
# NUMBERS.

**INSURANCE AUSTRALIA GROUP LIMITED**
ANNUAL REPORT 2017

ABN 60 090 739 923

## CONTENTS



## KEY DATES

| | |
|---|---|
| 2017 financial year end | 30 June 2017 |
| Full year results and dividend announcement | 23 August 2017 |
| Notice of meeting mailed to shareholders | 5 September 2017 |
| Final dividend for ordinary shares | |
| Record date | 7 September 2017 |
| Payment date | 9 October 2017 |
| Annual general meeting | 20 October 2017 |
| Half year end | 31 December 2017 |
| Half year results and dividend announcement | 14 February 2018* |
| Interim dividend for ordinary shares | |
| Record date | 21 February 2018* |
| Payment date | 29 March 2018* |
| 2018 financial year end | 30 June 2018 |
| Full year results and dividend announcement | 15 August 2018* |

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

### ABOUT THIS REPORT

The 2017 annual report of Insurance Australia Group Limited (IAG, or the Group) includes IAG's full statutory accounts, along with the Directors' and remuneration reports for the financial year 2017. This year's corporate governance report is available in the About Us area of our website (www.iag.com.au).

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

All figures are in Australian dollars unless otherwise stated.

### 2017 ANNUAL REVIEW AND SUSTAINABILITY REPORT

This report should be read in conjunction with the 2017 annual review and sustainability report, which provides a summary of IAG's operating performance, including the Chairman's, CEO's and CFO's reviews.

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

If you would like to have a copy of the annual report or annual review mailed to you, contact IAG's Share Registry using the contact details on page 95.

### BEHIND OUR COVERS

The covers for this year's annual report and annual review tell the story of DipStik, a flood monitoring system being trialled by NRMA Insurance and the NSW SES. When a storm occurs, warning messages are sent to the local council and NSW SES so they can take appropriate measures and advise the community of floodwater risk.

In keeping with our Safer theme for this year's reporting suite, the Australian Red Cross and NSW SES will have people available at our 2017 annual general meeting to advise shareholders about how to prepare for the summer storm season.

### 2017 ANNUAL GENERAL MEETING

IAG's 2017 annual general meeting will be held on Friday, 20 October 2017, at the Wesley Conference Centre, 220 Pitt Street, Sydney, commencing at 10.00am. Details of the meeting, including information about how to vote, will be contained in our notice of meeting, which will be mailed to shareholders, and available online at www.iag.com.au, from Tuesday, 5 September 2017.

# DIRECTORS' REPORT

The Directors present their report together with the financial report of Insurance Australia Group Limited and the consolidated financial report of Insurance Australia Group Limited and its subsidiaries for the financial year ended 30 June 2017 and the Auditor's Report.

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

## DIRECTORS OF INSURANCE AUSTRALIA GROUP LIMITED

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

### CHAIRMAN

**ELIZABETH B BRYAN AM**

**BA (Econ), MA (Econ), age 70 - Chairman and Independent Non-Executive Director**

INSURANCE INDUSTRY EXPERIENCE

Elizabeth Bryan was appointed a Director of IAG on 5 December 2014, and became Chairman on 31 March 2016. She is the Chairman of the Nomination Committee, and attends all Board committee meetings in an ex officio capacity. Elizabeth is also the Chairman of Insurance Manufacturers of Australia Pty Limited.

OTHER BUSINESS AND MARKET EXPERIENCE

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

She has over 30 years of experience in the financial services industry, government policy and administration, and on the boards of companies and statutory organisations.

In addition to her role as Chairman of IAG, Elizabeth is also currently Chairman of Virgin Australia Group.

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

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

### MANAGING DIRECTOR

**PETER G HARMER**

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

INSURANCE INDUSTRY EXPERIENCE

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

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

Before this, Peter was Chief Executive of the Commercial Insurance division and joined IAG as Chief Executive Officer, CGU Insurance.

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

He has over 36 years experience in the insurance industry, including senior roles in underwriting, reinsurance broking and commercial insurance broking as Managing Director of John C. Lloyd Reinsurance Brokers, Chairman and Chief Executive of Aon Re and Chairman of the London Market Reform Group.

Peter has completed the Harvard Advanced Management Program.

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

## OTHER DIRECTORS

### DUNCAN M BOYLE

**BA (Hons), FCII, FAICD, age 65 - Independent Non-Executive Director**

INSURANCE INDUSTRY EXPERIENCE

Duncan Boyle was appointed a Director of IAG on 23 December 2016. He is a member of IAG's Audit Committee, Risk Committee and Nomination Committee.

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

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

OTHER BUSINESS AND MARKET EXPERIENCE

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

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

- Stockland Group (2007-2015); and
- QBE Insurance Group (2006-2014).

### CATRIONA A DEANS (ALISON DEANS)

**BA, MBA, GAICD, age 49 - Independent Non-Executive Director**

INSURANCE INDUSTRY EXPERIENCE

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

OTHER BUSINESS AND MARKET EXPERIENCE

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

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

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

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

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

### HUGH A FLETCHER

**BSc/BCom, MCom (Hons), MBA, age 69 - Independent Non-Executive Director**

INSURANCE INDUSTRY EXPERIENCE

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

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

OTHER BUSINESS AND MARKET EXPERIENCE

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

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

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

- IAG Finance (New Zealand) Limited (a part of the Group), since 2008;
- Vector Limited, since 2007; and
- Rubicon Limited, since 2001.

**JONATHAN (JON) B NICHOLSON**
**BA, age 61 - Independent Non-Executive Director**
INSURANCE INDUSTRY EXPERIENCE
Jon Nicholson was appointed a Director of IAG on 1 September 2015. He is a member of IAG's People and Remuneration Committee, Risk Committee and Nomination Committee.

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

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

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

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

**HELEN M NUGENT AO**
**BA (Hons), PhD, MBA, HonDBus, age 68 - Independent Non-Executive Director**
INSURANCE INDUSTRY EXPERIENCE
Helen Nugent was appointed a Director of IAG on 23 December 2016. She is Chairman of IAG's People and Remuneration Committee and a member of the Audit Committee and Nomination Committee.

OTHER BUSINESS AND MARKET EXPERIENCE
Helen is Chairman of Australian Rail Track Corporation, Ausgrid and the National Disability Insurance Agency.

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

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

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

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

Directorships of other listed companies held in the past three years:
- Origin Energy Limited (2003-2017);
- Veda Group (2013-2016); and
- Macquarie Group (1999-2014).

**THOMAS (TOM) W POCKETT**
**CA, BCom, age 59 - Independent Non-Executive Director**
INSURANCE INDUSTRY EXPERIENCE
Tom Pockett was appointed a Director of IAG, effective 1 January 2015. He is Chairman of IAG's Audit Committee and a member of the Risk Committee and Nomination Committee.

OTHER BUSINESS AND MARKET EXPERIENCE
Tom is Chairman and Non-Executive Director of Stockland Group, Chairman and Non-Executive Director of Autosports Group Limited and a Director of Sunnyfield Independence Association and of O'Connell Street Associates. He previously spent over eleven years as Chief Financial Officer and over seven years as Finance Director with Woolworths Limited and retired from these roles in February 2014 and July 2014, respectively. Tom has also held senior finance roles at Commonwealth Bank, Lend Lease Corporation and Deloitte.

Directorships of other listed companies held in the past three years:
- Autosports Group Limited, since 2016;
- Stockland Group, since 2014; and
- Woolworths Limited (2006-2014).

**PHILIP J TWYMAN AM**
**BSc, MBA, FAICD, age 73 - Independent Non-Executive Director**
INSURANCE INDUSTRY EXPERIENCE
Philip Twyman was appointed a Director of IAG on 9 July 2008. He is Chairman of IAG's Risk Committee, and a member of the Audit Committee and Nomination Committee.

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

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

OTHER BUSINESS AND MARKET EXPERIENCE
Philip is also a director of Tokio Marine Management (Australasia) Pty Ltd.

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

## DIRECTORS WHO CEASED DURING THE FINANCIAL YEAR
Raymond Lim was a Director from 1 February 2013 to 20 February 2017.

## SECRETARY OF INSURANCE AUSTRALIA GROUP LIMITED
**CHRISTOPHER (CHRIS) J BERTUCH**
**BEc, LLB, LLM**
Chris Bertuch was appointed Group General Counsel and Company Secretary on 11 May 2011. Prior to joining IAG, he held the position of Group General Counsel and Company Secretary at CSR Limited. Chris joined CSR Limited as a corporate lawyer in 1993 and prior to that was a partner in the law firm Gadens Lawyers in Sydney. He brings to IAG more than 30 years of experience in corporate, commercial and trade practices law and dispute resolution. Chris has completed the Advanced Management Program at Harvard Business School.

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

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

(a) Elizabeth Bryan was Chairman of the People and Remuneration Committee until 21 February 2017 and a member of the Risk Committee until 7 February 2017. She attends People and Remuneration Committee, Audit Committee and Risk Committee meetings in an ex officio capacity.
(b) Duncan Boyle was appointed to the Board on 23 December 2016. He was appointed to the Audit Committee, Risk Committee and Nomination Committee on 7 February 2017.
(c) Alison Deans was appointed to the Audit Committee on 7 February 2017.
(d) Hugh Fletcher and Jonathan Nicholson were appointed to the People and Remuneration Committee on 7 February 2017 and were members of the Audit Committee until 7 February 2017.
(e) Raymond Lim was a member of the Board, People and Remuneration Committee and Nomination Committee until 20 February 2017.
(f) Helen Nugent was appointed to the Board on 23 December 2016. She was appointed to the People and Remuneration Committee, Audit Committee and Nomination Committee on 7 February 2017 and was appointed Chairman of the People and Remuneration Committee effective 21 February 2017.

## PRINCIPAL ACTIVITY

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

| DIVISION | OVERVIEW | PRODUCTS |
|---|---|---|
| Consumer Division (Australia)<br><br>52% of Group gross written premium (GWP) | Consumer insurance products are sold in Australia through branches, call centres, the internet and representatives, under the following brands:<br>▪ NRMA Insurance in NSW, ACT, Queensland and Tasmania;<br>▪ SGIO in Western Australia;<br>▪ SGIC in South Australia;<br>▪ RACV in Victoria, via a distribution agreement with RACV;<br>▪ Coles Insurance nationally, via a distribution agreement with Coles; and<br>▪ CGU through affinity and financial institution partnerships and broker and agent channels.<br><br>Consumer Division also includes travel insurance, life insurance and income protection products which are underwritten by third parties. | Short tail insurance<br>▪ Motor vehicle<br>▪ Home and contents<br>▪ Lifestyle and leisure, such as boat, veteran and classic car and caravan<br><br>Long tail insurance<br>▪ Compulsory Third Party (motor injury liability) |
| Business Division (Australia)<br><br>25% of Group GWP | Business insurance products are sold in Australia through a network of around 2,000 intermediaries, such as brokers, agents and financial institutions and directly through call centre and online channels. Business Division is a leading provider of business and farm insurance, and also provides workers' compensation services in every state and territory, except South Australia and Queensland.<br><br>Business Division operates across Australia under the following brands:<br>▪ CGU Insurance;<br>▪ Swann Insurance;<br>▪ WFI;<br>▪ NRMA Insurance;<br>▪ RACV;<br>▪ SGIO; and<br>▪ SGIC. | Short tail insurance<br>▪ Business packages<br>▪ Farm and crop<br>▪ Commercial property<br>▪ Construction and engineering<br>▪ Niche, such as consumer credit<br>▪ Commercial motor and fleet motor<br>▪ Marine<br><br>Long tail insurance<br>▪ Workers' compensation<br>▪ Professional indemnity<br>▪ Directors' and officers'<br>▪ Public and products liability |
| New Zealand<br><br>20% of Group GWP | The New Zealand business is the leading general insurance provider in the country in both the direct and broker/agent channels. Insurance products are provided directly to customers primarily under the State and AMI brands, and indirectly through insurance brokers and agents, under the NZI and Lumley Insurance brands. Personal products and simplified commercial products are also distributed through agents and under third party brands by corporate partners, which include large financial institutions. | Short tail insurance<br>▪ Motor vehicle<br>▪ Home and contents<br>▪ Commercial property, motor and fleet motor<br>▪ Construction and engineering<br>▪ Niche, such as pleasure craft, boat, caravan and travel<br>▪ Rural and horticultural<br>▪ Marine<br><br>Long tail insurance<br>▪ Personal liability<br>▪ Commercial liability |
| Asia<br><br>3% of Group GWP | The Group has interests in five general insurance businesses in Asia, comprising the direct and intermediated insurance business underwritten through subsidiaries in Thailand, Vietnam and Indonesia and the share of the operating result from the investment in associates in Malaysia and India. The businesses offer personal and commercial insurance products through local brands. | |
| Corporate and Other | Corporate and other comprises other activities, including corporate services, capital management activity, shareholders' funds investment activities and inward reinsurance from associates. | |

# OPERATING AND FINANCIAL REVIEW

## OPERATING RESULT FOR THE FINANCIAL YEAR

IAG produced a headline insurance margin of 14.9% in the current financial year, towards the upper end of the revised guidance of 13.5-15.5% provided on 28 June 2017. Underlying performance was softer than anticipated with an underlying margin of 11.9% (2016-14.0%) falling short of original expectations. The lower than expected underlying margin was primarily due to higher than expected claims inflation in short tail motor in Australia and New Zealand and elevated large loss experience in commercial classes, notably in Australia.

Gross Written Premium (GWP) growth of 3.9% (2016-negative 0.6%) was higher than that expected at the outset of the year, encompassing a rate response to the short tail motor claims issues being experienced and better than expected retention in Australian commercial lines.

Short tail personal lines in Australia and New Zealand continued to generate solid growth, predominantly reflecting higher rates. Overall volumes were relatively flat, with growth in motor offset by modest declines in home. Underlying short tail profitability was strong, but slightly lower than the corresponding prior year, as earned rate effects lagged claims inflation.

Long tail Compulsory Third Party (CTP) profitability improved, particularly in NSW, as lower claims frequency resulted from initial reform measures in late calendar year 2016.

Commercial lines' profitability in Australia was adversely affected by the incidence of large property losses. The modest rate increases implemented from the conclusion of calendar year 2015 have continued to gather pace. In New Zealand, there was a marked improvement in commercial rates and volumes, post the Kaikoura earthquake in November 2016.

Asia delivered a lower result, influenced by increased competitive pressures in the Thai and Malaysian motor markets, and increased claim costs in Thailand, including those from flood events. Regional proportional GWP was flat, with strong ongoing growth in India countering trends in Thailand and Malaysia.

A higher reported margin of 14.9% (2016-14.3%) included prior period reserve releases well in excess of original expectations, at 5.4% (2016-2.5%) of Net Earned Premium (NEP), reflecting the relative absence of inflation. This was partially offset by an increase in net natural peril claim costs of over $160 million, which overran the allowance by about $140 million.

Progress on IAG's optimisation program has been in line with expectations, with a range of cost-out initiatives building over the course of the current year. As foreshadowed, a small net negative of $12 million was borne within the current year insurance profit, as modest initial benefits were more than offset by related implementation costs. The creation of a single Australian division, with effect from July 2017, is the next step in simplifying IAG's operating model as part of this program.

