June 1976. 12 of his years with the consolidated entity have been in the position of chief executive officer, with four years as director of operations, seven years as director of finance, five years as chief financial officer and the remainder as Group financial controller. On 1 January 1998, a controlled entity entered into a retirement benefit arrangement with Mr O'Halloran, which is in addition to his entitlement under the QBE Australia defined benefit plan. This arrangement was revised during 2009. As Mr O'Halloran was employed by the consolidated entity in May 2004, on his retirement he will receive a lump sum payment of 100% of his fixed remuneration for the year prior to the date of his retirement. As a condition of this arrangement, Mr O'Halloran has entered into a non-compete agreement for three years from the date of his retirement.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

29 DEFINED BENEFIT PLANS

	2009 \$M	2008 \$M
Defined benefit plan surplus	2	2
Retirement benefit deficit	(96)	(111)
Post-employment health care benefit deficit	(11)	(14)
	(107)	(125)
Committed future contribution	(13)	(23)
Defined benefit plan deficit	(120)	(148)

Entities in the consolidated entity participate in a number of superannuation plans which have been established and are sponsored by those entities. A number of these plans provide defined benefits to employees on retirement, disability or death. The benefits are based on years of service and an average salary calculation.

Contributions are made to the plans by both employees and controlled entities, typically as a percentage of salary and within the rules of the plans, and are based on funding schedules prepared by independent actuaries. The contribution rate in respect of defined benefit plans is agreed between the relevant controlled entity and the plans' trustees and actuaries. The consolidated entity has no immediate legal obligation to settle the liability.

The consolidated entity also sponsors defined benefit health care plans that provide post-employment medical benefits and life assurance to eligible retired employees. Contributions are made to cover the current cash outflows from the plans and a liability is recorded to recognise the estimated accrued but not yet funded obligations.

Independent actuarial assessments of all significant plans are completed at least once every three years. The main plans were assessed by various qualified employees of Russell Employee Benefits, AON Consulting and Towers Watson. All valuations have been updated for information available at 31 December 2009.

(A) Defined benefit surpluses (deficits)

The amounts recognised in the balance sheet for defined benefit plans are as follows:

	DATE OF LAST ACTUARIAL ASSESSMENT	FAIR VALUE OF PLAN ASSETS		PRESENT VALUE OF PLAN OBLIGATIONS		SURPLUS NOT RECOGNISED		NET RECOGNISED SURPLUS (DEFICIT)	
		2009	2008	2009	2008	2009	2008	2009	2008
		\$M	\$M	\$M	\$M	\$M	\$M	\$M	\$M
Defined benefit retirement plans⁽¹⁾									
Iron Trades insurance staff trust	31 Dec 09	262	289	(265)	(263)	-	(26)	(3)	-
European staff retirement benefit plan	31 Dec 09	10	11	(13)	(14)	-	-	(3)	(3)
Janson Green final salary superannuation scheme	31 Dec 09	179	189	(182)	(186)	-	(3)	(3)	-
QBE Australia defined benefit plan	31 Dec 09	48	68	(49)	(90)	-	-	(1)	(22)
QBE Regional pension plan	31 Dec 09	188	225	(253)	(293)	-	-	(65)	(68)
National Farmers Union property and casualty company uniform pension plan	31 Dec 09	21	25	(30)	(36)	-	-	(9)	(11)
Other plans		13	22	(23)	(27)	-	-	(10)	(5)
		721	829	(815)	(909)	-	(29)	(94)	(109)
Defined benefit post-employment health care plans⁽²⁾									
QBE Regional retiree health care plan	31 Dec 09	-	-	-	(1)	-	-	-	(1)
QBE Regional pension restoration plan	31 Dec 09	-	-	(11)	(13)	-	-	(11)	(13)
		-	-	(11)	(14)	-	-	(11)	(14)
		721	829	(826)	(923)	-	(29)	(105)	(123)

(1) Defined benefit retirement plan obligations are funded.

(2) Defined benefit post-employment health care plan obligations are unfunded.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

29 DEFINED BENEFIT PLANS CONTINUED

(B) Reconciliation

	2009 \$M	2008 \$M
Fair value of plan assets at 1 January	829	910
Expected return on plan assets	45	58
Actuarial gains (losses) on plan assets	29	(130)
Employer contributions	29	13
Contributions by plan participants	–	1
Benefits and expenses paid	(43)	(36)
Curtailments and settlements	(39)	–
Foreign exchange	(129)	13
Fair value of plan assets at 31 December	721	829
Defined benefit obligation at 1 January	(923)	(922)
Current service cost	(16)	(15)
Interest cost	(49)	(52)
Actuarial (losses) gains	(73)	27
Benefits and expenses paid	43	36
Past service cost	1	24
Contributions by plan participants	–	(1)
Curtailments and settlements	38	14
Foreign exchange	153	(34)
Defined benefit obligation at 31 December	(826)	(923)
Net deficit at 31 December	(105)	(94)
Surplus derecognised	–	(29)
Committed future contributions	(13)	(23)
Net deficit recognised in the balance sheet at 31 December	(118)	(146)

	2009 \$M	2008 \$M
Net deficit at 1 January	(94)	(12)
Amounts recognised in the income statement		
Current service cost	(16)	(15)
Interest cost	(49)	(52)
Past service cost	1	24
Expected return on plan assets	45	58
Curtailments and settlements	(1)	14
	(20)	29
Actuarial losses included in the statement of comprehensive income	(44)	(103)
Employer contributions	29	13
Foreign exchange	24	(21)
Net deficit at 31 December	(105)	(94)

The charge recognised in the income statement in the year of \$20 million (2008 \$29 million credit) has been included in underwriting expenses. The actual return on plan assets was a gain of \$74 million (2008 \$72 million loss).

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

29 DEFINED BENEFIT PLANS CONTINUED

(C) Amounts included in the statement of comprehensive income

Cumulative actuarial gains and losses included in the statement of comprehensive income are as follows:

	2009 \$M	2008 \$M
Actuarial losses at 1 January	193	75
Movement in the year	13	118
Actuarial losses at 31 December	206	193
Deferred taxation on actuarial losses at 1 January	(55)	(19)
Movement in the year	(2)	(36)
Deferred taxation on actuarial losses at 31 December	(57)	(55)
Net actuarial losses at 31 December	149	138

(D) Principal actuarial assumptions

	2009 %	2008 %
Discount rate	5.1 – 9.3	3.3 – 13.0
Expected return on plan assets	4.9 – 7.0	4.9 – 8.3
Future salary increases	3.5 – 8.0	3.1 – 8.0
Future pension increases	2.0 – 3.5	1.8 – 3.1

The expected return on plan assets is based on historical and future expectations of returns for each of the major asset classes as well as the expected and actual allocation of plan assets to these major classes.