### Net profit after tax

Net profit after tax of $929 million (2016-$625 million) was nearly 50% higher than the prior year. In addition to the effect of a higher insurance profit, this outcome included:

- a significantly higher contribution from investment income on shareholders' funds, incorporating stronger equity market returns; partially offset by
- a greater than $30 million deterioration in the contribution from fee based business, which included a provision for costs associated with withdrawal from the NSW workers' compensation scheme; and
- the result in the corresponding prior year included nearly $140 million (post-tax) of non-cash accelerated amortisation and impairment of capitalised software assets.

### Gross written premium

GWP grew by 3.9%. The increase was primarily driven by:

- an ongoing rate response to claim cost pressures in short tail motor;
- further improvement in Australian commercial rates, while maintained retention levels were better than originally anticipated;
- a post-Kaikoura earthquake improvement in commercial rates and volumes in New Zealand;
- lower GWP in Asia, reflecting intensified price competition in motor in Thailand; and
- an overall positive foreign exchange translation effect (approximately 0.5%).

In addition, the current year GWP outcome contained:

- an initial $73 million contribution from IAG's entry into the South Australian CTP market from 1 July 2016, within Consumer Division; and
- lower GWP of approximately $130 million owing to the divestment of the Swann Insurance motor dealership business in early August 2016, within Business Division.

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

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

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

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

Additional details of the adjustments are provided on page 7 of the 2016 Annual Report.

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

### Insurance margin

IAG's current year reported insurance profit of $1,258 million (2016-$1,178 million) was nearly 7% higher than the prior year. The reported insurance margin of 14.9% (2016-14.3%) included:

- significantly higher than originally expected prior period reserve releases of $457 million (2016-$207 million), equivalent to 5.4% of NEP (2016-2.5%) arising from Australian long tail classes;
- net natural peril claim costs of $822 million (2016-$659 million), which exceeded allowance by over $140 million and included significant losses from the Kaikoura earthquake, Northern Sydney hailstorm and Tropical Cyclone Debbie events; and
- a favourable credit spread impact of $20 million, compared to an adverse effect of $37 million in the prior year.

### Underlying margin

IAG's underlying margin was 11.9% (2016-14.0%). The lower underlying margin included:

- an adverse impact of approximately 70 basis points (bps) from an $80 million increase in natural perils allowance to $680 million;
- increased short tail motor claims inflation in both Australia and New Zealand, where the earned effect of related rate increases has yet to match higher claim costs;
- elevated large loss experience in commercial lines, particularly in Australia in the second half;
- a slight drag from the Satellite business (in Consumer), which delivered strong growth but operates at a lower level of profitability;
- a near $20 million reduction from Asia; and
- the absorption of a small net cost from the Group's optimisation program, of approximately $12 million.

The above were partially offset by a greater than $40 million reduction in non-quota share reinsurance expense in the current year and improvement in NSW CTP profitability as pressure from small claim frequency eased.

IAG defines its underlying margin as the management reported insurance margin adjusted for:

- net natural peril claim costs less the related allowance for the period;
- reserve releases in excess of 1% of NEP; and
- credit spread movements.

| | **2017** | | 2016 | |
|---|---|---|---|---|
| INSURANCE MARGIN | **$m** | **%** | $m | % |
| Reported insurance margin* | **1,258** | **14.9** | 1,178 | 14.3 |
| Net natural peril claim costs less allowance | **142** | **1.7** | 59 | 0.7 |
| Reserve releases in excess of 1% of NEP | **(372)** | **(4.4)** | (125) | (1.5) |
| Credit spread movements | **(20)** | **(0.3)** | 37 | 0.5 |
| Underlying insurance margin | **1,008** | **11.9** | 1,149 | 14.0 |

* Reported insurance margin is the insurance profit/(loss) as a percentage of NEP as disclosed in the Statement of Comprehensive Income. The prior year represents the management reported insurance margin which is the insurance profit as a percentage of NEP as disclosed in the Investor Report. Based on the statutory results, the equivalent statutory insurance margin for the prior year was 13.0%.

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

**Tax expense**

IAG reported a tax expense of $329 million (2016-$218 million), representing an effective tax rate of 24.7% (2016-23.7%). The main reason for this lower than normal rate is the application of the concessional zero tax rate (previously 10%) to a greater proportion of reinsurance recoveries on the February 2011 Canterbury earthquake event by IAG's captive vehicle in Singapore, following a review by that country's revenue authorities.

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

**Investment income on shareholders' funds**

Net investment income on shareholders' funds was a profit of $249 million, a substantial increase on the profit of $97 million in the prior year. This was driven by a stronger equity market performance, with the broader Australian index (S&P ASX200 Accumulation) delivering a return of 14.1% (2016-0.6%) and the MSCI World Total Return Index (AUD Hedged) 16.4% (2016-negative 2.8%).

At 30 June 2017, the weighting to growth assets (equities and alternatives) within shareholders' funds stood at approximately 47% (2016-48%).

## DIVISIONAL HIGHLIGHTS

On 19 July 2017, IAG announced the creation of a single Australian division, with immediate effect. The Australia Division simplifies IAG's operating model by bringing together the former Australian Consumer, Australian Business, Operations and Satellite Divisions. It centralises accountability for the customer, product, distribution and operations functions for IAG's Australian brands, which include NRMA Insurance, CGU, WFI, SGIO and SGIC.

The segment information provided in this report references the reportable segments that were in place during the 2017 reporting period.

### A. CONSUMER DIVISION

The Consumer Division accounted for 52% of Group GWP. This business produced a strong underlying margin of 13.9% and its GWP increased by 5.5%.

**I. Premiums**

Consumer Division's collective brands continued to generate a sound top line performance in a dynamic and competitive environment. GWP increased by 5.5% to $6,119 million in the current year (2016-$5,801 million), and included growth in both short tail home and motor lines, as well as long tail CTP. Short tail GWP growth of 4.7% was predominantly rate-driven, largely in response to higher than originally expected claims inflation in motor. This was supplemented by modest volume gain in motor, while home volumes contracted marginally, reflecting lower new business.

Within Satellite, Coles Insurance and IAL (via the intermediated channel in partnership with Steadfast) delivered stronger growth than Consumer Division as a whole, albeit off considerably smaller bases than those of the major brands. Tougher conditions were experienced by the SGIO and SGIC brands in Western Australia and South Australia respectively, where GWP was flat.

Long tail CTP GWP increased by over 10%, reflecting IAG's entry into the South Australian market from 1 July 2016 and rate increases in NSW in the early part of the year.

**II. Insurance profit**

Consumer Division reported an insurance profit of $941 million (2016-$805 million). This equates to a higher reported insurance margin of 21.8% (2016-19.8%), and included the net effect of:
- considerably higher prior period reserve releases from long tail classes;
- a similar net natural peril claim cost; and
- a favourable credit spread movement of over $30 million.

Consumer division's underlying performance was strong, with an underlying margin of 13.9%. This outcome was lower than the corresponding prior year (16.0%) and contained:
- pressure on profitability from higher claim costs, notably in short tail motor, moderated by solid premium rate increases across the year;
- a slight drag on reported and underlying margin from the stronger growth of the lower margin Satellite offering, comprising Coles Insurance, SGIO, SGIC and IAL (via the intermediated channel in partnership with Steadfast); and
- an improvement in NSW CTP profitability, following the regulatory cap on legal fees for low value claims, introduced from 1 November 2016.

### B. BUSINESS DIVISION

The Business Division represented 25% of Group GWP. In overall terms, GWP was flat despite a reduction of almost $130 million as a result of the divestment of the Swann Insurance car dealership business. Like-for-like GWP growth exceeded 4%, with business retention levels holding up well and increased rate momentum evident in most intermediated classes. A lower underlying margin of 6.9% (2016-9.7%) included an increased large loss experience. A slightly lower reported margin of 9.2% (2016-10.0%) included higher reserve releases.

### I. Premiums
Business Division recorded relatively flat GWP of $2,962 million (2016-$2,979 million). This outcome contained:
- the $130 million reduction in premium from the divestment of the Swann Insurance car dealership business, as outlined above;
- targeted rate increases in most classes, with increased momentum over the course of the year;
- the shedding of poorly performing business, notably in the areas of workers' compensation and commercial property;
- strong underwriting agency-derived growth;
- steady retention rates, which held up better than expected; and
- lower new business opportunities and volumes.

Business Division has continued to focus on underwriting discipline and increasing rates in specific business segments through targeted portfolio reviews. This process commenced over 18 months ago and has gathered momentum. Whilst rate increases vary by segment, portfolios such as business packages, property and commercial motor have seen up to double digit advances, without adverse impact on volumes. The key June renewal period, which represents approximately 20% of Business Division's annual GWP, saw average rate increases of around 5% across the intermediated business portfolio.

The direct market continued to perform well and represented 24% of the Business Division's GWP (2016-23%). Policy growth in the online digital channel was approximately 8% off a low base. Long tail classes represented around 28% of the division's GWP (2016-27%).

### II. Insurance profit
Business Division reported a lower insurance profit of $204 million, compared to the prior year ($230 million). This equates to a reported insurance margin of 9.2% (2016-10.0%), which includes the net effect of:
- increased large loss experience;
- a similar net natural peril claim cost;
- lower investment income following the reduction in technical reserves as a result of the asbestos reinsurance arrangement in the prior year; partially offset by
- higher prior period reserve releases; and
- a favourable credit spread movement of $23 million.

Business Division produced a weaker underlying margin of 6.9% (2016-9.7%). This was driven by an adverse large loss experience against financial year 2016 and prior years. The earn-through of lower GWP in prior periods was also a contributory factor.

### III. Fee based business
Net income from fee based operations was a loss of $28 million, compared to a profit of $4 million in the prior year. The principal source of fee income is Business Division's role as agent under both the NSW and Victorian workers' compensation schemes, which are underwritten by the respective State governments. In March 2017 CGU announced its intention to withdraw from the NSW scheme by 31 December 2017 after assessment of associated risks and returns. As part of the withdrawal, anticipated redundancy payments and fixed technology recharges of approximately $13 million have been provided for in the current financial year.

Fee based income in the current year included $5 million of prior period fee income in respect of the Victorian scheme. Excluding this, the underlying result in the current year was lower by $17 million compared to the corresponding prior year, which was driven by:
- the loss of the largest employer in the Victorian scheme following an unsuccessful tender submission and a reduction in CGU's service fee under a new five year contract;
- unfavourable changes to the NSW remuneration model in the final year of the current contract period; and
- lower than expected returns from performance and incentive fees in both States.

A secondary source of fee income is Business Division's interest in authorised representative brokers, which it has consolidated into one entity following the integration of Westcourt General Insurance Brokers with National Advisor Services.

## C. NEW ZEALAND
New Zealand represented 20% of Group GWP and produced a strong underlying performance, with an underlying margin of 14.8% (2016-16.9%).

### I. Premiums
New Zealand reported GWP of $2,339 million (2016-$2,182 million), representing growth of 7.2%. This included a favourable foreign exchange translation effect, with local currency GWP increasing by 4.3% to NZ$2,475 million. This outcome embraces:
- strong GWP growth in the Consumer Division, led by the private motor vehicle portfolio from a combination of higher volumes and rates; and
- improving GWP growth in the Business Division where positive signs of rate and volume growth emerged in commercial lines in the second half.

### II. Insurance profit
The New Zealand business produced an insurance profit of $125 million (2016-$135 million), translating to a reported insurance margin of 7.6% (2016-8.6%). The slightly lower outcome reflects the net effect of:
- substantially higher net natural peril claim costs, notably from the Kaikoura earthquake;
- higher than expected working claim costs, predominantly in the personal lines and commercial motor books as a result of higher average claim costs and frequency;
- challenging market conditions in the Business Division where the focus remains on the maintenance of pricing and underwriting discipline;

- a continued focus on disciplined expense management; and
- the absence of the NZ$150 million increase to risk margin for the February 2011 earthquake event, which was recognised in the prior year.

New Zealand generated a strong underlying margin of 14.8% (2016-16.9%). The current year margin was impacted by a deterioration in working and large claim costs, as well as the cumulative effect of competitive pricing pressure in commercial lines. Steps taken to address these trends include rate and excess increases, supply chain initiatives and internal claim process changes.

#### III. Canterbury Rebuild

The settlement of claims associated with the financial year 2011 Canterbury earthquake events continues to make sound progress. At 30 June 2017:

- nearly NZ$6.4 billion of claim settlements had been completed;
- over 97% of all claims by number had been fully settled;
- over 98% of commercial claims had been fully settled; and
- over 97% of residential claims had been settled, with the balance either in construction or negotiation for cash settlement.

During the current year IAG continued to receive new claims from the Earthquake Commission (EQC) as they tipped over the EQC cap of NZ$100,000 (plus GST), but at a diminishing rate. IAG's reserving position at the end of the current year allows for some further claims exceeding the EQC's cap.

In financial year 2016, IAG acquired NZ$600 million of adverse development cover in respect of the February 2011 earthquake, which effectively increased IAG's cover for this event to NZ$5 billion. IAG's reserved position remains below the attachment point of this cover.

### D. ASIA

Asia reported a decline in consolidated GWP of over 5%, as intensified price competition in Thailand was exaggerated by an adverse foreign exchange translation effect. Asia's overall earnings contribution decreased to $10 million (2016-$26 million), as both Thailand and Malaysia incurred the effect of increased competitive pressures and, in the case of Thailand, flood-related claim costs. The combined contribution from the developing markets of India, Vietnam and Indonesia improved, driven by the move into profit from India as better claim and expense outcomes were supplemented by higher investment income.

#### I. Divisional result

The division contributed a total profit of $10 million in the current year, including shares of associates and allocated costs, compared to a $26 million profit in the corresponding prior year. The lower result reflects the combination of:

- the move to a small loss in Thailand, driven by a higher claims ratio and increased competitive pressures in motor;
- a lower margin from Malaysia in the face of soft new car sales and increased competition in motor ahead of detariffication;
- an increased loss from Indonesia, as it explores the development of a digital model; offset by
- a move into profit by India on the back of better risk selection, coupled with improved expense management;
- a favourable net movement in mark-to-market valuations of investments in Malaysia and India; and
- lower regional support and development costs.

#### II. Controlled entities

GWP from the Group's controlled entities was $366 million, which was a decrease of over 5% on the corresponding prior financial year (2016-$386 million), within this:

- the Thai business (Safety Insurance) reported a decrease in GWP of 3.9% to $348 million from $362 million in the prior year, compared to a local currency GWP decline of 1.8% in the current year. This outcome was influenced by weaker than expected growth in new vehicle sales, intensified price competition in the motor segment and significantly lower commercial volumes following a planned reduction in exposure to selected segments;
- AAA Assurance in Vietnam recorded GWP equivalent to $15 million (2016-$17 million); and
- Parolamas in Indonesia recorded GWP equivalent to $3 million (2016-$7 million).

The controlled entities reported an insurance loss of $7 million for the current year (2016-$21 million profit) excluding allocated costs. Within this:

- the Thai business reported an insurance loss of $2 million, compared to a profit of $23 million in the corresponding prior year. The significantly weaker outcome was driven by a deterioration in the loss ratio, which was characterised by a higher number of large losses in the engineering and fire classes, significantly lower prior period reserve releases; a regulatory-led increase in compulsory motor claim limits, with no commensurate premium increase; and increased natural peril-related net claim costs of $6 million, associated with flood incidents and a prolonged wet season;
- AAA Assurance contributed an insurance loss of $1 million (2016-$1 million loss). The result included an increase in the loss ratio, which was in line with expectations following the expiration of the earnings contribution from the run-off loan protection portfolio; and
- Parolamas in Indonesia contributed an insurance loss of $4 million (2016-$1 million loss).

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

The Group's share of associates was a profit of $42 million (2016-$36 million), excluding allocated costs and before amortisation. This result includes AmGeneral Holdings Berhad (AmGeneral) in Malaysia and SBI General Insurance Company Limited (SBI General) in India. AmGeneral accounts for the majority of the Group's share of net profit from associates.

- IAG's share of AmGeneral's profit for the current year decreased to $28 million (2016-$40 million). The decrease was primarily due to reduced net earned premium on the back of a reduction in average premiums for motor insurance; an increased loss ratio of 64.6% (2016-60.7%), largely driven by higher repair costs from motor franchise partnerships, changes to motor business mix and the adverse impact of the ringgit's depreciation on replacement car parts; increased expenses relating to marketing and sales campaigns; and higher administration expenses, particularly those associated with motor detariffication and GST implementation.

- IAG's share of SBI General's profit for the current year was $14 million compared to a $4 million loss in 2016. This move into profit comprised an improved loss ratio arising from motor portfolio remediation; a favourable monsoon season in the current year, reducing seasonal losses; an improved expense ratio resulting from tightened cost control; and higher investment income bolstered by business growth and favourable mark-to-market movements in technical reserves income.

**E. CORPORATE AND OTHER**

A pre-tax profit of $83 million was reported, which compares to a loss of $282 million in the corresponding prior year. The movement is mainly comprised of increased net investment income on shareholders' funds of $152 million in the current year and the non-recurrence of the $198 million non-cash accelerated amortisation and impairment charge on capitalised software assets incurred in the prior year.

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

## REVIEW OF FINANCIAL CONDITION

**A. FINANCIAL POSITION**

The total assets of the Group as at 30 June 2017 were $29,597 million compared to $30,030 million as at 30 June 2016. Movements within the overall decrease of $433 million include:

- a decrease in investments and cash of $649 million from the funds outflow associated with payment of the 2016 final dividend and 2017 interim dividend, the off-market ordinary share buy-back of 64 million shares, redemption of GBP and NZD subordinated debt and buy-back of convertible preference shares, partially offset by the issuance of capital notes and sound operating earnings for the year;
- a decrease in trade and other receivables of $168 million, predominantly driven by a $416 million decrease in reinsurance recoveries on paid claims as recoveries on claims associated with the Canterbury earthquakes were settled, partially offset by an increase of $182 million in investment related receivables, relating to the outstanding settlement of fixed interest holdings at year end; and
- an increase in reinsurance and other recoveries on outstanding claims of $569 million, predominantly due to recoveries relating to the Kaikoura earthquake and Tropical Cyclone Debbie, partially offset by the continued settlement of the 2011 Canterbury earthquake and other prior period natural peril events.

The total liabilities of the Group as at 30 June 2017 were $22,805 million compared to $23,245 million at 30 June 2016. The decrease in liabilities of $440 million is mainly attributable to the net effect of:

- a decrease in the outstanding claims liability of $370 million primarily due to prior year reserve releases from Australian long tail classes, higher discount rates impacting claim reserves and settlements on prior year events, partially offset by the Kaikoura earthquake and Tropical Cyclone Debbie claim reserves;
- a decrease in interest bearing liabilities of $338 million following the redemption of NZD and GBP subordinated debt and buy-back of convertible preference shares, partially offset by issuance of capital notes;
- an increase in unearned premium liability of $111 million consistent with growth in GWP; and
- an increase in trade and other payables of $88 million driven by an increase in payables relating to unsettled investment trades at year end, offset by lower reinsurance premiums payable.

IAG shareholders' equity (excluding non-controlling interests) decreased from $6,563 million at 30 June 2016 to $6,562 million at 30 June 2017, mainly attributable to:

- payment of the 2016 final and 2017 interim dividends and the dividend component of the off-market share buy-back, totalling $746 million;
- reduction in share capital following the off-market share buy-back totalling $193 million; and
- a sound earnings performance in the current year resulting in a net profit attributable to shareholders of $929 million.

**B. CASH FROM OPERATIONS**

The net cash inflows from operating activities for the year ended 30 June 2017 were $636 million compared to net cash outflows of $1,946 million for the prior year. The movement is mainly attributable to the net effect of:

- a $483 million increase in premiums received consistent with growth in GWP;
- an increase in reinsurance and other recoveries received of $959 million predominantly due to higher recoveries under the Berkshire Hathaway (BH) quota share and continued collection of recoveries pertaining to the 2010 and 2011 Canterbury earthquakes;
- a $452 million decrease in claims costs paid, mainly attributable to the period on period reduction in payments made in respect of natural peril events; and
- a $700 million decrease in outwards reinsurance premium expense paid, primarily driven by the purchase of the run-off portfolio protection placement in the prior financial year and lower catastrophe reinsurance premiums, stemming from the favourable renewals.

**C. INVESTMENTS**

The Group's investments totalled $12.1 billion as at 30 June 2017, excluding investments held in joint ventures and associates, with over 67% represented by the technical reserves portfolio. The decrease in total investments since 30 June 2016 ($12.9 billion) reflects the combined effect of:

- further reduction in technical reserves, mirroring the progressive effect of the 20% BH quota share in lowering related insurance liabilities and the significant reserve releases recognised in the current year; and
- the net reduction in shareholders' funds due to dividend payments ($623 million) and completion of the off-market share buyback ($316 million) in the first half of the current financial year.

As at 30 June 2017, the Group's overall investment allocation remains conservatively positioned and the credit quality of the investment book remains strong, with 73% (2016-77%) of the fixed interest and cash portfolio rated in the 'AA' category or higher.

Technical reserves as at 30 June 2017 accounted for $8.1 billion (2016-$8.7 billion) of the Group's investments, and were invested in fixed interest and cash.

The Group's allocation to growth assets was 47% of the $4 billion of shareholders' funds at 30 June 2017 (2016-48%). Included within the Group's allocation to growth assets are Australian and international equities and alternative investments.

**D. INTEREST BEARING LIABILITIES**

The Group's interest bearing liabilities stood at $1,624 million at 30 June 2017, compared to $1,962 million at 30 June 2016. The net decrease of $338 million is largely explained by:

- the buy-back of $377 million convertible preference shares;
- the redemption of NZ$187 million subordinated bonds ($179 million as of the redemption date);
- the redemption of £100 million subordinated term notes ($171 million as of the redemption date); partially offset by
- the issue of $404 million capital notes, qualifying as Additional Tier 1 Capital for regulatory purposes.

**E. CAPITAL MIX**

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

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

At 30 June 2017, the Group's capital mix was within the targeted range, with debt and hybrids representing 31.9% (2016-36.8%) of total tangible capitalisation.

**F. CAPITAL MANAGEMENT**

The Group remains strongly capitalised under APRA's Prudential Standards, with regulatory capital of $4,526 million at 30 June 2017 (2016-$4,619 million). The Group has set the following related targeted benchmarks:

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

At 30 June 2017, the Group had a PCA multiple of 1.70 (2016-1.72) and a CET1 multiple of 1.09 (2016-1.06).

Further capital management details are set out in Note 3.1 Risk and capital management within the Financial Statements.

## STRATEGY AND RISK MANAGEMENT

**A. STRATEGY**

- At IAG, our purpose is to make your world a safer place: IAG's purpose means that whether you are a customer, partner, employee, shareholder or part of the communities IAG serves across Australia, New Zealand or Asia, IAG exists to 'make your world a safer place'. IAG believes its purpose will enable it to become a more sustainable business over the long term, and deliver stronger and more consistent returns for its shareholders.
- IAG's opportunity is to embrace innovation: The way we live our lives is changing at a rapid pace driven by new technologies and shifting demographic trends. This means our customers are faced with new challenges and opportunities every day. IAG is determined to lead, helping our customers navigate through this journey and using innovation to make their lives safer and better.
- Our promise is to deliver world class customer experiences: All the elements of our strategy are driven by our customers' needs. As well as delivering world class customer experiences, we will make IAG as successful as possible so that we can reinvest in our leadership position.

**Financial targets**

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

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

**Strategic themes**

IAG is focused on optimising its core business and building the necessary platforms for future growth. IAG has identified two key strategic themes to deliver this strategy:

**I. Leading:**

- IAG is determined to lead the change that its customers need and demand. This has the company's customers at its core and IAG will embrace innovation and new technology to make each individual interaction a world class experience. This will be driven by:
  - deepening customer intimacy through digitally-enabled customer experiences, providing needs-based customer propositions and creating ecosystems of relevant adjacent services alongside insurance to help make customers' lives safer and fulfil IAG's purpose.
  - partnering selectively to complement and strengthen our capabilities, incorporating third party offerings in our ecosystems and investing in new ventures and incubation.

**II. Fuelling:**

- IAG will fuel the business so that it can deliver on these opportunities. This involves tackling necessary changes to the way IAG operates – simplifying processes and systems, and optimising resources, to be more efficient. This will be driven by:
  - optimising our core through simplification and scalability and becoming an agile organisation so that we can deliver inspiring customer experiences with less cost and complexity.

- modularising our operating and capital platforms so that the business can derive maximum value from each component of the value chain, including offering elements on a fee-for-service basis where they strengthen our competitive advantage and partnering for capability in areas that are not a competitive advantage.

**B. BUSINESS RISK AND RISK MANAGEMENT**

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

Roles and responsibilities of the Board and its standing committees, the Audit Committee, Risk Committee, People and Remuneration Committee and Nomination Committee, are set out in the Corporate Governance section of the IAG website.

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

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

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

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

**C. ECONOMIC, ENVIRONMENTAL AND SOCIAL SUSTAINABILITY RISK**

As a general insurer that operates in Australia, New Zealand and throughout Asia, IAG is exposed to economic, environmental and social sustainability risks and opportunities. The IAG Board has overarching responsibility for these areas, which are managed under shared value and sustainability. Performance and risk management is formally reported to the Board annually, with ad-hoc updates as required.

The Consumer Advisory Board and Ethics Committee provide external stakeholder input into the understanding of economic, environmental and social sustainability risk. The Shared Value Advisory Council is an internal governance body that acts as a forum to identify environmental and social risks, determine the materiality of risks and make decisions on how the Company responds through our approach to shared value, sustainability and broader community activity. Established in 2014, the Shared Value Advisory Council fulfils the role of a sustainability committee for IAG. It meets at least quarterly, is chaired by the Group Executive Office of the CEO, and is comprised of Senior Leaders from across the business, including the Group Executive for People, Performance and Reputation and the Chief Customer Officer.

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

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

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

Detail of IAG's material issues, how IAG manages related risks and opportunities and details of other shared value and sustainability activities can be found in the 2017 Annual Review & Sustainability Report, which is available at www.iag.com.au/shared-value/our-performance. IAG's management of Economic, Environmental and Social Sustainability Risk is outlined in detail in Principle 7.4 of the Corporate Governance Statement, which is available at www.iag.com.au/about-us/corporate-governance.

## CORPORATE GOVERNANCE

IAG is committed to attaining the highest level of corporate governance to ensure the future sustainability of the organisation and to create long term value for its shareholders.

IAG's Corporate Governance Statement has been approved by the Board. Throughout the financial year ended 30 June 2017, IAG has complied with the Australian Securities Exchange Corporate Governance Council Principles and Recommendations (3rd edition) and is compliant as at 23 August 2017. Further details on IAG's corporate governance practices and the Corporate Governance Statement are available at www.iag.com.au/about-us/corporate-governance.

## OUTLOOK

IAG expects to report an improved underlying operating performance in financial year 2018. GWP growth is expected to be in the low single digit range. The Group's reported margin guidance for the year ended 30 June 2018 is a range of 12.5-14.5%. Underlying assumptions behind the reported margin guidance are:

- net losses from natural perils in line with an allowance of $680 million (2017-$680 million);
- prior period reserve releases of at least 2% of NEP;
- no material movement in foreign exchange rates or investment markets; and
- a relatively neutral impact from optimisation program initiatives, as benefits are matched by related costs.

## DIVIDENDS

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

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

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

| CASH EARNINGS | **2017 $m** | 2016 $m |
|---|---|---|
| Net profit after tax | **929** | 625 |
| Acquired intangible amortisation and impairment (post-tax) | **59** | 57 |
| | **988** | 682 |
| **Non-recurring items:** | | |
| Corporate expenses | **8** | 221 |
| Tax effect on corporate expenses | **(6)** | (36) |
| Cash earnings* | **990** | 867 |
| Interim dividend | **307** | 316 |
| Final dividend | **474** | 316 |
| Dividend payable | **781** | 632 |
| Cash payout ratio* | **78.9%** | 72.9% |

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

IAG's full year dividend payout policy is to pay dividends equivalent to approximately 60-80% (30 June 2016-60-80%) of reported full year cash earnings.

The Board has determined to pay a fully franked final dividend of 20.0 cents per ordinary share (cps) (2016-13.0 cps), bringing the full year dividend to 33.0 cps (2016-26.0 cps). The final dividend is payable on 9 October 2017 to shareholders registered as at 5pm on 7 September 2017. The Company's Dividend Reinvestment Plan (DRP) will operate for the final dividend by acquiring shares on market with no discount applied. The DRP Issue Price will be based on a volume weighted average share price as defined in the DRP terms. The last date for receipt of an election notice for participation in the Company's DRP is 8 September 2017. Information about IAG's DRP is available at www.iag.com.au/shareholder centre/dividends/reinvestment.

## SIGNIFICANT CHANGES IN STATE OF AFFAIRS

During the financial year the following changes became effective:

- On 10 October 2016, IAG completed its ordinary share off-market buy-back, with IAG acquiring 64 million shares (representing 2.6% of IAG's issued share capital) for a consideration of $316 million (including transaction costs). The buy-back price per share was $4.91, which comprised a capital component of $2.99 and a fully franked dividend of $1.92.
- On 15 December 2016, IAG redeemed NZ$187 million of subordinated bonds ($179 million as of the redemption date).
- On 21 December 2016, IAG redeemed £100 million of subordinated term notes ($171 million as of the redemption date).
- On 22 December 2016, IAG bought back $224 million of convertible preference shares (CPS) and the proceeds received by holders were reinvested in capital notes (refer below).
- On 22 December 2016, IAG issued $404 million of capital notes including the above mentioned reinvestment. The notes qualify as Additional Tier 1 Capital under APRA's Prudential Framework for General Insurance.
- On 1 May 2017, IAG bought back the remaining CPS for a consideration of $156 million. The buy-back price per CPS was $102.08 which comprised the issue price of $100.00 and an additional amount determined by the Directors of $2.08 which was equivalent to the dividend that was scheduled to be paid on 1 May 2017 and was fully franked.

## EVENTS SUBSEQUENT TO REPORTING DATE

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

- Effective 19 July 2017, IAG announced the creation of a single Australian division to be led by Mark Milliner as CEO Australia. The Australian division simplifies IAG's operating model by bringing together the former Australian Consumer, Australian Business, Operations and Satellite divisions. There has been no change to the reportable segments in the current financial year as financial information was prepared and reviewed by the chief operating decision maker based on the pre-existing segment structure for Australia.
- On 1 August 2017, IAG consolidated its nine Australian Insurance licences into two licences following Federal Court approval received in July 2017. The consolidation transferred the insurance assets and liabilities of seven entities into a related entity, Insurance Australia Limited, with no impact to the Group's consolidated financial performance or position. Following the transfer, IAG retains two authorised insurers in Australia being Insurance Australia Limited and Insurance Manufacturers of Australia Pty Limited. The transfer is part of IAG's focus on becoming a simpler, more efficient and agile business.
- On 23 August 2017, the Board determined to pay a final dividend of 20 cents per share, 100% franked. The dividend will be paid on 9 October 2017. The dividend reinvestment plan will operate by acquiring shares on market for participants with no discount applied.