(E) Analysis of plan assets

	2009 \$M	2008 \$M
Equities	214	234
Bonds	454	555
Property	1	1
Other	52	39
	721	829

(F) Historical summary

	2009 \$M	2008 \$M	2007 \$M	2006 \$M	2005 \$M	2004 \$M
Experience (losses) gains arising on plan liabilities	(9)	32	2	9	(6)	(42)
Experience gains (losses) arising on plan assets	29	(130)	(17)	(9)	39	7

	2009 \$M	2008 \$M	2007 \$M	2006 \$M	2005 \$M	2004 \$M
Present value of plan obligations	(826)	(923)	(922)	(725)	(726)	(698)
Fair value of plan assets	721	829	910	727	560	498
Net (deficit) surplus	(105)	(94)	(12)	2	(166)	(200)

(G) Funding

Employer contributions to the defined benefit retirement plans are based on recommendations by the plans' actuaries. The objective of the consolidated entity's funding schedules is to ensure that benefit entitlements are fully funded at the time they become payable. Total employer contributions expected to be paid to the various plans in 2010 amount to \$18 million.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

30 REMUNERATION OF AUDITORS

	2009 \$'000	2008 \$'000
PricewaterhouseCoopers – Australian firm⁽¹⁾		
Audit or review of financial reports of the parent entity	1,668	1,604
Audit of financial reports of controlled entities	3,547	3,032
Audit of statutory returns	1,042	815
Other audit assurance services	144	280
Taxation services	9	117
Actuarial services	61	74
Advisory services (including business continuity management assistance)	30	97
	6,501	6,019
Related practices of PricewaterhouseCoopers – Australian firm⁽¹⁾ (including overseas PricewaterhouseCoopers firms)		
Audit of financial reports of controlled entities	12,185	11,506
Audit of statutory returns	1,638	985
Other audit assurance services	172	306
Taxation services	621	941
Advisory services (including due diligence services)	30	157
	14,646	13,895
	21,147	19,914
Audit and assurance services	20,396	18,528
Other services	751	1,386
	21,147	19,914
Other auditors		
Audit of financial reports of controlled entities	165	154

(1) From 1 January 2003, the consolidated entity may engage PricewaterhouseCoopers for non-audit services, subject to the general principle that fees for non-audit services should not exceed 30% of the total of all fees in any one year. Consistent with prior periods, PricewaterhouseCoopers cannot provide the excluded services of preparing accounting records or financial reports, asset or liability valuations, acting in a management capacity, acting as a custodian of assets or acting as share registrar.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

31 CONTINGENT LIABILITIES

The company and the consolidated entity had the following contingent liabilities:

	THE COMPANY		CONSOLIDATED	
	2009 \$M	2008 \$M	2009 \$M	2008 \$M
Guarantees of interest-bearing liabilities in controlled entities	354	620	–	–
Letters of credit issued in support of the consolidated entity's participation in Lloyd's of London	1,080	948	1,080	948
Letters of credit issued in support of insurance provisions of controlled entities	831	848	–	–
Guarantees to investors in hybrid securities	465	772	–	–
Guarantees to investors in ABC securities for funds at Lloyd's (due 2009)	–	313	–	–
Guarantees to investors in capital securities	1,154	391	–	–

A controlled entity has entered into a number of deeds of covenant in respect of its controlled entities to meet part of their obligations to Lloyd's of London. The total guarantee given under these deeds of covenant amounts to \$nil (2008 \$126 million). The obligations under the deeds of covenant are secured by a fixed and floating charge over certain investments and other assets in favour of Lloyd's of London.

Controlled entities have entered into acquisition agreements. The costs of certain of these acquisitions have a contingent consideration component. The consolidated entity has made provision for the amount of contingent consideration that it expects to settle based on the achievement of specified performance criteria in future years. Details are provided in notes 18(F) and 23. Further amounts totalling \$243 million (2008 \$584 million) may be payable in the future subject to the achievement of performance criteria but are not considered probable at the balance sheet date.

Details of the guarantees to investors in Eurobonds, hybrid securities and capital securities and security arrangements in respect of borrowings are provided in note 24.

Details of contingent liabilities in respect of ABC securities for funds at Lloyd's are included in note 34.

32 CAPITAL EXPENDITURE COMMITMENTS (CONSOLIDATED)

	2009 \$M	2008 \$M
Capital expenditure commitments contracted but not provided for in the financial statements (not later than one year)	5	7

33 OPERATING LEASE COMMITMENTS (CONSOLIDATED)

	2009 \$M	2008 \$M
Payable:		
Not later than one year	79	85
Later than one year but not later than five years	199	213
Later than five years	325	391
Total future minimum lease payments under non-cancellable operating leases	603	689

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

34 ABC SECURITIES

	THE COMPANY		CONSOLIDATED	
	2009 \$M	2008 \$M	2009 \$M	2008 \$M
ABC financial assets pledged for funds at Lloyd's (due 2009)				
Interest-bearing short-term money £120 million	-	-	-	250
ABC securities for funds at Lloyd's (due 2009) US\$220 million	-	-	-	(312)
Swap (liability) asset relating to ABC securities	-	(1)	-	67

(A) ABC securities (redeemed in 2009)

In October 2004, the company entered into an arrangement with Mantis Reef II Limited ("MR(II)L") to issue US\$220 million of ABC (Asset Backed Capital) securities to support funds at Lloyd's ("FAL") pursuant to Lloyd's collateral requirements. This arrangement substantially replaced bank letters of credit and assisted in meeting FAL requirements. MR(II)L is a special purpose entity incorporated with limited liability under the laws of the Cayman Islands. The ABC securities were redeemed on 3 November 2009 in accordance with the terms of the ABC custody arrangement. The related swaps matured on the same date.

The swap agreement comprised three swaps which were measured at fair value. Two of the swaps were designated as cash flow hedges and satisfied the effectiveness tests throughout the period. The movement in the fair value of these cash flow hedges was taken to equity. An amount was transferred from equity and taken to the income statement to offset:

- the differential between the fixed and variable interest payments; and
- the foreign exchange gain or loss on translation of the financial liabilities.

During the year, a loss of \$79 million (2008 gain of \$96 million) was recognised in equity relating to the fair value movements on the cash flow hedges. During the year, a loss of \$67 million (2008 gain of \$90 million) was transferred from equity to the income statement.

(B) Fair value

The fair value of ABC securities (due 2009) is \$nil (2008 \$310 million).

(C) Risk exposure

The credit risk arising from swaps relating to ABC securities is \$nil (2008 \$67 million).

The maturity profile and the effective weighted average interest rate of ABC financial assets pledged for funds at Lloyd's and ABC securities for funds at Lloyd's are provided below.

As at 31 December 2008

		FIXED INTEREST RATE MATURING IN 1 YEAR OR LESS
ABC financial assets pledged for funds at Lloyd's	\$M	250
Weighted average interest rate	%	2.2
ABC securities for funds at Lloyd's	\$M	(312)
Weighted average interest rate	%	4.8

For an analysis of the sensitivity of the consolidated entity's financial instruments to market risks refer to note 5(A).

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

35 RELATED PARTIES (COMPANY AND CONSOLIDATED)

All material information required to be disclosed under AASB 124: Related Party Disclosures has been included in the financial statements as follows:

	REFERENCE
Dividends from controlled entities	Note 7(B)
Amounts due from controlled entities	Note 13
Investments in controlled entities	Note 18
Amounts due to controlled entities	Note 20
Tax sharing agreement	Note 8(B)
Remuneration of key management personnel	Directors' report and note 28
Retirement allowances of key management personnel	Directors' report
Shares and options held by key management personnel	Note 28
Related party transactions with key management personnel	Note 28(D)
Defined benefit plans	Note 29
Guarantees in respect of related parties	Note 31

In the ordinary course of business, various controlled entities receive dividends and purchase and sell investments in public entities in which directors of the company are directors and shareholders.