## NON-AUDIT SERVICES

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

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

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

The level of fees for total non-audit services amounted to approximately $1,359 thousand (refer to Note 8.3 Remuneration of auditors for further details of costs incurred on individual non-audit assignments).

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

The lead auditor's independence declaration is set out on page 39 and forms part of the Directors' Report for the year ended 30 June 2017.

## INDEMNIFICATION AND INSURANCE OF DIRECTORS AND OFFICERS

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

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

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

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

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

# REMUNERATION REPORT
## EXECUTIVE SUMMARY

IAG's remuneration approach is designed to align the interests of shareholders and Executives as well as to encourage sustainable, superior performance.

**The alignment between the short term performance of the Group and the reward of Executives has been strengthened.**

In August 2016, the People and Remuneration Committee (PARC) and the Board reviewed IAG's short term performance goals for the Managing Director and Chief Executive Officer (Group CEO) and the Executive Team, and the way performance against these goals translates into Short Term Incentive (STI) outcomes. Previously, the STI of the Executive Team was determined with reference to individual balanced scorecards that were tied to the performance of the division each Executive managed. For the year ended 30 June 2017, the STI of the Group CEO and each member of the Executive Team has been measured against the Group Balanced Scorecard, which drives collective accountability for the performance of the Group under the concept of "One IAG". STI awards for the year ended 30 June 2017 have been calculated with reference to the Group Balanced Scorecard outcome, with the Board able to exercise discretion up or down from this outcome to reflect the Executive's contribution to the Group's performance. Other significant changes to the Group Balanced Scorecard include:

- highlighting the importance of the Group's financial performance in determining STI outcomes by increasing the weighting of financial measures in the Group Balanced Scorecard to comprise 60% of all goals;
- introducing a Net Promoter Score as the customer measure for the Group Balanced Scorecard. This reflects IAG's strategic focus on delivering world class customer experiences; and
- simplifying the Group Balanced Scorecard by reducing the number of measures.

**PARC considers that IAG's executive reward framework supports the creation of sustainable financial performance.**

To focus Executives on achieving sustainable, long term performance, Executives are provided with Long Term Incentive (LTI) awards in the form of performance rights. The LTI requires Executives to meet challenging long term financial performance targets based on cash Return on Equity and relative Total Shareholder Return. Vesting of the LTI only occurs if the Group exceeds its long term performance targets and delivers superior financial performance over a three year period for the cash Return on Equity hurdle, and four years in the case of the relative Total Shareholder Return hurdle.

As foreshadowed in the 2016 Remuneration Report, a review of the cash Return on Equity hurdle was completed during the 2017 financial year. The outcome of this review was that cash Return on Equity was confirmed for this year as an important strategic measure.

**The remuneration outcomes presented in the 2017 Remuneration Report demonstrate a strong link between value created for IAG's shareholders and reward for its Executives.**

To attract and retain Executive talent, IAG provides competitive fixed pay. IAG has taken a conservative approach to fixed pay increases, with increases awarded where Executives are below the market for equivalent roles, or where there has been an increase in responsibilities. For the year ended 30 June 2017 fixed pay was held constant for the majority of IAG's Executives, with only four out of the thirteen Executives receiving increases due to changes in role or to reflect market pay levels. For the remuneration review conducted in August 2017, two out of twelve Executives will receive a fixed pay increase.

In the 2017 financial year, IAG's business performance was sound. After allowing for divestments and new market entry, the business maintained a stable market position and generated a sound underlying performance despite industry-wide claim cost pressures. A strong capital position was maintained, while shareholder returns were improved through active capital management. Reflecting this performance, the Group Balanced Scorecard outcome was 67% of the maximum achievable. The Board determined to cap STI payments to Executives at the Group Balanced Scorecard outcome and in some cases exercised downward discretion. The average STI payment for the Group CEO and the Executive Team was 64% of the maximum achievable.

Based on multiple years of strong returns, the cash Return on Equity hurdle for the three year period up to 30 June 2016 vested in full. The Board actively considers the performance tests of the LTI to ensure that the outcome appropriately rewards management for the value created for shareholders and has due regard for risk and compliance. The Board determined that software impairments announced to the market on 19 August 2016 would be included in the calculation when determining the cash Return on Equity vesting outcome.

On 30 September 2016, the relative Total Shareholder Return hurdle of the LTI grant awarded in the year ended 30 June 2013 was tested for the second time. Following this retest, IAG's Total Shareholder Return was ranked at the 53rd percentile of its peer group, resulting in an overall vesting outcome of 56%. This result translated to an additional 2% vesting above the 54% that had already vested following the original test on 30 September 2015. This was the last LTI grant issued with a retesting provision, with the final retest for this grant to be performed on 30 September 2017.

**PARC maintains a strong governance focus to ensure remuneration outcomes support the long term financial soundness of the Group.**

The Board conducted a review of IAG's remuneration policy to ensure it reflects sound governance practices that reinforce the financial soundness of IAG and encourages behaviour that supports its risk management framework.

In addition, a more comprehensive review of IAG's remuneration structure is underway.

IAG considers it is important to align the interests of Non-Executive Directors and Executives with those of shareholders. To support this alignment, Non-Executive Directors and Executives are required to hold a significant number of IAG shares with a period allowed to acquire those shares. Non-Executive Directors who had served at least three years and Executives who had served at least four years as at 30 June 2017 were tested at this date and all met this requirement.

As part of the Board's role in providing sound governance for IAG's remuneration programs, the Board conducted an assessment to determine if any reduction of unvested or unexercised equity grants was required. The Board is satisfied that no adjustment was necessary.

For employees whose primary role is risk and financial control, including the Chief Risk Officer and the Chief Financial Officer, the Board maintains oversight of their remuneration to ensure the independence of their functions and its alignment with IAG's risk management framework.

| CONTENTS | | PAGE |
|---|---|---|


## A. KEY MANAGEMENT PERSONNEL COVERED IN THIS REPORT

This report sets out the remuneration details for IAG's key management personnel (KMP). For the year ended 30 June 2017, KMP included the Executives and Non-Executive Directors listed below. Although the Non-Executive Directors are listed below, they do not have management responsibility. Their remuneration is, therefore, dealt with separately.

| NAME | POSITION | TERM AS KMP[a] |
|---|---|---|
| **EXECUTIVES** | | |
| Peter Harmer | Managing Director and Chief Executive Officer | Full year |
| Julie Batch | Chief Customer Officer | Full year |
| Chris Bertuch | Group General Counsel and Company Secretary | Full year |
| Ben Bessell[b] | Chief Executive, Australian Business Division | Full year |
| Duncan Brain | Chief Executive, Asia | Full year |
| David Harrington | Group Executive, Office of the CEO | Full year |
| Nicholas Hawkins | Chief Financial Officer | Full year |
| Jacki Johnson | Group Executive, People, Performance and Reputation | Full year |
| Anthony Justice[b] | Chief Executive, Australian Consumer Division | Full year |
| Mark Milliner[b] | Chief Operating Officer | Full year |
| Craig Olsen | Chief Executive, New Zealand | Full year |
| Clayton Whipp | Chief Risk Officer | Full year |
| **EXECUTIVES WHO CEASED AS KEY MANAGEMENT PERSONNEL** | | |
| Claire Rawlins | Group Executive, Digital and Technology | Ceased 7 December 2016 |
| **NON-EXECUTIVE DIRECTORS** | | |
| Elizabeth Bryan | Chairman, Independent Non-Executive Director | Full year |
| Duncan Boyle | Independent Non-Executive Director | From 23 December 2016 |
| Alison Deans | Independent Non-Executive Director | Full year |
| Hugh Fletcher | Independent Non-Executive Director | Full year |
| Jonathan Nicholson | Independent Non-Executive Director | Full year |
| Helen Nugent | Independent Non-Executive Director | From 23 December 2016 |
| Tom Pockett | Independent Non-Executive Director | Full year |
| Philip Twyman | Independent Non-Executive Director | Full year |
| **NON-EXECUTIVE DIRECTORS WHO CEASED AS KEY MANAGEMENT PERSONNEL** | | |
| Raymond Lim | Independent Non-Executive Director | Ceased 20 February 2017 |

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

(b) Following the implementation of the new IAG Australian Operating Model, effective 19 July 2017, Mark Milliner commenced in the role of Chief Executive, Australia and Ben Bessell assumed the role of Executive General Manager, Business Distribution, while Anthony Justice will cease employment with IAG on 18 November 2017.

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

## B. EXECUTIVE REMUNERATION STRUCTURE

### I. Remuneration guiding principles

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

- align remuneration with the interests of IAG's shareholders;
- retain market competitiveness to attract and retain high quality people; and
- encourage constructive, collaborative behaviours as well as prudent risk-taking that support long term financial soundness.

### II. Summary of remuneration components

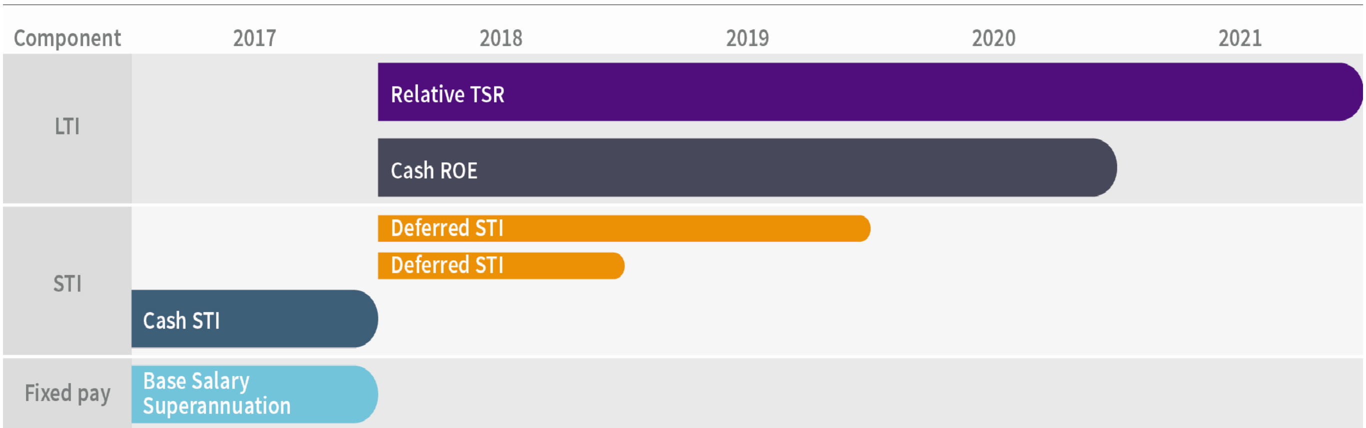
The Executive remuneration approach consists of the following components: fixed pay, cash STI, deferred STI and LTI. The table below describes the structure and purpose of each component.

TABLE 1 - REMUNERATION COMPONENTS

| COMPONENT | STRUCTURE | PURPOSE |
|---|---|---|
| Fixed pay | Fixed pay comprises base salary and superannuation. Fixed pay for an Executive is determined by reference to the experience and skills an individual brings to the role, the internal relativities within the Executive Team and market pay levels for similar external roles.<br><br>Further details relating to fixed pay are presented in table 2. | Fixed pay is provided to remunerate IAG employees for performing their ongoing work. |
| STI | STI is provided on an annual basis subject to the achievement of short term goals agreed by the Board, outlined in the Group Balanced Scorecard.<br><br>Two thirds of the total STI is delivered in cash in the remuneration review following the financial year end, the remaining one third is deferred over the subsequent two years based on continued service and is subject to downward adjustment if determined by the Board (termed malus).<br><br>Further details relating to the STI plan are presented in table 3. | STI plays a key role in aligning superior operational outcomes for shareholders with remuneration outcomes for management. A focus for the year ended 30 June 2017 has been on encouraging collaboration.<br><br>Deferral of incentives encourages ongoing employment of senior management and allows the Board to consider adjustment (malus). Share based remuneration reinforces the link between shareholder value creation and rewarding employees. |
| LTI | LTI rewards Executives for achieving challenging long term financial performance based on two hurdles: cash Return on Equity (ROE) over a three year period and relative Total Shareholder Return (TSR) over a four year period.<br><br>Further details relating to the LTI plan are presented in table 4. | LTI creates a direct link between Executive reward and the return experienced by IAG's shareholders, subject to the two hurdles below:<br><br>■ cash ROE provides evidence of the Group's return on shareholders' funds employed. The ROE hurdle utilises cash earnings, which is the measure used to determine the dividend paid to shareholders; and<br>■ relative TSR reflects the value created for shareholders through the movement of the share price and the value of dividends. |

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

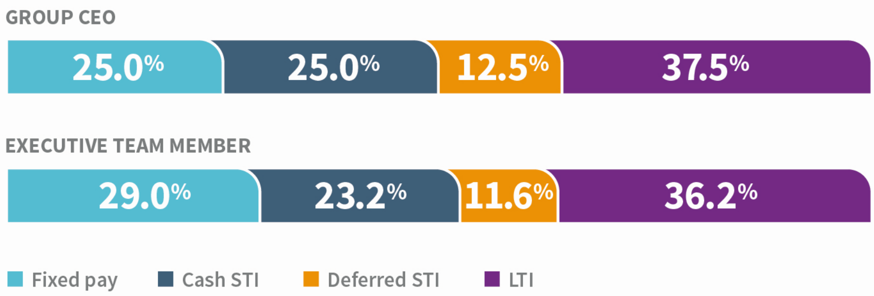
REMUNERATION COMPONENT TIMEFRAMES



### III. Remuneration mix

The mix of remuneration components in IAG's remuneration framework is outlined in the following graph. This represents the structure based on the maximum potential earnings for the Group CEO and Executive Team. The remuneration mix is current as at 30 June 2017.

REMUNERATION MIX BASED ON MAXIMUM INCENTIVE OPPORTUNITY




Each remuneration component is described in more detail below.

### IV. Fixed pay

TABLE 2 - FIXED PAY

| | |
|---|---|
| Overview | Fixed pay at IAG is set with reference to the median of the external market for comparable roles, with the flexibility to adjust based on the size and complexity of the role, and the skills and experience of the Executive. Fixed pay for Australian based Executives is compared to the market using peer groups, including financial services companies in the S&P/ASX 50 Index and companies that are of similar size to that of IAG. Relevant local market peer groups are referenced for overseas based Executives. |

### V. Short term incentive

TABLE 3 - STI AND DEFERRED STI

| | |
|---|---|
| Performance gateway | The IAG Spirit describes what is important to IAG: how we serve our customers, partners, shareholders, communities and each other. The IAG Spirit gateway is designed to ensure that IAG's employees demonstrate appropriate behaviours in the achievement of performance outcomes. Eligibility for an STI payment depends on demonstrating the IAG Spirit. The IAG Spirit is measured through demonstrating behaviour in line with IAG's core values of being 'Closer, Braver, Faster' as evaluated by the reporting manager and approved by the second level manager. |
| STI opportunity | The maximum value of STI that can be granted to the Group CEO is 150% of fixed pay. The maximum value of STI that can be granted to the Executive Team is 120% of fixed pay. |
| Performance measures and evaluation | STI is the at risk remuneration component designed to motivate and reward Executives for superior performance in the financial year. Performance is measured against the Group Balanced Scorecard using both financial and non-financial goals (the Group Balanced Scorecard is discussed in more detail in table 5a). The Group CEO's STI is recommended by PARC based on balanced scorecard performance and is approved by the Board.<br><br>The amount of STI paid to members of the Executive Team is recommended by the Group CEO to PARC based on the Group Balanced Scorecard outcome. These remuneration outcomes are subsequently recommended by PARC for approval by the Board.<br><br>For all individuals, the Board may apply discretion in determining the STI outcomes to ensure they appropriately reflect performance. |
| Instrument | An Executive's STI award is paid in cash and deferred in the form of Deferred Award Rights (DARs). The cash component is two thirds of the total STI and is paid in September following the end of the performance year. The deferred component is one third of the total STI and vests in equal amounts over the subsequent two years. |

| | |
|---|---|
| Key terms of the deferred STI | DARs are rights over IAG ordinary shares. DARs are granted at no cost to the Executives and no dividend is paid or payable for any unvested or vested and unexercised DARs.<br><br>For grants of DARs made after 1 July 2017, the number of DARs issued is calculated based on the volume weighted average share price of an IAG ordinary share over the 30 days up to and including 30 June before the grant date. Prior grants utilised the closing price at 30 June to determine the number of DARs granted.<br><br>Executives who participate in the STI plan become eligible to receive one IAG ordinary share per DAR by paying an exercise price of $1 per tranche of DARs exercised, subject to their continuing employment with the Group at the vesting date.<br><br>Executives may not enter into transactions or arrangements which operate to limit the economic risk of unvested entitlements to IAG Securities (termed hedging). |
| Forfeiture conditions | The Board retains the discretion to adjust downwards the unvested portion of any deferred STI awards, including to zero. DARs will be forfeited if the Executive resigns before the vesting date, except in special circumstances as outlined below.<br><br>When an Executive ceases employment in special circumstances, any unvested rights may be retained on cessation of employment up to the point they vest, subject to Board discretion. Special circumstances include: redundancy, retirement, death or total and permanent disability. Any rights retained under these circumstances will remain subject to the original vesting period unless the Board determine an alternative vesting date, which would only be done in exceptional circumstances. |

**VI. Long term incentive**

TABLE 4 - LTI

| | |
|---|---|
| Overview | LTI grants are determined annually by the Board. The grants provided are in the form of Executive Performance Rights (EPRs) that have performance hurdles which align to the Group's strategic financial targets. |
| LTI opportunity | The maximum value of LTI that can be granted to the Group CEO is 150% of fixed pay. The maximum value of LTI that can be granted to the Executive Team is 125% of fixed pay. |
| Instrument | If performance hurdles are achieved, rights granted after 1 July 2013 can be settled with IAG ordinary shares. The Board may, however, choose to exercise discretion to settle rights on vesting in cash in circumstances where it is restrictive to settle rights with shares, including in jurisdictions where legislative requirements prohibit share ownership in a foreign entity. Where rights are settled in cash, the value of the cash payment is determined based on the volume weighted average share price for the five trading days up to and including the date of vesting.<br><br>Rights granted prior to 1 July 2013 are only settled with IAG ordinary shares. |
| Key terms of the LTI | The number of EPRs issued is calculated based on the volume weighted average share price over the 30 days up to and including 30 June before the grant date. EPRs granted during the year will not vest and have no value to the Executive unless the performance hurdles are achieved. The cash ROE performance hurdle is measured over three years, while the relative TSR hurdle is measured over four years. No dividend is paid or payable for any unvested or vested and unexercised EPRs.<br><br>Executives may not enter into transactions or arrangements which operate to limit the economic risk of unvested entitlements to IAG Securities. |
| Forfeiture conditions | The Board retains the discretion to adjust downwards the unvested portion of any LTI awards, including to zero. Under the terms of the LTI, if an Executive resigns before the performance hurdles are tested, the unvested EPRs will generally lapse. In cases where the Executive acts fraudulently or dishonestly or is in breach of his or her obligations to the Group, the unvested EPRs will lapse.<br><br>When an Executive ceases employment in special circumstances, any unvested rights may be retained on cessation of employment up to the point they vest, subject to Board discretion. Special circumstances include: redundancy, retirement, death or total and permanent disability. Any rights retained under these circumstances will remain subject to the original performance conditions. |

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

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

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

IAG's strategic priorities are to drive customer and business benefits through the 'leading' and 'fuelling' themes. Leading puts customers at the centre of what IAG does using enhanced technology, offering innovative new products through IAG's core businesses, and identifying new ways to meet ever-changing customer needs. To fuel IAG's leading position, IAG is simplifying the operations of the business, optimising resources, leveraging the benefits of IAG's supply chain and continuing to build strong partnerships. In working to achieve these priorities, IAG is mindful of its social and environmental responsibilities.

The tables below provide a summary of key balanced scorecard objectives and outcomes for the Group for the year ended 30 June 2017. The objectives are agreed with the Board at the beginning of each financial year and are designed to focus Executives on delivering superior performance outcomes against the agreed priorities. To drive collective responsibility, in the year ended 30 June 2017 each Executive shared the same objectives.

TABLE 5a - BALANCED SCORECARD OBJECTIVES

| CATEGORY | OBJECTIVE | RATIONALE |
|---|---|---|
| Financial measures<br><br>(60% of scorecard) | Growth | IAG continues to expand its product and service offerings to its markets, which creates value for its shareholders, customers and partners. |
| | Controllable operating expense | IAG's continued focus on optimisation of its operating model and related cost-out initiatives improve the efficiency with which IAG deploys its resources. |
| | Profitability | Underlying insurance margin presents a view of normalised performance, which is an important measure of how IAG generates value for shareholders. |
| | Return on equity | The Group sets targets to achieve a return on its equity that requires outperformance through the cycle. This return reflects how effectively IAG uses its capital. |
| Non-financial measures<br><br>(40% of scorecard) | Customer advocacy | IAG's strategy is designed to put the customer at the centre of what IAG does. IAG considers this is essential to drive the Group's ability to grow profitably over the longer term. IAG is focused on designing compelling product offerings by developing a deeper understanding of customers' needs and the changing environment, then delivering world class customer experiences, including through digital channels. IAG uses Customer Net Promoter Score to measure the impact of these initiatives for our customers. |

| CATEGORY | OBJECTIVE | RATIONALE |
|---|---|---|
| | Partner advocacy | IAG fosters collaborative relationships with its partners to deliver mutual benefit. IAG works with distribution partners to develop joint strategies that develop their business capabilities, and aspires to provide best in class products and value added services. Ultimately, the Group aims to jointly deliver world leading experiences to mutual end customers. IAG uses Partner Net Promoter Score to measure the Group's effectiveness in delivering through partners. |
| | Agility | A constructive and agile culture enables IAG to provide great experiences for its people and customers. |
| | Risk and governance | Management of risk is integral to delivering IAG's strategy to meet short term objectives and achieve long term sustainability. IAG seeks to optimise the evaluation and pricing of risk. IAG has a clear articulation of its risk appetite, which the Board approves to uphold the expectations of IAG's stakeholders for how IAG employees conduct themselves. Due to the importance of risk management to IAG, it is included as an explicit measure on the scorecard. |

TABLE 5b - BALANCED SCORECARD RESULTS FOR THE YEAR ENDED 30 JUNE 2017

| OBJECTIVE AND WEIGHTING | MEASURE AND OUTCOME | COMMENT |
|---|---|---|
| Growth<br><br>10% | Exceeded<br><br>IAG achieved Gross Written Premium (GWP) growth of 3.9%, compared to -0.6% in the year ended 30 June 2016. | Over the year, IAG's GWP increased in its Australian Consumer Division and in New Zealand. This was slightly offset by a contraction in the Australian Business Division, reflecting the sale of renewal rights to the Swann motor dealer business and planned portfolio remediation activity, and in Asia due to competitive pressures and unfavourable foreign exchange effects. |
| Controllable operating expense<br><br>20% | Partially exceeded<br><br>Controllable expenses were lower than the prior year and slightly bettered the targeted reduction. | This result was due to favourable variances in the Australian Consumer Division, Australian Business Division and Chief Operating Office. This was partially offset by unfavourable foreign exchange effects. |
| Profitability<br><br>15% | Did not meet<br><br>IAG's underlying insurance margin was 11.9% compared to 14.0% in the year ended 30 June 2016. | IAG's Australian and New Zealand businesses were adversely impacted this year by claims cost pressures and an unusually high incidence of large losses. |
| Return on equity<br><br>15% | Exceeded<br><br>The Group's cash ROE was 15.2% for the year ended 30 June 2017, compared to 13.0% in the prior year. | The Group achieved its return on equity target for the year. Solid shareholders' fund investment returns in conjunction with prior year reserve releases contributed to this success. |
| Customer advocacy<br><br>15% | Partially exceeded<br><br>IAG sets a full year Customer Net Promoter Score (NPS) relative to its peers. IAG's NPS is +7 NPS above the competitive market average. This exceeded the target range of +4 to +6 NPS points above the competitor average. | The superior result in customer advocacy was driven by strong performances by NRMA, Coles Insurance, CGU and WFI; achieving absolute Strategic Customer NPS scores of +25, +28, +37 and +27 respectively.<br><br>IAG continues to invest in its customer advocacy programs to drive improvements across the customer journey. |

| OBJECTIVE AND WEIGHTING | MEASURE AND OUTCOME | COMMENT |
|---|---|---|
| Partner advocacy<br><br>5% | Met<br><br>IAG sets a full year Partner NPS target. IAG's partner brands (CGU and NZI) achieved an NPS of +24. | IAG's partner brands outperformed their competitive market means, with the 2017 financial year Strategic Partner NPS results of +31 and +15 for CGU and NZI respectively.<br><br>In the 2017 financial year, both CGU and NZI were voted Insurer of the Year in their respective industry surveys. |
| Agility<br><br>10% | Partially met<br><br>Measured based on performance against agility-related components of IAG's culture survey.<br><br>Whilst target results were achieved for some behaviours and outcomes achieved target results, IAG failed to achieve the target for all measures. | IAG continues to invest in building a constructive and agile culture. While the Group did not realise targets set for the current year, significant progress has been made in delivering a Diversity, Inclusion and Belonging strategy and framework; as well as strengthening community connection through Shared Value initiatives and the IAG Foundation.<br><br>Further focus is required to embed leadership capability, and continuing to create a positive and effective employee experience. The Leading@IAG program was launched during the 2017 financial year. This program will help connect structure with strategy, provide role clarity to employees, and set clear expectations for leadership behaviours with a particular focus on building trust and empowering people. |
| Risk and governance<br><br>10% | Partially met<br><br>IAG partially met new targets designed to deliver a step change in IAG's risk management practices. | IAG continues to strengthen its risk management framework, with ongoing focus on embedding improvements to risk management and governance models made during the 2017 financial year. Key achievements during the year included delivering further improvements in IAG's risk management practices in relation to Operational Risk, Regulatory Compliance, Enterprise Risk Profiling, Cyber resilience and an overall uplift in risk management maturity. |

**II. STI outcomes for the year ended 30 June 2017**

Set out below are the STI outcomes that will be made to Executives who were classed as a KMP for the full year ended 30 June 2017. STI outcomes are based on achievement against the Group Balanced Scorecard objectives described in table 5a. Reflecting the desire to encourage collaboration among Executives, all shared the same performance measures. The Board has the ability to adjust each Executive's STI up or down by 20%. The Board decided to cap Executive STI outcomes at the overall Group Balanced Scorecard result of 67%, with individual performance being reflected in the different outcomes for Executives. The average STI for all Executives was 64%.

TABLE 6 - ACTUAL STI OUTCOMES FOR THE YEAR ENDED 30 JUNE 2017

| | MAXIMUM STI OPPORTUNITY | ACTUAL STI OUTCOME | | CASH STI OUTCOME (2/3 OF OUTCOME) | DEFERRED STI OUTCOME (1/3 OF OUTCOME) |
|---|---|---|---|---|---|
| | (% of fixed pay) | (% of maximum)[(a)] | (% of fixed pay) | (% of fixed pay) | (% of fixed pay) |
| Peter Harmer | 150 % | 67 % | 101 % | 67 % | 34 % |
| Julie Batch | 120 % | 63 % | 76 % | 50 % | 26 % |
| Chris Bertuch | 120 % | 67 % | 80 % | 54 % | 26 % |
| Ben Bessell | 120 % | 55 % | 66 % | 44 % | 22 % |
| Duncan Brain | 120 % | 67 % | 80 % | 54 % | 26 % |
| David Harrington | 120 % | 67 % | 80 % | 54 % | 26 % |
| Nicholas Hawkins | 120 % | 67 % | 80 % | 54 % | 26 % |
| Jacki Johnson | 120 % | 60 % | 72 % | 48 % | 24 % |
| Anthony Justice | 120 % | 67 % | 80 % | 54 % | 26 % |
| Mark Milliner | 120 % | 67 % | 80 % | 54 % | 26 % |
| Craig Olsen | 120 % | 67 % | 80 % | 54 % | 26 % |
| Clayton Whipp | 120 % | 50 % | 60 % | 40 % | 20 % |

(a) The proportion of STI forfeited is derived by subtracting the actual percentage of maximum received from 100% and was 36% on average for the year ended 30 June 2017 (compared to 33% in 2016).

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

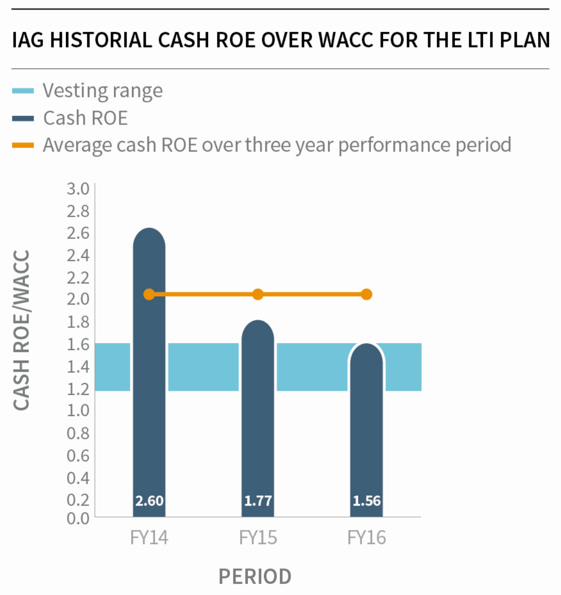
Details of LTI vested during the year are set out below:

**Cash ROE – 100% vesting**

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

For the performance period from 1 July 2013 to 30 June 2016, the average cash ROE was 2.00 times WACC. This award vested in full in the year ended 30 June 2017. The strong cash ROE performance has similarly been reflected in the dividend provided to shareholders.