36 EARNINGS PER SHARE (CONSOLIDATED)

	2009 CENTS	2008 CENTS
Basic earnings per share	196.5	208.8
Diluted earnings per share	192.8	205.5

(A) Reconciliation of earnings used in calculating earnings per share

	2009 \$M	2008 \$M
Net profit after income tax attributable to ordinary equity holders of the company, used in calculating basic earnings per share	1,970	1,859
Add: finance costs of hybrid securities	27	3
Earnings used in calculating diluted earnings per share	1,997	1,862

(B) Reconciliation of weighted average number of ordinary shares used in calculating earnings per share

	2009 MILLION	2008 MILLION
Weighted average number of ordinary shares on issue	1,007	895
Weighted average number of non-recourse loan shares issued under the Plan	(4)	(5)
Weighted average number of treasury shares held in trust	-	-
Weighted average number of ordinary shares used as the denominator in calculating basic earnings per share ⁽¹⁾	1,003	890
Weighted average number of dilutive potential ordinary shares relating to:		
Shares issued under the Plan	4	5
Options issued under the Plan	2	2
Hybrid securities ⁽²⁾	27	9
Unvested conditional rights supported by treasury shares held in trust	-	-
Weighted average number of ordinary shares used as the denominator in calculating diluted earnings per share	1,036	906

(1) Weighted average number of ordinary shares reflects shares adjusted to derecognise shares issued under the Plan. Basic earnings per share calculated with reference to issued share capital notified to the ASX would have been 195.6 cents (2008 207.7 cents). Refer to note 25(A).

(2) If all hybrid securities had been included in the calculation of diluted earnings per share at 31 December 2009, diluted earnings per share would have been 192.8 cents (2008 205.9 cents).

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

37 SEGMENT INFORMATION

(A) Business segments

The consolidated entity is an international general insurance and reinsurance group underwriting most major commercial and personal lines classes of business through operations in 47 countries. The business is managed on a divisional basis as follows:

- Australian operations primarily underwrites general insurance risks throughout Australia providing all major lines of insurance cover for personal and commercial risks.
- Asia Pacific operations provides personal, commercial and specialist general insurance covers throughout the Asia Pacific region.
- European operations comprises QBE Insurance Europe and QBE Underwriting Limited (Lloyd's division). QBE Insurance Europe writes insurance business in the UK, Ireland and mainland Europe, and reinsurance business in Ireland. QBE Underwriting Limited underwrites reinsurance and commercial insurance in the Lloyd's market.
- the Americas writes insurance and reinsurance business in the US, Central and South America and Bermuda.
- Equator Re is based in Bermuda providing reinsurance protection to related entities and participating on reinsurances placed with external reinsurers.

The table below sets out key financial information relating to the divisions as reported internally to the board of directors, the Group operations executive and Group head office management being the management bodies responsible for the consolidated entity's strategy and operations. Intersegment transactions are priced on an arm's length basis and are eliminated on consolidation.

2009	AUSTRALIA \$M	ASIA PACIFIC \$M	EUROPEAN OPERATIONS \$M	THE AMERICAS \$M	EQUATOR RE \$M	ELIMINATION \$M	TOTAL \$M
Total assets	10,894	1,434	16,128	12,263	5,120	(4,875)	40,964
Total liabilities	8,339	970	13,432	9,088	3,712	(4,875)	30,666
Net assets	2,555	464	2,696	3,175	1,408	-	10,298
Property, plant and equipment	105	13	69	197	-	-	384
Investment properties	-	6	20	44	-	-	70
Intangible assets	1,739	24	602	2,649	-	-	5,014
Purchases of fixed assets	19	2	18	30	-	-	69
Depreciation expense	14	3	26	28	-	-	71
Purchases of intangible assets	457	-	22	(172)	-	-	307
Gross written premium	3,509	706	5,094	5,146	2,564	(2,564)	14,455
Gross earned premium	3,328	674	5,006	5,066	2,467	(2,467)	14,074
Outward reinsurance premium expense	(579)	(195)	(1,747)	(1,816)	(55)	2,467	(1,925)
Net earned premium	2,749	479	3,259	3,250	2,412	-	12,149
Net claims incurred	(1,670)	(223)	(2,010)	(1,992)	(1,433)	-	(7,328)
Net commission	(307)	(99)	(541)	(458)	(567)	-	(1,972)
Underwriting and other expenses	(469)	(100)	(426)	(465)	(127)	-	(1,587)
Underwriting result	303	57	282	335	285	-	1,262
Investment income on policyholders' funds	284	14	226	144	134	-	802
Insurance profit	587	71	508	479	419	-	2,064
Investment income on shareholders' funds	108	19	111	147	50	-	435
Amortisation of intangibles and impairment of goodwill/intangibles	(14)	-	(3)	(50)	-	-	(67)
Profit before income tax	681	90	616	576	469	-	2,432
Income tax expense	(101)	(22)	(146)	(178)	(1)	-	(448)
Profit after income tax	580	68	470	398	468	-	1,984
Net profit attributable to minority interests	(4)	(6)	(3)	(1)	-	-	(14)
Net profit after income tax attributable to ordinary equity holders of the company	576	62	467	397	468	-	1,970

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

37 SEGMENT INFORMATION CONTINUED

2008	AUSTRALIA \$M	ASIA PACIFIC \$M	EUROPEAN OPERATIONS \$M	THE AMERICAS \$M	EQUATOR RE \$M	ELIMINATION \$M	TOTAL \$M
Total assets	10,930	1,660	19,970	16,299	4,936	(5,412)	48,383
Total liabilities	8,108	1,051	17,230	12,270	3,891	(5,412)	37,138
Net assets	2,822	609	2,740	4,029	1,045	–	11,245
Property, plant and equipment	111	15	91	287	1	–	505
Investment properties	–	7	27	78	–	–	112
Intangible assets	1,296	25	642	3,623	–	–	5,586
Purchases of fixed assets	22	3	25	29	1	–	80
Depreciation expense	10	3	32	18	–	–	63
Purchases of intangible assets	600	–	–	2,264	–	–	2,864
Gross written premium	2,914	661	5,011	4,462	2,231	(2,137)	13,142
Gross earned premium	2,800	626	4,753	4,590	1,978	(1,894)	12,853
Outward reinsurance premium expense	(437)	(175)	(1,501)	(1,482)	(65)	1,894	(1,766)
Net earned premium	2,363	451	3,252	3,108	1,913	–	11,087
Net claims incurred	(1,485)	(186)	(1,762)	(1,872)	(1,083)	–	(6,388)
Net commission	(280)	(93)	(537)	(589)	(410)	–	(1,909)
Underwriting and other expenses	(377)	(95)	(483)	(449)	(111)	–	(1,515)
Underwriting result	221	77	470	198	309	–	1,275
Investment income on policyholders' funds	273	35	352	160	88	–	908
Insurance profit	494	112	822	358	397	–	2,183
Investment income on shareholders' funds	319	(16)	(42)	37	(29)	–	269
Amortisation of intangibles and impairment of goodwill/intangibles	–	–	(4)	(28)	–	–	(32)
Profit before income tax	813	96	776	367	368	–	2,420
Income tax expense	(253)	(15)	(201)	(85)	–	–	(554)
Profit after income tax	560	81	575	282	368	–	1,866
Net profit attributable to minority interest	–	(5)	(1)	(1)	–	–	(7)
Net profit after income tax attributable to ordinary equity holders of the company	560	76	574	281	368	–	1,859

(B) Geographical analysis

The business segments reported to management in the table above are defined by reference to the geographical locations of each division and as such satisfy the requirements of a geographical analysis as well as a business segment analysis.