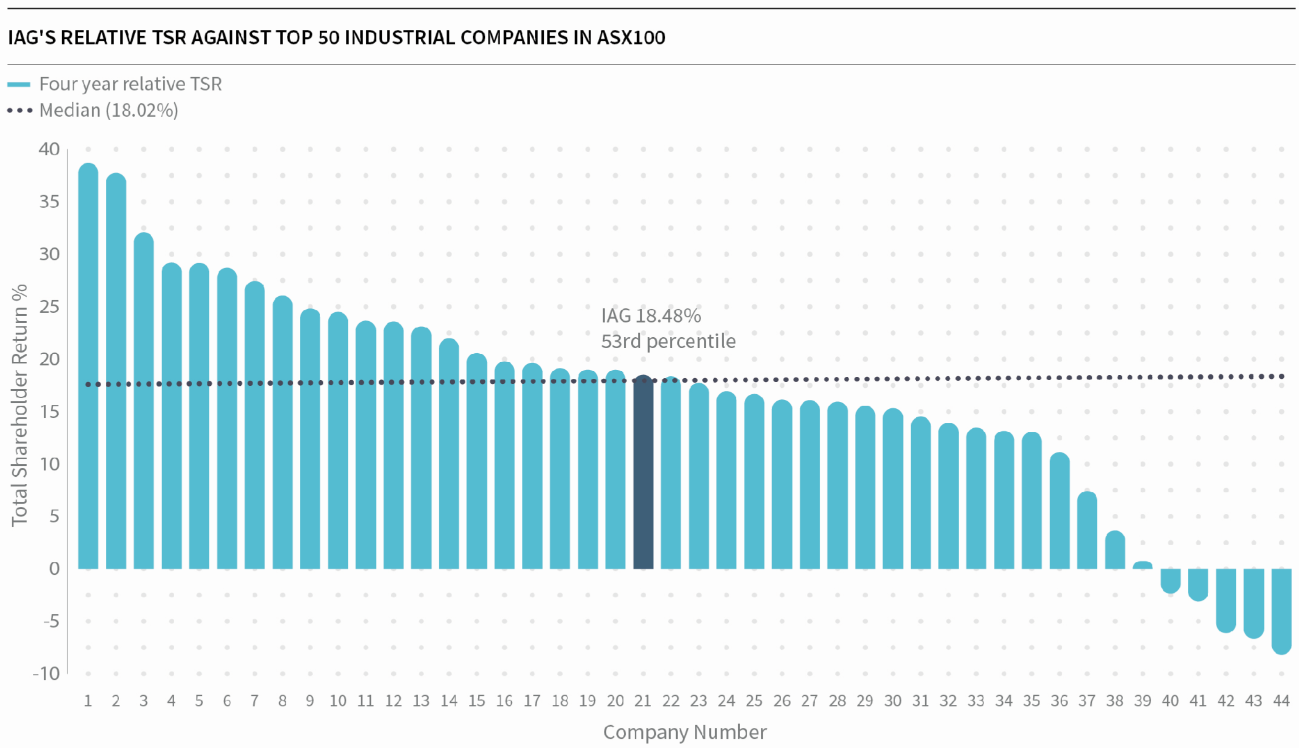
The Board considers any adjustments to cash earnings during the three year performance period to ensure reward outcomes appropriately reflect performance. The Board determined that impairments for software announced to the market on 19 August 2016 would be included when determining the cash ROE vesting outcome.




**Relative TSR - additional 2% vesting**

There was a legacy retest of the 2012/2013 LTI award on 30 September 2016. Following the retest, IAG's TSR was ranked at the 53rd percentile of its peer group, resulting in an overall vesting outcome of 56%. This result translated to an additional 2% vesting above the 54% that had already vested following the test on 30 September 2015. The final retest for this grant will occur on 30 September 2017. This will be the last retest performed for any LTI award.

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



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

TABLE 7 - HISTORICAL ANALYSIS OF SHAREHOLDER RETURN

| | YEAR ENDED 30 JUNE 2013 | YEAR ENDED 30 JUNE 2014 | YEAR ENDED 30 JUNE 2015 | YEAR ENDED 30 JUNE 2016 | **YEAR ENDED 30 JUNE 2017** |
|---|---|---|---|---|---|
| Closing share price ($) | 5.44 | 5.84 | 5.58 | 5.45 | **6.78** |
| Dividends per ordinary share (cents) | 36.00 | 39.00 | 29.00 | 36.00[a] | **33.00** |
| Basic earnings per share (cents) | 37.57 | 56.09 | 31.22 | 25.79 | **39.03** |
| Cash ROE (%) | 25.3 | 23.0 | 15.3 | 13.0 | **15.2** |
| Three year average cash ROE to WACC outcome for EPR Plan | 1.83 | 2.34 | 2.47 | 2.00[b] | **1.76**[b] |

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

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

### IV. Changes to Executive appointments and remuneration impacts

Increases to an Executive's fixed pay are generally only provided in situations where either their pay is below market levels, or where there has been a material change in the responsibilities of their role. During the 2017 financial year Duncan Brain and Anthony Justice received fixed pay increases to meet market pay levels. Julie Batch and Nicholas Hawkins received fixed pay increases to reflect a change in their role. The table below summarises how changes in roles within the Executive Team during the last two financial years have been reflected in Executive pay.

TABLE 8 - CHANGES IN ROLE AND IMPACTS ON REMUNERATION DURING 2017 AND 2016

| | YEAR | FIXED PAY $000 | CHANGE IN ROLE | PART YEAR KMP | SUMMARY OF CHANGES |
|---|---|---|---|---|---|
| **EXECUTIVES** | | | | | |
| Peter Harmer | **2017**<br>2016 | **1,700**<br>1,460 | <br>✓ | | Appointed as Group CEO on 16 November 2015, with an increase in remuneration at that time to reflect the increased responsibilities. |
| Julie Batch | **2017**<br>2016 | **662**<br>343 | ✓<br>✓ | <br>✓ | Appointed to a role classed as KMP on 8 December 2015. Julie Batch received a fixed pay increase in the year ended 30 June 2017 to reflect the expansion of her role to include responsibility for Digital Labs. |
| Chris Bertuch | **2017**<br>2016 | **700**<br>400 | <br>✓ | <br>✓ | Appointed as KMP on 8 December 2015. The remuneration for the year ended 30 June 2016 reflects the period served as KMP which was less than twelve months. |
| Ben Bessell | **2017**<br>2016 | **700**<br>686 | <br>✓ | | Appointed the Chief Executive, Australian Business Division (previously acting Chief Executive Commercial Insurance) on 8 December 2015. |
| Duncan Brain | **2017**<br>2016 | **943**<br>934 | | | Served as KMP for both financial years with no change in role. |
| David Harrington | **2017**<br>2016 | **600**<br>346 | <br>✓ | <br>✓ | Appointed as KMP on 8 December 2015. The remuneration for the year ended 30 June 2016 reflects the period served as KMP which was less than twelve months. |
| Nicholas Hawkins | **2017**<br>2016 | **1,173**<br>1,026 | <br>✓ | | Changed role 8 December 2015 to incorporate leadership of the NZ and Asian businesses. Subsequently received a fixed pay increase in the year ended 30 June 2017 to reflect the increased responsibility. |
| Jacki Johnson | **2017**<br>2016 | **1,091**<br>1,053 | <br>✓ | | Changed role on 1 January 2016 to become Group Executive, People Performance and Reputation. Previously, Jacki Johnson was the Chief Executive, New Zealand. There was no adjustment to remuneration. |
| Anthony Justice | **2017**<br>2016 | **690**<br>372 | <br>✓ | <br>✓ | Appointed as KMP on 8 December 2015. The remuneration for the year ended 30 June 2016 reflects the period served as KMP which was less than twelve months. |
| Mark Milliner | **2017**<br>2016 | **1,000**<br>181 | <br>✓ | <br>✓ | Commenced as the Chief Operating Officer at IAG on 27 April 2016. Remuneration was set upon appointment with no subsequent changes. |
| Craig Olsen | **2017**<br>2016 | **711**<br>330 | <br>✓ | <br>✓ | Appointed as KMP on 1 January 2016. The remuneration for the year ended 30 June 2016 reflects the period served as KMP which was less than twelve months. |
| Clayton Whipp | **2017**<br>2016 | **775**<br>784 | | | Served as KMP for both financial years with no change in role. |
| **EXECUTIVES WHO CEASED AS KEY MANAGEMENT PERSONNEL** | | | | | |
| Claire Rawlins | **2017**<br>2016 | **250**<br>341 | <br>✓ | ✓<br>✓ | Appointed to a role classed as KMP on 8 December 2015 and ceased as KMP on 7 December 2016. Claire Rawlins' remuneration for both years reflects the period served as a KMP. In each financial year the period served was less than twelve months. |

### V. Actual remuneration received by Executives

Table 9 below provides details of the remuneration received by Executives during the financial year. The table provides fixed pay and other benefits paid, and the value of prior years' deferred STI and LTI awards that vested during the financial year. For remuneration details provided in accordance with the Accounting Standards, refer to Appendix 1. Statutory remuneration disclosure requirements.

TABLE 9 - ACTUAL REMUNERATION RECEIVED IN 2017 AND 2016

| | FINANCIAL YEAR | FIXED PAY $000 (1) | OTHER BENEFITS AND LEAVE ACCRUALS $000 (2) | TERMINATION BENEFITS $000 (3) | CASH STI $000 (4) | DEFERRED STI VESTED $000 (5) | LTI VESTED $000 (6) | TOTAL ACTUAL REMUNERATION RECEIVED $000 |
|---|---|---|---|---|---|---|---|---|
| **EXECUTIVES** | | | | | | | | |
| Peter Harmer | **2017** | **1,700** | **17** | **-** | **1,139** | **288** | **697** | **3,841** |
| | 2016 | 1,460 | 70 | - | 905 | 311 | 1,428 | 4,174 |
| Julie Batch | **2017** | **662** | **(11)** | **-** | **353** | **110** | **111** | **1,225** |
| | 2016 | 343 | 34 | - | 153 | - | - | 530 |
| Chris Bertuch | **2017** | **700** | **(4)** | **-** | **375** | **129** | **127** | **1,327** |
| | 2016 | 400 | 33 | - | 138 | - | - | 571 |
| Ben Bessell | **2017** | **700** | **33** | **-** | **308** | **82** | **91** | **1,214** |
| | 2016 | 686 | 31 | - | 271 | 83 | 161 | 1,232 |
| Duncan Brain | **2017** | **943** | **341** | **-** | **508** | **217** | **620** | **2,629** |
| | 2016 | 934 | 261 | - | 532 | 154 | 273 | 2,154 |
| David Harrington | **2017** | **600** | **3** | **-** | **322** | **112** | **125** | **1,162** |
| | 2016 | 346 | 33 | - | 160 | - | - | 539 |
| Nicholas Hawkins | **2017** | **1,173** | **25** | **-** | **643** | **327** | **697** | **2,865** |
| | 2016 | 1,026 | (48) | - | 593 | 318 | 1,428 | 3,317 |
| Jacki Johnson(7) | **2017** | **1,091** | **(40)** | **-** | **524** | **240** | **644** | **2,459** |
| | 2016 | 1,053 | 92 | - | 585 | 252 | 1,286 | 3,268 |
| Anthony Justice | **2017** | **690** | **(6)** | **-** | **375** | **71** | **-** | **1,130** |
| | 2016 | 372 | (6) | - | 156 | - | - | 522 |
| Mark Milliner | **2017** | **1,000** | **22** | **-** | **536** | **-** | **-** | **1,558** |
| | 2016 | 181 | 20 | - | - | - | - | 201 |
| Craig Olsen(8) | **2017** | **711** | **33** | **-** | **381** | **74** | **79** | **1,278** |
| | 2016 | 330 | 36 | - | 124 | - | - | 490 |
| Clayton Whipp | **2017** | **775** | **11** | **-** | **310** | **153** | **127** | **1,376** |
| | 2016 | 784 | 64 | - | 415 | 117 | 243 | 1,623 |
| **EXECUTIVES WHO CEASED AS KEY MANAGEMENT PERSONNEL** | | | | | | | | |
| Claire Rawlins(9) | **2017** | **250** | **(15)** | **600** | **126** | **-** | **-** | **961** |
| | 2016 | 341 | 32 | - | 152 | - | - | 525 |

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

(2) Further details are provided in table 14 in Appendix 1. Statutory remuneration disclosure requirements.

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

(4) Cash STI earned within the year ended 30 June 2017 and to be paid in September 2017.

(5) The deferred STI vesting on 1 September 2016 was valued using the five day weighted average share price $5.60 (1 September 2015: $5.14).

(6) The LTI vested was valued using the five day weighted average share price at vesting date which was $5.90 for awards vested on 22 August 2016 and $5.46 for awards vested on 30 September 2016 (24 August 2015: $5.50 and 30 September 2015: $4.84).

(7) Remuneration for Jacki Johnson was determined in New Zealand dollars and reported in Australian dollars for the period between 1 July 2015 and 31 December 2015 using the average exchange rate for the year ended 30 June 2016, which was 1 NZD = 0.91957 AUD.

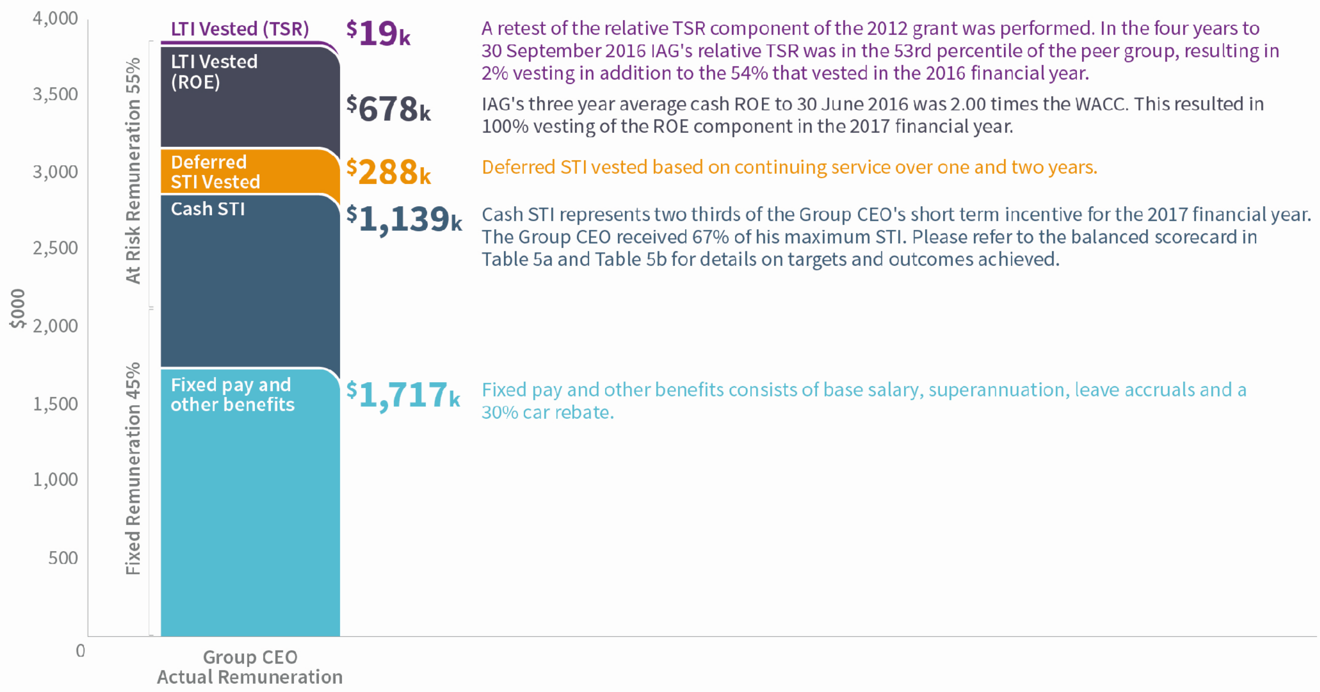
(8) Remuneration for Craig Olsen was determined in New Zealand dollars and reported in Australian dollars using the average exchange rate for the year ended 30 June 2017 which was 1 NZD = 0.94497 AUD.