Notes to the financial statements

FOR THE YEAR ENDED 31 DECEMBER 2009

38 RECONCILIATION OF CASH FLOWS FROM OPERATING ACTIVITIES TO NET PROFIT AFTER INCOME TAX ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE COMPANY

	THE COMPANY		CONSOLIDATED	
	2009 \$M	2008 \$M	2009 \$M	2008 \$M
Cash flows from operating activities	(599)	126	1,908	2,251
Depreciation of property, plant and equipment	-	-	(71)	(63)
Amortisation and impairment of goodwill/intangibles	-	-	(67)	(32)
Amortisation of premium/discount on fixed interest securities	-	-	(2)	11
Profit on sale of controlled entities	-	1	8	-
Loss on sale of plant and equipment	-	-	(1)	(11)
Net foreign exchange gains (losses)	253	(58)	92	104
Other (losses) gains on financial assets	(38)	(2,391)	426	(54)
Increase in net outstanding claims	-	-	(220)	(342)
Increase in unearned premium	-	-	(676)	(363)
Increase in deferred insurance costs	-	-	245	84
Increase in net amounts receivable from controlled entities	922	1,433	-	-
Increase (decrease) in trade debtors	17	-	(133)	598
Increase (decrease) in other operating assets	252	(266)	(35)	(111)
Decrease (increase) in trade payables	-	-	494	(209)
(Increase) decrease in tax liabilities	(10)	41	(26)	(120)
(Increase) decrease in other payables and provisions	(10)	44	42	123
Minority interest	-	-	(14)	(7)
Net profit (loss) after income tax attributable to ordinary equity holders of the company	787	(1,070)	1,970	1,859

Directors' declaration

In the directors' opinion:

- (a) the financial statements and notes set out on pages 80 to 157 are in accordance with the *Corporations Act 2001*, including:
 - (i) complying with accounting standards, the Corporations Regulations 2001 and other mandatory professional reporting requirements; and
 - (ii) giving a true and fair view of the company's and consolidated entity's financial position as at 31 December 2009 and of their performance, as represented by the results of their operations, changes in equity and their cash flows, for the financial year ended on that date; and
- (b) there are reasonable grounds to believe that the company will be able to pay its debts as and when they become due and payable.

The directors have been given the declarations by the chief executive officer and chief financial officer required by section 295A of the *Corporations Act 2001* for the financial year ended 31 December 2009.

Signed in SYDNEY this 26th day of February 2010 in accordance with a resolution of the directors.



EJ Cloney AM
Director



FM O'Halloran
Director

Independent auditor's report

TO THE MEMBERS OF QBE INSURANCE GROUP LIMITED

Report on the financial report

We have audited the accompanying financial statements of QBE Insurance Group Limited ("the company"), which comprise the balance sheets as at 31 December 2009 and the income statements, the statements of comprehensive income, statements of changes in equity and statements of cash flows for the year ended on that date, a summary of significant accounting policies, other explanatory notes and the directors' declaration for both QBE Insurance Group Limited and the QBE Insurance Group ("the consolidated entity"). The consolidated entity comprises the company and the entities it controlled at the year's end or from time to time during the financial year.

Directors' responsibility for the financial report

The directors of the company are responsible for the preparation and fair presentation of the financial report in accordance with Australian Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Act 2001*. This responsibility includes establishing and maintaining internal controls relevant to the preparation and fair presentation of the financial report that is free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances. In note 1, the directors also state, in accordance with Accounting Standard AASB 101 Presentation of Financial Statements, that compliance with the Australian equivalents to International Financial Reporting Standards ensures that the financial report, comprising the financial statements and notes, complies with International Financial Reporting Standards.

Auditor's responsibility

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

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

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

Our audit did not involve an analysis of the prudence of business decisions made by directors or management.

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

Independence

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

Auditor's opinion

In our opinion:

- (a) the financial report of QBE Insurance Group Limited is in accordance with the *Corporations Act 2001*, including:
 - (i) giving a true and fair view of the company's and consolidated entity's financial position as at 31 December 2009 and of their performance for the year ended on that date; and
 - (ii) complying with Australian Accounting Standards (including the Australian Accounting Interpretations) and the Corporations Regulations 2001; and
- (b) the financial report also complies with International Financial Reporting Standards as disclosed in note 1.

Report on the remuneration report

We have audited the Remuneration Report included in pages 56 to 76 of the directors' report for the year ended 31 December 2009. The directors of the company are responsible for the preparation and presentation of the remuneration report in accordance with section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the remuneration report, based on our audit conducted in accordance with Australian Auditing Standards.

Auditor's opinion

In our opinion, the remuneration report of QBE Insurance Group Limited for the year ended 31 December 2009 complies with section 300A of the *Corporations Act 2001*.

PricewaterhouseCoopers

Sydney
26 February 2010

KG Smith
Partner

Liability limited by a scheme approved under Professional Standards Legislation

Annual financial report extracts presented in US dollars

31 DECEMBER 2009

The audited annual financial statements of the consolidated entity presented in Australian dollars are included in pages 80 to 157.

On pages 161 to 166, extracts from the audited financial statements are presented in US dollars ("US\$"). This information does not form part of the audited annual financial statements. This information is presented as a simple translation using the following rates of exchange to the Australian dollar:

	2009 US\$	2008 US\$
Income statement and cash flows	0.778	0.838
Balance sheet and equity	0.896	0.702

Opening retained earnings at 1 January 2008 have been translated to US dollars using the balance date rate of \$US0.877. Profit and loss amounts for each financial year are translated to US dollars using the appropriate cumulative average rate of exchange. Dividends are translated at rates of exchange relevant to the period during which the relevant retained profits were earned. The impact of foreign exchange movements is included in reserves on the balance sheet.

The extracts included are as follows:

Consolidated US dollar balance sheet	161
Consolidated US dollar income statement	162
Consolidated US dollar statement of cash flows	163
Selected notes to the financial statements in US dollars	164

Consolidated US dollar balance sheet

AS AT 31 DECEMBER 2009

	NOTE	2009 US\$M	2008 US\$M
ASSETS			
Financial assets at fair value through profit or loss			
Cash and cash equivalents	10	1,435	1,921
Investments	11	20,995	18,038
ABC financial assets pledged for funds at Lloyd's	34	–	175
Derivative financial instruments	12	133	609
Swaps relating to ABC securities	34	–	47
Trade and other receivables	13	3,855	3,539
Reinsurance and other recoveries on outstanding claims	22	3,302	3,540
Current tax assets		126	55
Other assets		38	58
Deferred insurance costs	14	1,753	1,395
Defined benefit plan surplus	29	2	1
Property, plant and equipment	15	344	354
Deferred tax assets	16	182	234
Investment properties	17	63	79
Intangible assets	19	4,495	3,922
Total assets		36,723	33,967
LIABILITIES			
Financial liabilities at fair value through profit or loss			
Derivative financial instruments	12	36	786
Trade and other payables	20	1,178	1,400
Current tax liabilities		189	227
Unearned premium	21	6,127	5,003
ABC securities for funds at Lloyd's	34	–	219
Outstanding claims	22	16,166	14,886
Provisions	23	536	501
Defined benefit plan deficit	29	108	104
Deferred tax liabilities	16	488	373
Borrowings	24	2,663	2,574
Total liabilities		27,491	26,073
Net assets		9,232	7,894
EQUITY			
Share capital	25(A)	6,604	4,714
Share capital, fully paid yet to be issued	25(B)	–	81
Treasury shares held in trust	25(C)	(1)	(1)
Equity component of hybrid securities	25(D)	102	80
Reserves	26	(1,828)	(840)
Retained profits		4,287	3,800
Shareholders' funds		9,164	7,834
Minority interests	18(D)	68	60
Total equity		9,232	7,894

The note references above are to the notes to the audited financial statements on pages 87 to 157.

Consolidated US dollar income statement

FOR THE YEAR ENDED 31 DECEMBER 2009

	NOTE	2009 US\$M	2008 US\$M
REVENUE			
Premium revenue		10,943	10,773
Other revenue		1,511	2,402
Net fair value gains on financial assets		358	–
Realised gains on sale of controlled entities		6	–
Investment income – ABC financial assets pledged for funds at Lloyd's		101	186
	6	12,919	13,361
EXPENSES			
Outward reinsurance premium expense		1,497	1,480
Gross claims incurred		6,342	6,490
Other expenses	7(C)	2,873	2,929
Net fair value losses on financial assets		–	28
Net fair value losses on investment properties		16	–
Net fair value losses on owner occupied properties		23	–
Expenses – ABC securities for funds at Lloyd's		107	205
Finance costs		170	201
Profit before income tax	7	1,891	2,028
Income tax expense	8	348	464
Profit after income tax		1,543	1,564
Net profit attributable to minority interests		11	6
Net profit after income tax attributable to ordinary equity holders of the company		1,532	1,558
Earnings per share for net profit after income tax attributable to ordinary equity holders of the company			
	NOTE	2009 US\$ CENTS	2008 US\$ CENTS
Basic earnings per share	36	152.8	175.0
Diluted earnings per share	36	149.9	172.2

The note references above are to the notes to the audited financial statements on pages 87 to 157.

Consolidated US dollar statement of cash flows

FOR THE YEAR ENDED 31 DECEMBER 2009

	NOTE	2009 US\$M	2008 US\$M
OPERATING ACTIVITIES			
Premium received		11,144	10,978
Reinsurance and other recoveries received		1,092	1,170
Outward reinsurance paid		(1,537)	(1,417)
Claims paid		(6,557)	(6,413)
Insurance costs paid		(2,035)	(2,263)
Other underwriting costs		(705)	(778)
Interest received		523	950
Dividends received		40	55
Other operating income		23	12
Other operating payments		(97)	(49)
Interest paid		(121)	(135)
Income taxes paid		(287)	(224)
Net cash flows from operating activities	38	1,483	1,886
INVESTING ACTIVITIES			
Proceeds on sale of equity investments		760	851
Proceeds on sale of investment property		–	2
Proceeds on sale of property, plant and equipment		6	6
Payments for purchase of equity investments		(772)	(1,180)
(Payments for) proceeds from foreign exchange transactions		(614)	(413)
(Payments for) proceeds from purchase of other financial assets		(674)	1,453
Payments for purchase of controlled entities and businesses acquired ⁽¹⁾		(93)	(1,987)
Proceeds on disposal of controlled entities		11	–
Payments for purchase of investment property		(1)	–
Payments for purchase of property, plant and equipment		(54)	(60)
Net cash flows from investing activities		(1,431)	(1,328)
FINANCING ACTIVITIES			
Proceeds from issue of shares		–	1,773
(Refund of) proceeds from over-subscribed portion of share issue		(87)	94
Payments for purchase of treasury shares		(15)	(8)
Share issue expenses		(3)	(27)
Proceeds from settlement of staff share loans		11	9
Proceeds from borrowings		933	335
Repayment of borrowings		(875)	(186)
Repayment of ABC securities		–	(550)
Dividends paid		(664)	(895)
Net cash flows from financing activities		(700)	545
NET MOVEMENT IN CASH AND CASH EQUIVALENTS			
Cash and cash equivalents at the beginning of the financial year		1,921	866
Effect of exchange rate changes		162	(48)
Cash and cash equivalents at the end of the financial year	10	1,435	1,921

(1) Net of cash acquired.

The note references above are to the notes to the audited financial statements on pages 87 to 157.

Selected notes to the financial statements in US dollars

FOR THE YEAR ENDED 31 DECEMBER 2009

7 PROFIT BEFORE INCOME TAX

(A) Profit before income tax (consolidated)

	NOTE	2009 US\$M	2008 US\$M
Gross written premium		11,239	11,015
Unearned premium movement		(296)	(242)
Gross earned premium		10,943	10,773
Outward reinsurance premium		(1,610)	(1,418)
Deferred reinsurance premium movement		113	(62)
Outward reinsurance premium expense		(1,497)	(1,480)
Net earned premium		9,446	9,293
Gross claims incurred		(6,342)	(6,490)
Reinsurance and other recoveries		644	1,136
Net claims incurred	9	(5,698)	(5,354)
Net commission		(1,533)	(1,600)
Other acquisition costs		(550)	(509)
Underwriting and other expenses ⁽¹⁾		(684)	(761)
		(8,465)	(8,224)
Underwriting profit		981	1,069
Investment income on policyholders' funds		624	761
Insurance profit		1,605	1,830
Investment income on shareholders' funds		338	226
Amortisation of intangibles and impairment of goodwill/intangibles		(52)	(28)
Profit before income tax		1,891	2,028

(1) Includes US\$235 million (2008 US\$87 million) of agency income earned by the consolidated entity's agency operations which is treated as a recovery of the consolidated entity's underwriting expenses.

Selected notes to the financial statements in US dollars

FOR THE YEAR ENDED 31 DECEMBER 2009

7 PROFIT BEFORE INCOME TAX CONTINUED

(B) Net investment and other income

	CONSOLIDATED	
	2009 US\$M	2008 US\$M
Dividends from non-related entities	40	54
Interest received or receivable from non-related entities	535	870
Other investment income	8	–
Investment and dividend income	583	924
Investment income – ABC financial assets pledged for funds at Lloyd's	101	186
Net realised (losses) gains – equities and investment properties	(285)	33
Net realised gains – fixed interest and other	218	172
Net unrealised gains (losses) – equities and investment properties	344	(497)
Net unrealised gains – fixed interest and other	10	11
Net unrealised losses on owner occupied properties	(23)	–
Realised gains on sale of controlled entities	6	–
Gain on repurchase of debt securities ⁽¹⁾	55	254
Foreign exchange gains ^(2,3)	284	342
Investment and other income	1,293	1,425
Expenses – ABC securities for funds at Lloyd's	(107)	(205)
Finance costs paid or payable to non-related entities	(170)	(201)
Investment expenses	(54)	(32)
Foreign exchange losses	–	–
Net investment and other income	962	987
Investment income on policyholders' funds	624	761
Investment income on shareholders' funds	338	226
Net investment and other income	962	987

(1) Gains arose principally on the repurchase of capital securities. Details are provided in note 24.

(2) 2009 realised foreign exchange gains include US\$191 million arising following a change in the consolidated entity's approach to hedging its net investment in foreign operations.

(3) 2008 realised foreign exchange gains include US\$318 million arising from forward foreign exchange contracts entered into to protect the consolidated entity's cash position against foreign currency volatility on the acquisition of QBE Lenders' Mortgage Insurance (Holdings) Pty Limited. This entity was acquired in October 2008 and the purchase price was payable in US dollars.