(9) Claire Rawlins was a KMP for the period up to 7 December 2016. Claire Rawlins received a payment in lieu of notice of $600,000, equivalent to 12 months' fixed pay, under the terms of her contract upon her termination.

### VI. Group CEO remuneration

Below are further details on drivers of the actual remuneration received by the Group CEO that are outlined in table 9. His remuneration has been broken down into the components of the remuneration mix, with commentary on how performance has translated into remuneration outcomes.

GROUP CEO FY17 PERFORMANCE AND ACTUAL REMUNERATION OUTCOMES




### VII. Remuneration allocated to Executives

The following table provides details of the remuneration allocated to each Executive who was a KMP for the entire year ended 30 June 2017. This table comprises: fixed pay, STI awarded for performance during the financial year to be paid in September 2017, and LTI grants made during the financial year. The difference between this table and table 9 is that table 9 includes the value of equity awards (LTI and deferred STI) that vested during the year, whereas table 10 includes the face value of equity awards that were allocated during the year. For remuneration details provided in accordance with the Accounting Standards, refer to Appendix 1. Statutory remuneration disclosure requirements.

TABLE 10 - TOTAL PAY ALLOCATED FOR THE YEAR ENDED 30 JUNE 2017

| | | | | | EQUITY PAY | | |
|---|---|---|---|---|---|---|---|
| | Fixed pay $000 | Other benefits and leave accruals $000 | Cash STI $000 | Total cash remuneration $000 | STI deferred $000 | LTI allocation $000 | Total awarded remuneration $000 |
| | (1) | (2) | (3) | (4) | (5) | (6) | (7) |
| Peter Harmer | 1,700 | 17 | 1,139 | 2,856 | 569 | 2,550 | 5,975 |
| Julie Batch | 662 | (11) | 353 | 1,004 | 176 | 875 | 2,055 |
| Chris Bertuch | 700 | (4) | 375 | 1,071 | 188 | 875 | 2,134 |
| Ben Bessell | 700 | 33 | 308 | 1,041 | 154 | 875 | 2,070 |
| Duncan Brain | 943 | 341 | 508 | 1,792 | 254 | 1,184 | 3,230 |
| David Harrington | 600 | 3 | 322 | 925 | 161 | 750 | 1,836 |
| Nicholas Hawkins | 1,173 | 25 | 643 | 1,841 | 322 | 1,500 | 3,663 |
| Jacki Johnson | 1,091 | (40) | 524 | 1,575 | 262 | 1,364 | 3,201 |
| Anthony Justice | 690 | (6) | 375 | 1,059 | 188 | 875 | 2,122 |
| Mark Milliner(8) | 1,000 | 22 | 536 | 1,558 | 268 | 2,500 | 4,326 |
| Craig Olsen | 711 | 33 | 381 | 1,125 | 190 | 864 | 2,179 |
| Clayton Whipp | 775 | 11 | 310 | 1,096 | 155 | 969 | 2,220 |

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

(2) Further details are provided in table 14 in Appendix 1. Statutory remuneration disclosure requirements.

(3) Cash STI earned within the year ended 30 June 2017 to be paid in September 2017.

(4) The sum of columns 1 to 3.

(5) The deferred component of the STI earned within the year ended 30 June 2017, which is one third of the total STI and vests in equal amounts over the subsequent two years.

(6) The value of the LTI awards granted to Executives within the year ended 30 June 2017. The value ultimately received by Executives will be dependent on IAG meeting challenging performance targets over a three and four year period. Further details are provided in table 4.

(7) The sum of columns 4 to 6.

(8) In the year ended 30 June 2017, Mark Milliner received LTI awards for two financial years. Mr Milliner commenced his employment after the annual grant of LTI for the year ended 30 June 2016, therefore this grant was made in the year ended 30 June 2017.

### VIII. Fixed pay changes for the year ending 30 June 2018

In August 2017 the Board determined to maintain the current fixed pay levels for all Executives except the Chief Executive, New Zealand and the Group Executive, Office of the CEO. All other Executives including the Group CEO have not received fixed pay increases.

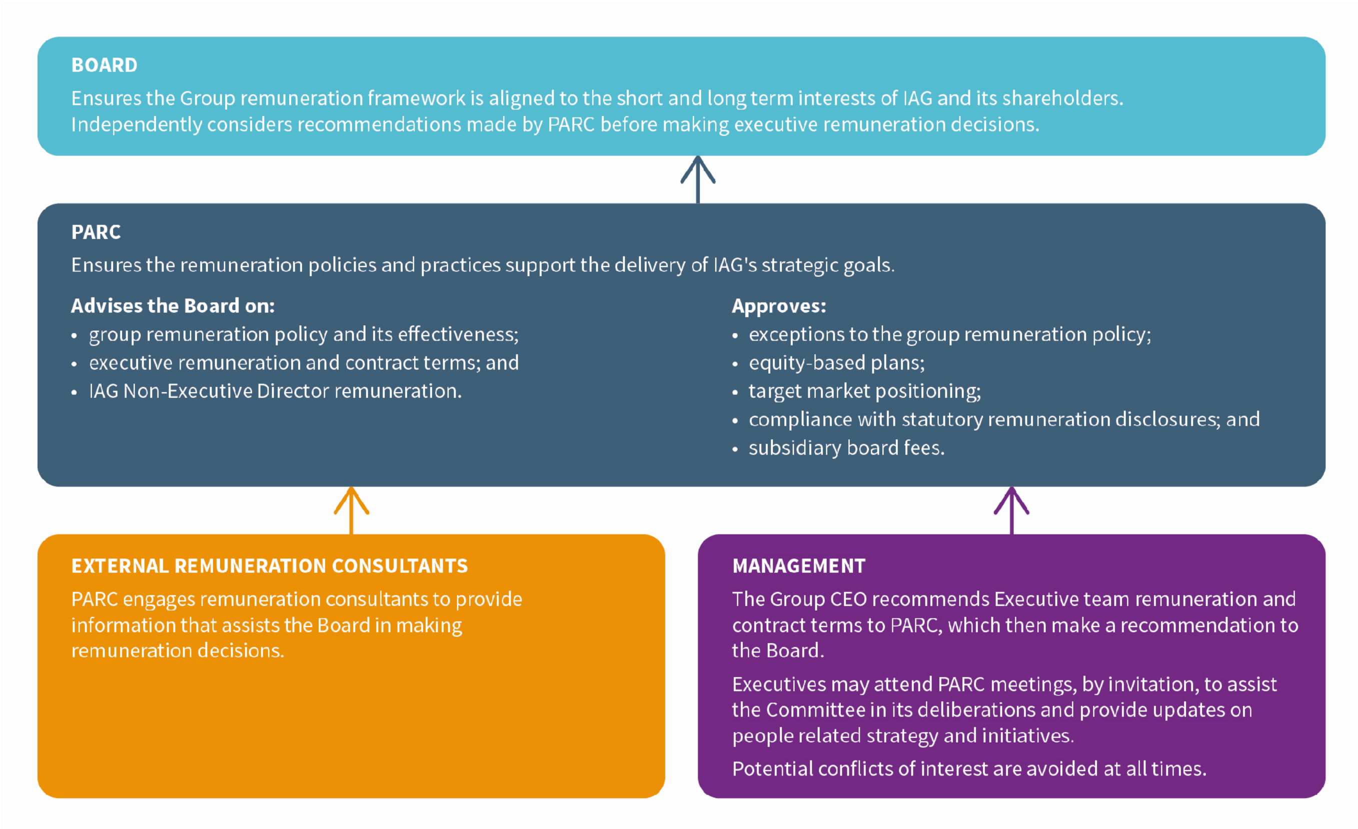
### IX. Upcoming LTI awards

The proposed LTI awards to Executives for the year ending 30 June 2018 will again be 150% of fixed pay for the Group CEO, and 125% of fixed pay for other Executives, other than for Anthony Justice who will leave IAG on 18 November 2017. The value of these LTI allocations will be calculated based on the Executive's fixed pay at the time of grant. The LTI allocation for the Group CEO will be subject to approval by shareholders at the AGM.

## D. EXECUTIVE REMUNERATION GOVERNANCE

### I. IAG's approach to remuneration governance

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




### II. Use of remuneration consultants

PARC engaged Pay Governance as external remuneration consultants to independently review IAG's approach to Executive remuneration. This review is ongoing as part of a comprehensive review of IAG's remuneration structure. No remuneration recommendations were provided in the year ended 30 June 2017. EY was engaged during the year to provide Non-Executive Director and KMP remuneration benchmarking. The remuneration data provided was used as an input to the remuneration decisions by the Board only. No remuneration recommendations, as defined by the Corporations Act 2001, were provided by EY. The Board considered the data provided, together with other factors, in setting Executives' remuneration.

### III. Adjustment policy

Each year, the Board assesses whether variable remuneration under the DARs and EPRs Plans needs to be adjusted to:

- protect the financial soundness of IAG or an operating segment;
- respond to significant unexpected or unintended consequences that were not foreseen by the Board; or
- respond to other circumstances where the Board determines that an adjustment is necessary, including circumstances where behaviour does not align with a desired risk culture, to ensure that an inappropriate reward outcome does not occur.

Annually PARC makes a recommendation to the Board on whether to adjust variable reward. This assessment requires the Group CEO, the Chief Risk Officer, the Chief Financial Officer, Group Executive People, Performance and Reputation, Chief Actuary and all Executives with profit and loss responsibility to attest as to whether an adjustment is necessary to the remuneration of any individual or group of employees. PARC and the Board separately consider these attestations in conducting their own assessment of whether an adjustment of variable remuneration is required. In the year ended 30 June 2017, this assessment did not reveal any requirement for the Board to adjust remuneration.

### IV. Mandatory shareholding requirement for Executives

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

All Executives appointed prior to 30 June 2013 met the mandatory shareholding requirement at 30 June 2017.

## E. NON-EXECUTIVE DIRECTOR REMUNERATION

### I. Remuneration policy

The principles that underpin IAG's approach to remuneration for Non-Executive Directors are that remuneration should:

- be sufficiently competitive to attract and retain a high calibre of Non-Executive Director; and
- create alignment between the interests of Non-Executive Directors and shareholders through the mandatory shareholding requirement.

### II. Mandatory shareholding requirement for Non-Executive Directors

Non-Executive Directors are required to hold IAG shares with a value equal to their annual Board fee. The Non-Executive Directors have three years from the date of their appointment to the Board to meet their required holding. Compliance with this requirement is assessed at the end of each financial year. For the test conducted at 30 June 2017, this requirement was assessed using the closing share price at 30 June and the Non-Executive Directors' Board fee from three years prior. Non-Executive Directors appointed prior to 30 June 2014 were required to meet the mandatory shareholding requirement at 30 June 2017 and all have done so.

From the year ending 30 June 2018, the mandatory shareholding requirement for Non-Executive Directors will be set based on either the value of shares at acquisition or the market value at the testing date, whichever is higher. Each Non-Executive Director will continue to be required to hold shares to the value of their annual Board fee, with a three year period allowed to reach that holding. This change is intended to allow Non-Executive Directors to build a long-term shareholding in IAG without being impacted by short term share price volatility.

### III. Board performance

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

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

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

### IV. Remuneration structure

Non-Executive Director remuneration is comprised of:

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

#### a. CHANGES TO NON-EXECUTIVE DIRECTOR REMUNERATION DURING THE YEAR ENDED 30 JUNE 2017

In August 2016, the Board approved a fee increase of 2.0% for Chairman and director fees paid for service on the IAG Limited Board, with all Committee fees remaining unchanged. The Board has determined that there will be no increase to Board fees for the year ended 30 June 2018. Fees for the Nomination Committee have been removed for the Chair and all directors. The aggregate limit of Board fees approved by shareholders at the Annual General Meeting in October 2013 remains unchanged at $3,500,000 per annum.

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

TABLE 11 - BOARD AND COMMITTEE FEES

| | | ROLE | |
|---|---|---|---|
| BOARD/COMMITTEE | YEAR | CHAIRMAN | DIRECTOR |
| Board | **2017** | **$577,166** | **$192,372** |
| | 2016 | $565,800 | $188,600 |
| Audit Committee | **2017** | **$50,000** | **$25,000** |
| | 2016 | $50,000 | $25,000 |
| Risk Committee | **2017** | **$50,000** | **$25,000** |
| | 2016 | $50,000 | $25,000 |
| People and Remuneration Committee | **2017** | **$50,000** | **$25,000** |
| | 2016 | $50,000 | $25,000 |
| Nominations Committee* | **2017** | **N/A** | **N/A** |
| | 2016 | N/A | $10,000 |

* In the year ended 30 June 2016 the Chair of the Nominations Committee is also the Chairman of the Group, therefore no Chair fee was applicable.

b. SUBSIDIARY BOARD AND COMMITTEE FEES

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

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

| DIRECTOR | SUBSIDIARY | CAPACITY | ANNUAL FEE |
|---|---|---|---|
| Elizabeth Bryan | Insurance Manufacturers of Australia Pty Limited | Chairman | $247,000 |
| Hugh Fletcher* | IAG New Zealand Limited | Chairman | $141,746 |

* This amount was paid to Hugh Fletcher in New Zealand dollars and reported in Australian dollars using the average exchange rate for the year ended 30 June 2017 which was 1 NZD = 0.94497 AUD.