Selected notes to the financial statements in US dollars

FOR THE YEAR ENDED 31 DECEMBER 2009

7 PROFIT BEFORE INCOME TAX CONTINUED

(C) Other expenses

	CONSOLIDATED	
	2009 US\$M	2008 US\$M
Commission	1,533	1,600
Other acquisition costs	550	509
Underwriting and other expenses	684	761
Investment expenses	54	32
Amortisation of intangibles and impairment of goodwill/intangibles	52	27
Foreign exchange losses	-	-
Other expenses	2,873	2,929

(D) Specific items

	CONSOLIDATED	
	2009 US\$M	2008 US\$M
Defined contribution superannuation plan expense	32	33
Payments on operating leases	72	85
Depreciation of property, plant and equipment	55	53

Shareholder information

QBE is incorporated in Australia, is listed on the Australian Securities Exchange ("ASX") and trades under the code "QBE".

Annual General Meeting ("AGM")

Time: 11:00am Wednesday, 31 March 2010

The Westin Hotel, 1 Martin Place, Sydney NSW Australia

Online proxy voting is available through the Link investor service centre website.

Voting rights of ordinary shares

The constitution provides for votes to be cast:

- on a show of hands, one vote for each shareholder; and
- on a poll, one vote for each fully paid ordinary share.

Shareholder information and enquiries

Most enquiries and correspondence regarding shareholdings can be directed to QBE's share registrar:

Link Market Services Limited ("Link")

Locked Bag A14, Sydney South NSW 1235 Australia

Level 12, 680 George Street, Sydney NSW 2000 Australia

Telephone: +61 2 8280 7158

Facsimile: +61 2 9287 0303

Internet: www.linkmarketservices.com.au (Link investor service centre website)

Email: registrars@linkmarketservices.com.au

For security purposes, please quote your Securityholder Reference Number ("SRN") or Holder Identification Number ("HIN").

If you are broker (CHESS) sponsored, queries relating to incorrect registrations and changes to name and/or address can only be processed by your stockbroker. Link cannot assist you with these changes. Please quote your HIN.

Relevant interests register

Orient Capital Pty Limited of Level 12, 680 George Street, Sydney NSW 2000, Australia maintains QBE's register of information about relevant interests. The register contains any responses from custodians on and after 1 January 2005 to searches relating to the beneficial ownership of QBE's shares. Shareholders and other parties can telephone Orient Capital on +61 2 8280 6000 or facsimile on +61 2 8280 6001 if they wish to inspect this register.

Shareholding details online

View your shareholdings and update your details online at the Link investor service centre website. You will be asked to provide either your SRN or HIN, your surname and postcode.

You may receive dividend statements, notices of meetings, annual reports and major company announcements electronically by registering your email address at the Link investor service centre website.

Annual report mailing list

Amendments to the Corporations Act have removed the obligation for companies to mail an annual report to shareholders. To improve efficiency, save costs and reduce our impact on the environment by minimising unnecessary use of paper and printing resources, the annual report is published on our website at www.qbe.com.

If you wish to receive a hard copy of the annual report, please notify Link in writing or select the annual report option under "communication options" on the Link investor service centre website.

The half yearly results summary to 30 June 2010 will be mailed with the interim dividend. The next annual report for the year ending 31 December 2010 will be distributed in March 2011. QBE does not produce a concise financial report.

Shareholder information

Tax File Number (“TFN”), Australian Business Number (“ABN”) or exemption – Australian residents

You can confirm whether you have lodged your TFN, ABN or exemption by visiting the Link investor service centre website. If you choose not to lodge these details, QBE is obliged to deduct tax at the highest marginal rate (plus the Medicare levy) from the unfranked portion of dividends paid. Australian shareholders living abroad should advise Link of their resident status. TFN forms are available from Link or can be downloaded from either the QBE or Link websites.

Conduit foreign income (“CFI”)

Shareholders will receive CFI credits in respect of the whole unfranked portion of QBE dividends. These credits exempt non-resident shareholders from Australian withholding tax.

Dividends

QBE encourages shareholders to have cash dividends credited directly to a bank, building society or credit union account in either Australia or New Zealand to eliminate delays in funds clearance and to significantly reduce the risk of loss or theft. A dividend advice confirming the deposit details is either mailed to you or is available online on the payment date.

Eligible shareholders can participate in QBE's Dividend Reinvestment Plan (“DRP”) and Bonus Share Plan (“BSP”) when the plans are active. The DRP enables you to subscribe for additional shares. The BSP is a bonus share plan whereby the dividend entitlement is forgone for bonus shares in lieu of the dividend. In order to participate in either the DRP or BSP, you must have a minimum shareholding of 100 shares.

Participants may change their election to participate in the DRP and BSP at any time. DRP/BSP election cut-off dates and application forms are available from QBE's website.

Unpresented cheques/unclaimed money

Under the Unclaimed Moneys Act, unclaimed dividends must be given to the NSW state treasury. It is very important that shareholders bank outstanding dividend cheques promptly and advise Link immediately of changes of address or bank account details.

Privacy legislation

Chapter 2C of the *Corporations Act 2001* requires information about you as a security holder (including your name, address and details of the securities you hold) to be included in QBE's share register. These details must continue to be included in the public register even if you cease to be a security holder. A copy of the privacy policy is available on Link's website.

Registered office

QBE Insurance Group Limited
Level 2, 82 Pitt Street, Sydney NSW 2000 Australia

Telephone: +61 2 9375 4444

Facsimile: +61 2 9235 3166

Internet: www.qbe.com

QBE website

QBE's website provides investors with information about QBE including annual reports, half yearly reports and announcements to the ASX. The website also offers regular QBE share price updates, a calendar of events, a brief history of QBE's dividends, access to standard forms (change of address, direct credit advice and more) and online access to your shareholding details via the share registry.

Shareholder information

RECENT QBE DIVIDENDS

DATE PAID	TYPE	RECORD DATE	CENTS PER SHARE	FRANKING %
31 March 2000	interim	10 March 2000	14.0	10
29 September 2000	final	11 September 2000	15.0	35
12 April 2001	final	26 March 2001	16.0	30
28 September 2001	interim	7 September 2001	16.5	25
12 April 2002	final	25 March 2002	13.5	15
3 October 2002	interim	13 September 2002	16.5	12
11 April 2003	final	19 March 2003	18.5	12
25 September 2003	interim	1 September 2003	20.0	15
25 March 2004	final	9 March 2004	22.0	30
20 September 2004	interim	30 August 2004	24.0	50
23 March 2005	final	7 March 2005	30.0	50
16 September 2005	interim	29 August 2005	33.0	50
29 March 2006	final	10 March 2006	38.0	50
14 September 2006	interim	1 September 2006	40.0	60
2 April 2007	final	14 March 2007	55.0	60
21 September 2007	interim	10 September 2007	57.0	60
26 March 2008	final	6 March 2008	65.0	50
17 September 2008	interim	1 September 2008	61.0	20
31 March 2009	final	11 March 2009	65.0	20
22 September 2009	interim	1 September 2009	62.0	20

TOP 20 SHAREHOLDERS AS AT 31 JANUARY 2010

NAME	NUMBER OF SHARES	% OF TOTAL ⁽¹⁾
HSBC Custody Nominees (Australia) Limited	286,453,055	27.95
J P Morgan Nominees Australia Limited	180,694,422	17.63
National Nominees Limited	141,022,350	13.76
Citicorp Nominees Pty Limited	62,414,578	6.09
ANZ Nominees Limited	21,142,695	2.06
RBC Dexia Investor Services c/- Australian Nominees Pty Limited	20,477,664	2.00
Cogent Nominees Pty Limited	20,154,142	1.97
Queensland Investment Corporation c/- National Nominees Limited	8,206,369	0.80
AMP Life Limited	8,044,240	0.78
Bond Street Custodians Limited	7,335,748	0.72
UBS Nominees Pty Ltd	5,788,952	0.57
Perpetual Trustee Company Limited	5,153,890	0.50
Invia Custodian Pty Limited	5,037,633	0.49
Australian Foundation Investment Company Limited	4,136,370	0.40
UBS Wealth Management c/- Australian Nominees Pty Limited	3,939,580	0.38
Australian Reward Investment Alliance c/- JP Morgan Nominees Australia Limited	3,386,666	0.33
Argo Investments Limited	3,086,095	0.30
Avanteos Investments Limited	2,744,129	0.27
BT Portfolio Services Limited	2,141,776	0.21
QBE Management Services Pty Ltd	2,085,732	0.20
Total	793,446,086	77.41

(1) Percentage of total at date of notice.

Shareholder information

QBE SUBSTANTIAL SHAREHOLDERS AS AT 31 JANUARY 2010

NAME	NUMBER OF SHARES	% OF TOTAL ⁽¹⁾	DATE OF NOTICE
Credit Suisse Holdings (Australia) Limited	69,890,441	6.9%	24 August 2009
Aberdeen Asset Management Asia Limited	61,721,007	6.0%	22 October 2009
Blackrock Investment Management (Australia) Limited	52,569,915	5.1%	2 December 2009

(1) Percentage of total at date of notice.

DISTRIBUTION OF SHAREHOLDERS AND SHAREHOLDINGS AS AT 31 JANUARY 2010

SIZE OF HOLDING	NUMBER OF SHAREHOLDERS	%	NUMBER OF SHARES	%
1 to 1000	86,205	63	39,823,071	3.89
1001 to 5000	43,155	32	89,931,324	8.77
5001 to 10000	4,161	3	29,018,599	2.83
10001 to 100000	2,149	2	47,011,472	4.59
100001 and over	182	0	819,250,752	79.92
Total	135,852	100	1,025,035,218	100.00

SHAREHOLDINGS OF LESS THAN A MARKETABLE PARCEL AS AT 31 JANUARY 2010

	SHAREHOLDERS		SHARES	
	NUMBER	% OF TOTAL	NUMBER	% OF TOTAL
Holdings of 22 or fewer shares	1,177	0.87	13,180	0.00

Financial calendar and ASX announcements

FINANCIAL CALENDAR

2010

26 February	Profit and dividend announcement for the year ended 31 December 2009 Annual report available on website Annual report mailed as requested
1 March	Notice of Meeting and proxy form mailed to shareholders
3 March	Shares begin trading ex-dividend
10 March	Record date for determining shareholders' entitlement to 2009 final dividend
30 March	2009 final dividend paid
31 March	Annual General Meeting
30 June	Half year end
19 August*	Profit and dividend announcement for the six months ending 30 June 2010
24 August*	Shares begin trading ex-dividend
30 August*	Record date for determining shareholders' entitlement to 2010 interim dividend
22 September*	2010 interim dividend paid
31 December	Year end

* Dates shown are provisional and may be subject to change.

MATERIAL ANNOUNCEMENTS TO THE ASX

2010

Announced the appointment of a new non-executive director	16 February
Variations to the rules of QBE's dividend reinvestment plans	25 January and 9 February

2009

Announced change of interests of substantial holder in relation to Austbrokers	24 December
Announced conversion of hybrid securities into ordinary shares of the company	9 November
Announced change of interests of substantial holder in relation to Elders	4 November and 24 December
Investor update	2 November
Announced becoming substantial holder for Elders	19 October
CFO presentation to JP Morgan New York conference	6 October
Announced the completion of the Elders insurance businesses acquisition	30 September
Announced senior debt issue	23 September
Announced interim dividend details	21 August, 25 August and 10 September
Announced a record first half year profit	20 August
Announced final conversion of hybrid securities into ordinary shares of the company	7 August
Announced the acquisition of Elders insurance businesses	31 July
Announced conversion of hybrid securities into ordinary shares of the company	24 July and 5 August
Announced Standard & Poor's rating for QBE Lenders' Mortgage Insurance and QBE Mortgage Insurance (Asia) affirmed at AA- and outlook revised from negative to stable	15 July
Announced Standard & Poor's rating for QBE Insurance Group Limited raised from A- to A with a stable outlook	9 July
CFO presentation to Macquarie Australia conference in Sydney	7 May
2009 AGM	8 April
Chairman's message to major investors	1 April
Announced DCP option exercise	11 March
CEO presentation to Citi Australia and New Zealand investment conference in London	9 March
Announced dividend pricing details and the reinstatement of the Dividend Reinvestment Plan	27 February and 11 March
Announced 2008 results	26 February
Announced issue of shares under the share purchase plan	20 January
Provided progress updates on share purchase plan	9, 16 and 20 January
Advised change in directors' interests in shares of the company	27 and 29 January, 5 and 11 March, 3, 9, 24 and 28 April, 26 June and 1, 18, 25 and 28 September

Glossary of insurance terms

Accident year experience	Simplistically, the matching of all claims occurring (regardless of when reported or paid) during a given 12 month period with all premium earned over the same period.
Attritional claims ratio	Total net claims with a cost of less than \$2.5 million as a percentage of net earned premium.
Broker	One who negotiates contracts of insurance or reinsurance on behalf of an insured party, receiving a commission from the insurer or reinsurer for placement and other services rendered.
Casualty insurance	Insurance that is primarily concerned with the losses caused by injuries to third persons or their property (i.e. not the policyholder) and the resulting legal liability imposed on the insured. It includes, but is not limited to, general liability, employers' liability, workers' compensation, professional liability, public liability and motor liability insurance.
Catastrophe reinsurance	A form of excess of loss reinsurance that, subject to specified limits, indemnifies the insured for the amount of loss in excess of a specified retention with respect to an accumulation of claims resulting from a catastrophe event or series of events.
Claim	The amount payable under a contract of insurance or reinsurance arising from a loss relating to an insured event.
Claims incurred	The aggregate of all claims paid during an accounting period adjusted by the change in the claims provision for that accounting period.
Claims provision	The estimate of the most likely cost of settling present and future claims and associated claims adjustment expenses plus a risk margin for the possible fluctuation of the liability.
Combined operating ratio	The sum of the claims ratio, commission ratio and expense ratio. A combined operating ratio below 100% indicates profitable underwriting results. A combined operating ratio over 100% indicates unprofitable underwriting results.
Commission ratio	Net commission expense as a percentage of net earned premium.
Excess of loss reinsurance	A form of reinsurance in which, in return for a premium, the reinsurer accepts liability for claims settled by the original insurer in excess of an agreed amount, generally subject to an upper limit.
Expense ratio	Underwriting and administrative expenses as a percentage of net earned premium.
Facultative reinsurance	The reinsurance of individual risks through a transaction between the reinsurer and the cedant (usually the primary insurer) involving a specified risk.
General insurance	Generally used to describe non-life insurance business including property and casualty insurance.
Gross claims incurred	The amount of claims incurred during an accounting period before deducting reinsurance recoveries.
Gross earned premium	The total premium on insurance earned by an insurer or reinsurer during a specified period on premiums underwritten in the current and previous underwriting years.
Gross written premium	The total premium on insurance underwritten by an insurer or reinsurer during a specified period, before deduction of reinsurance premium.
Incurred but not reported (IBNR)	Claims arising out of events that have occurred before the end of an accounting period but have not been reported to the insurer by that date.
Insurance profit	The sum of the underwriting profit (loss) and investment income on policyholders' funds.
Insurance solvency ratio	Ratio of net tangible assets to net earned premium. This is an important industry indicator in assessing the ability of general insurers to settle their existing liabilities.
Inward reinsurance	The reinsurance or assumption of risks written by another insurer.
Large individual risk and catastrophe claims ratio	The aggregate of claims each with a cost of \$2.5 million or more as a percentage of net earned premium.
Lenders' mortgage insurance (LMI)	A policy which protects the lender (e.g. a bank) against non-payment or default on a residential property loan.
Long-tail	Classes of insurance business involving coverage for risks where notice of a claim may not be received for many years and claims may be outstanding for more than one year before they are finally settled and quantifiable by the insurer.
Net claims incurred	The amount of claims incurred during an accounting period after deducting reinsurance recoveries.
Net claims ratio	Net claims incurred as a percentage of net earned premium.
Net earned premium	Net written premium adjusted by the net change in unearned premium for a year.
Net investment income	Gross investment income net of finance costs, foreign exchange gains and losses and investment expenses.
Net written premium	The total premium on insurance underwritten by an insurer during a specified period after the deduction of premium applicable to reinsurance.
Outstanding claims provision	The amount of provision established for claims and related claims expenses that have occurred but have not been paid.
Policyholders' funds	Those financial assets held to fund the insurance liabilities of the consolidated entity.
Premium	Amount payable by the insured or reinsured in order to obtain insurance or reinsurance protection.
Proportional reinsurance	A type of reinsurance in which the original insurer and the reinsurer share claims in the same proportion as they share premiums.
Recoveries	The amount of claims recovered from reinsurance, third parties or salvage.
Reinsurance	An agreement to indemnify a primary insurer by a reinsurer in consideration of a premium with respect to agreed risks insured by the primary insurer. The enterprise accepting the risk is the reinsurer and is said to accept inward reinsurance. The enterprise ceding the risks is the cedant or ceding company and is said to place outward reinsurance.
Reinsurer	The insurer that assumes all or part of the insurance or reinsurance liability written by another insurer. The term includes retrocessionaires, being insurers that assume reinsurance from a reinsurer.
Retention	That amount of liability for which an insurance company will remain responsible after it has completed its reinsurance arrangements.
Short-tail	Classes of insurance business involving coverage for risks where notice of a claim is received and claims are outstanding for one year or less before they are finally quantifiable and settled by the insurer.
Survival ratio	A measure of how many years it would take for dust disease claims to exhaust the current level of claims provision. It is calculated on the average level of claims payments in the last three years.
Treaty reinsurance	Reinsurance of risks in which the reinsurer is obliged by agreement with the cedant to accept, within agreed limits, all risks to be underwritten by the cedant within specified classes of business in a given period of time.
Underwriting	The process of reviewing applications submitted for insurance or reinsurance coverage, deciding whether to provide all or part of the coverage requested and determining the applicable premium.
Underwriting expenses	The aggregate of policy acquisition costs, excluding commissions, and the portion of administrative, general and other expenses attributable to underwriting operations.
Underwriting profit (loss)	The amount of profit (loss) from insurance activities exclusive of net investment income and capital gains or losses.
Underwriting year	The year in which the contract of insurance commenced or was underwritten.
Unearned premium	The portion of a premium representing the unexpired portion of the contract term as of a certain date.
Written premium	Premiums written, whether or not earned, during a given period.



QBE Insurance Group Limited

82 Pitt Street
Sydney 2000 Australia
Phone +61 2 9375 4444

www.qbe.com



**QBE INSURANCE GROUP LIMITED
MARKET ANNOUNCEMENT**

QBE ANNOUNCES INCREASE IN 2009 PROFIT AND DIVIDEND

QBE announced today that its 2009 net profit after tax increased by 6% to \$1,970 million. This followed a year of continuing volatility in financial markets and a strengthening Australian dollar. Despite the difficult economic conditions and historically low interest rates, QBE produced an excellent return on equity of 18.4%, compared with 20.9% last year.

In recognition of the solid return on equity and profit increase, the directors have declared a final dividend of 66 cents per share compared with 65 cents last year. The total dividend for 2009 is 128 cents per share, up from 126 cents for the previous year. Total dividend payout for 2009 is up 10% to \$1,306 million. The franking rate will remain at 20% due to the substantial profits generated from overseas operations. Books close on 10 March and final dividend is payable 30 March. The Dividend Reinvestment Plan and Bonus Share Plan will continue but at no discount.

As was the case in 2008, the 2009 pre tax profit includes a number of significant items resulting from the volatility caused by the global financial crisis and the subsequent economic downturn. In particular:

- claims directly attributable to the global financial crisis of \$144 million, compared with \$200 million last year;
- unrealised losses of \$50 million on the revaluation of owner occupied properties, mainly in the US;
- continued low yields on cash and fixed interest investments, adversely impacting investment income by \$300 million;
- foreign exchange gains of \$365 million, compared with gains of \$409 million last year;
- profit of \$70 million on repurchase of QBE debt, compared with a profit of \$303 million last year; and
- net realised and unrealised gains on equities of \$97 million, compared with a net loss of \$554 million last year.

Gross written premium income was up 10% to \$14,455 million and net earned premium was up 10% to \$12,149 million. QBE's combined operating ratio (that is the ratio of claims, commissions and expenses to net earned premium) was an excellent 89.6% in the circumstances, compared with 88.5% last year. The insurance profit margin to net earned premium was a strong 17.0% at the mid point of our original target range. The insurance profit margin was after lower interest yields on investments set aside to meet our obligations to policyholders, significantly lower savings on prior year claims provisions and a 0.6% impact from a prudent upgrade of old latency claims.

Mr Frank O'Halloran, QBE's Group Chief Executive Officer, said "2009 is the fifth year in succession that we have produced a combined operating ratio of less than 90%. The substantial majority of our products and the 47 countries in which we operate continue to exceed our minimum return on equity requirements of 15%. QBE's careful and prudent approach to management of its substantial cash and fixed interest portfolio has assisted in achieving a very satisfactory overall investment performance and no permanent impairment on any one security."

Frank O'Halloran continued "QBE made four acquisitions in 2009 which will assist premium growth in 2010. Premium growth is expected to be 3% in Australian dollars or 18% in US dollars at current exchange rates. Our balance sheet is well positioned for further acquisitions and distribution opportunities to enhance our diverse product range and geographic spread."

"Subject to the usual caveats, including large risk claims and catastrophes not exceeding the substantial allowance in our business plan, we expect underwriting profitability to improve in 2010."

"QBE's cash and fixed interest portfolio remains short in duration which means that a rise in interest rates will be very beneficial for our profit."

For further information, please either phone +61 2 9375 4636 or email investor.relations@qbe.com.

26 February 2010