TABLE 13 - NON-EXECUTIVE DIRECTOR AWARD RIGHTS (NAR) PLAN

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

## APPENDIX 1. STATUTORY REMUNERATION DISCLOSURE REQUIREMENTS

### I. Total remuneration for Executives

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

TABLE 14 - STATUTORY REMUNERATION DETAILS (EXECUTIVES)

| | SHORT TERM EMPLOYMENT BENEFITS | | | POST EMPLOY-MENT BENEFITS | OTHER LONG TERM EMPLOY-MENT BENEFITS | TERM-INATION BENEFITS | SUB-TOTAL | SHARE BASED PAYMENT | | TOTAL | AT-RISK REMUN-ERATION PAID |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | Base salary | Cash STI | Leave accruals and other benefits | Superan-nuation | Long service leave accruals | | | Value of deferred STI | Value of rights granted | | As a % of total reward |
| | $000 | $000 | $000 | $000 | $000 | $000 | $000 | $000 | $000 | $000 | % |
| | (1) | (2) | (3) | (4) | (5) | (6) | | (7) | (8) | | |
| **EXECUTIVES** | | | | | | | | | | | |
| Peter Harmer(9) | | | | | | | | | | | |
| **2017** | **1,665** | **1,139** | **(8)** | **35** | **25** | **-** | **2,856** | **307** | **1,139** | **4,302** | **60** |
| 2016 | 1,425 | 905 | 16 | 35 | 54 | - | 2,435 | 313 | 1,016 | 3,764 | 59 |
| Julie Batch(10) | | | | | | | | | | | |
| **2017** | **632** | **353** | **(21)** | **30** | **10** | **-** | **1,004** | **111** | **267** | **1,382** | **53** |
| 2016 | 326 | 153 | 16 | 17 | 18 | - | 530 | 110 | 171 | 811 | 54 |
| Chris Bertuch(10) | | | | | | | | | | | |
| **2017** | **665** | **375** | **(14)** | **35** | **10** | **-** | **1,071** | **118** | **302** | **1,491** | **53** |
| 2016 | 380 | 138 | 25 | 20 | 8 | - | 571 | 131 | 195 | 897 | 52 |
| Ben Bessell(11) | | | | | | | | | | | |
| **2017** | **670** | **308** | **23** | **30** | **10** | **-** | **1,041** | **96** | **285** | **1,422** | **48** |
| 2016 | 656 | 271 | (5) | 30 | 36 | - | 988 | 86 | 156 | 1,230 | 42 |
| Duncan Brain | | | | | | | | | | | |
| **2017** | **908** | **508** | **327** | **35** | **14** | **-** | **1,792** | **1,090** | **723** | **3,605** | **64** |
| 2016 | 899 | 532 | 245 | 35 | 16 | - | 1,727 | 815 | 719 | 3,261 | 63 |
| David Harrington(10) | | | | | | | | | | | |
| **2017** | **565** | **322** | **(6)** | **35** | **9** | **-** | **925** | **113** | **276** | **1,314** | **54** |
| 2016 | 326 | 160 | 29 | 20 | 4 | - | 539 | 96 | 163 | 798 | 53 |
| Nicholas Hawkins | | | | | | | | | | | |
| **2017** | **1,143** | **643** | **8** | **30** | **17** | **-** | **1,841** | **293** | **853** | **2,987** | **60** |
| 2016 | 996 | 593 | (35) | 30 | (13) | - | 1,571 | 341 | 977 | 2,889 | 66 |
| Jacki Johnson(12)(13) | | | | | | | | | | | |
| **2017** | **1,056** | **524** | **(56)** | **35** | **16** | **-** | **1,575** | **234** | **857** | **2,666** | **61** |
| 2016 | 1,025 | 585 | 78 | 28 | 14 | - | 1,730 | 258 | 957 | 2,945 | 61 |
| Anthony Justice(10) | | | | | | | | | | | |
| **2017** | **660** | **375** | **(16)** | **30** | **10** | **-** | **1,059** | **92** | **249** | **1,400** | **51** |
| 2016 | 355 | 156 | (17) | 17 | 11 | - | 522 | 64 | 76 | 662 | 45 |
| Mark Milliner(14) | | | | | | | | | | | |
| **2017** | **965** | **536** | **7** | **35** | **15** | **-** | **1,558** | **235** | **232** | **2,025** | **50** |
| 2016 | 176 | - | 19 | 5 | 1 | - | 201 | - | - | 201 | - |
| Craig Olsen(15)(16) | | | | | | | | | | | |
| **2017** | **711** | **381** | **33** | **-** | **-** | **-** | **1,125** | **87** | **261** | **1,473** | **49** |
| 2016 | 330 | 124 | 36 | - | - | - | 490 | 75 | 130 | 695 | 47 |
| Clayton Whipp | | | | | | | | | | | |
| **2017** | **740** | **310** | **-** | **35** | **11** | **-** | **1,096** | **187** | **437** | **1,720** | **54** |
| 2016 | 749 | 415 | 48 | 35 | 16 | - | 1,263 | 184 | 321 | 1,768 | 52 |
| **EXECUTIVES WHO CEASED AS KEY MANAGEMENT PERSONNEL** | | | | | | | | | | | |
| Claire Rawlins(10)(17) | | | | | | | | | | | |
| **2017** | **233** | **126** | **(13)** | **17** | **(2)** | **600** | **961** | **-** | **(15)** | **946** | **12** |
| 2016 | 321 | 152 | 30 | 20 | 2 | - | 525 | - | 21 | 546 | 32 |

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

(2) Cash STI represents the amount to be settled in cash in relation to the financial year from 1 July 2016 to 30 June 2017.

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

(4) Superannuation represents the employer's contributions.

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

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

(7) The deferred STI is granted as DARs and is valued using the Black-Scholes valuation model. An allocated portion of unvested DARs are included in the total remuneration disclosure above. The deferred STI for the year ended 30 June 2017 will be granted in the next financial year, so no value was included in the current financial year's total remuneration.

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

(9) Peter Harmer was appointed Group CEO on 16 November 2015. His remuneration increased upon his appointment.

(10) Executive Team members were appointed to KMP roles on 8 December 2015.

(11) Ben Bessell was appointed to the role of Chief Executive, Australian Business Division on 8 December 2015. Mr Bessell was previously acting Chief Executive, Commercial Insurance.

(12) Jacki Johnson was appointed to the role of Group Executive, People Performance and Reputation on 1 January 2016. Prior to this, Jacki Johnson was the CEO IAG New Zealand.

(13) Prior year remuneration for Jacki Johnson was determined in New Zealand dollars and reported in Australian dollars for the period between 1 July 2015 and 31 December 2015 using the average exchange rate for the year ended 30 June 2016, which was 1 NZD = 0.91957 AUD.

(14) Mark Milliner commenced with IAG on 27 April 2016.

(15) Craig Olsen commenced as a KMP on 1 January 2016 upon appointment to the role of CEO IAG New Zealand.

(16) Remuneration for Craig Olsen was determined in New Zealand dollars and reported in Australian dollars using the average exchange rate for the year ended 30 June 2017 which was 1 NZD = 0.94497 AUD.

(17) Claire Rawlins received a payment in lieu of notice of $600,000 upon her termination in accordance with her contractual terms.

## II. Total remuneration details for Non-Executive Directors

Details of total remuneration for Non-Executive Directors for the year ended 30 June 2017 are set out below:

TABLE 15 - STATUTORY REMUNERATION DETAILS (NON-EXECUTIVE DIRECTORS)

| | SHORT TERM EMPLOYMENT BENEFITS | | POST-EMPLOYMENT BENEFITS | | OTHER LONG TERM EMPLOYMENT BENEFITS | TERMINATION BENEFITS | SHARE BASED PAYMENT | TOTAL |
|---|---|---|---|---|---|---|---|---|
| | IAG Board fees received as cash | Other Boards and Committee fees | Superannuation | Retirement benefits | | | | |
| | $000 | $000 | $000 | $000 | $000 | $000 | $000 | $000 |
| **NON-EXECUTIVE DIRECTORS** | | | | | | | | |
| Elizabeth Bryan | | | | | | | | |
| **2017** | **474** | **226** | **19** | **-** | **-** | **-** | **97** | **816** |
| 2016 | 276 | 111 | 19 | - | - | - | - | 406 |
| Duncan Boyle(1) | | | | | | | | |
| **2017** | **92** | **18** | **10** | **-** | **-** | **-** | **-** | **120** |
| Alison Deans | | | | | | | | |
| **2017** | **149** | **32** | **20** | **-** | **-** | **-** | **24** | **225** |
| 2016 | 172 | 28 | 19 | - | - | - | - | 219 |
| Hugh Fletcher | | | | | | | | |
| **2017** | **176** | **187** | **21** | **-** | **-** | **-** | **-** | **384** |
| 2016 | 172 | 184 | 21 | - | - | - | - | 377 |
| Jonathan Nicholson | | | | | | | | |
| **2017** | **177** | **46** | **20** | **-** | **-** | **-** | **-** | **243** |
| 2016 | 145 | 36 | 14 | - | - | - | - | 195 |
| Helen Nugent(1) | | | | | | | | |
| **2017** | **69** | **26** | **11** | **-** | **-** | **-** | **24** | **130** |
| Tom Pockett | | | | | | | | |
| **2017** | **180** | **68** | **19** | **-** | **-** | **-** | **-** | **267** |
| 2016 | 177 | 78 | 19 | - | - | - | - | 274 |
| Philip Twyman | | | | | | | | |
| **2017** | **180** | **70** | **19** | **-** | **-** | **-** | **-** | **269** |
| 2016 | 177 | 82 | 19 | - | - | - | - | 278 |
| **NON-EXECUTIVE DIRECTORS WHO CEASED AS KEY MANAGEMENT PERSONNEL** | | | | | | | | |
| Raymond Lim | | | | | | | | |
| **2017** | **113** | **14** | **12** | **-** | **-** | **-** | **-** | **139** |
| 2016 | 172 | 23 | 19 | - | - | - | - | 214 |

(1) Non-Executive Directors appointed part way through the year ended 30 June 2017.

## APPENDIX 2. EXECUTIVE EMPLOYMENT AGREEMENTS

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

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

### I. Retrenchment

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

- the 12 month notice period, or payment in lieu of notice, as provided in their employment agreement; or
- the retrenchment benefits due under the company retrenchment policy.

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

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

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

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

Generally, this could occur where the Executive:

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

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

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

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

### IV. Executives who ceased employment in the financial year

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

Termination benefits for Claire Rawlins included a contractual payment in lieu of notice of $600,000. No other payments were provided to Ms Rawlins upon termination.

## APPENDIX 3. MOVEMENT IN EQUITY PLANS WITHIN THE FINANCIAL YEAR

Changes in each Executive's holding of DARs and EPRs and each Non-Executive Director's holdings of NARs during the financial year are set out below. The DARs granted during the year reflect the deferred portion of the STI outcome for the year ended 30 June 2016. The EPRs granted during the year ended 30 June 2017 were in relation to the LTI plan. The NARs granted during the year represents the total number of rights a Non-Executive Director has agreed to receive as part of the payment of their base Board fees.

TABLE 16 - MOVEMENT IN POTENTIAL VALUE OF DARS, EPRS AND NARS FOR THE YEAR ENDED 30 JUNE 2017

| | | RIGHTS ON ISSUE 1 JULY (1) | RIGHTS GRANTED DURING THE YEAR (2) | | RIGHTS EXERCISED DURING THE YEAR (3) | | RIGHTS LAPSED DURING THE YEAR | | RIGHTS ON ISSUE 30 JUNE | RIGHTS VESTED DURING THE YEAR | RIGHTS VESTED AND EXERCIS-ABLE 30 JUNE |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | | Number | Number | Value ($000) | Number | Value ($000) | Number | Value ($000) | Number | Number | Number |
| **EXECUTIVES** | | | | | | | | | | | |
| Peter Harmer | DAR | 72,650 | 83,100 | 409 | (51,400) | 303 | - | - | 104,350 | 51,400 | - |
| | EPR | 898,283 | 467,900 | 1,580 | (118,421) | 697 | - | - | 1,247,762 | 118,421 | - |
| Julie Batch | DAR | 29,450 | 24,900 | 122 | (19,600) | 115 | - | - | 34,750 | 19,600 | - |
| | EPR | 176,929 | 151,200 | 522 | (18,923) | 111 | - | - | 309,206 | 18,923 | - |
| Chris Bertuch | DAR | 33,950 | 22,500 | 111 | (22,950) | 135 | - | - | 33,500 | 22,950 | - |
| | EPR | 203,045 | 160,600 | 542 | (21,615) | 127 | - | - | 342,030 | 21,615 | - |
| Ben Bessell | DAR | 22,850 | 24,900 | 122 | (14,600) | 86 | - | - | 33,150 | 14,600 | - |
| | EPR | 199,700 | 160,600 | 542 | (36,116) | 213 | - | - | 324,184 | 15,547 | - |

| | | RIGHTS ON ISSUE 1 JULY (1) | RIGHTS GRANTED DURING THE YEAR (2) | | RIGHTS EXERCISED DURING THE YEAR (3) | | RIGHTS LAPSED DURING THE YEAR | | RIGHTS ON ISSUE 30 JUNE | RIGHTS VESTED DURING THE YEAR | RIGHTS VESTED AND EXERCIS-ABLE 30 JUNE |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | | Number | Number | Value ($000) | Number | Value ($000) | Number | Value ($000) | Number | Number | Number |
| Duncan | DAR | 418,350 | 48,900 | 240 | (38,800) | 229 | - | - | 428,450 | 38,800 | - |
| Brain | EPR | 629,379 | 217,300 | 734 | (104,550) | 616 | - | - | 742,129 | 105,223 | 673 |
| David | DAR | 29,450 | 26,000 | 128 | (20,050) | 118 | - | - | 35,400 | 20,050 | - |
| Harrington | EPR | 182,491 | 137,700 | 465 | (20,900) | 123 | - | - | 299,291 | 21,217 | 317 |
| Nicholas | DAR | 85,350 | 54,400 | 268 | (58,350) | 344 | - | - | 81,400 | 58,350 | - |
| Hawkins | EPR | 755,483 | 275,300 | 930 | (118,421) | 697 | - | - | 912,362 | 118,421 | - |
| Jacki | DAR | 61,700 | 53,700 | 264 | (42,950) | 253 | - | - | 72,450 | 42,950 | - |
| Johnson | EPR | 757,033 | 250,300 | 845 | (106,250) | 626 | - | - | 901,083 | 109,421 | 3,171 |
| Anthony | DAR | 20,600 | 25,300 | 124 | (12,750) | 75 | - | - | 33,150 | 12,750 | - |
| Justice | EPR | 122,800 | 160,600 | 542 | - | - | - | - | 283,400 | - | - |
| Mark | DAR | - | 150,000 | 714 | - | - | - | - | 150,000 | - | - |
| Milliner(4) | EPR | - | 453,500 | 1,715 | - | - | - | - | 453,500 | - | - |
| Craig Olsen | DAR | 20,350 | 23,200 | 114 | (13,150) | 77 | - | - | 30,400 | 13,150 | - |
| | EPR | 154,962 | 158,700 | 536 | (13,394) | 79 | - | - | 300,268 | 13,394 | - |
| Clayton | DAR | 65,150 | 38,200 | 188 | (27,250) | 160 | - | - | 76,100 | 27,250 | - |
| Whipp | EPR | 306,554 | 177,800 | 600 | (21,000) | 124 | - | - | 463,354 | 21,598 | 598 |
| **EXECUTIVES WHO CEASED AS KEY MANAGEMENT PERSONNEL** | | | | | | | | | | | |
| Claire | DAR | - | - | - | - | - | - | - | - | - | - |
| Rawlins(5) | EPR | 75,500 | - | - | - | - | (75,500) | 445 | - | - | - |
| **NON-EXECUTIVE DIRECTORS** | | | | | | | | | | | |
| Elizabeth Bryan | NAR | - | 18,877 | 97 | - | - | - | - | 18,877 | 18,877 | 18,877 |
| Alison Deans | NAR | - | 4,720 | 24 | - | - | - | - | 4,720 | 4,720 | 4,720 |
| Helen Nugent | NAR | - | 4,112 | 24 | - | - | - | - | 4,112 | 4,112 | 4,112 |

(1) Opening number of rights on issue represents the balance as at the date of appointment as KMP or 1 July 2016.

(2) The value of the DARs granted during the year is the fair value at grant date calculated using the Black-Scholes valuation model. The value of the annual DARs granted on 2 November 2016 was $4.92 except for the grant of 150,000 DARs provided to Mark Milliner which had a value of $4.76 per DAR. This amount is allocated to remuneration over years ending 30 June 2017 to 30 June 2019. The value of the cash ROE portion of the EPRs granted on 2 November 2016 and 24 March 2017 is the fair value at grant date, calculated using the Black-Scholes valuation model, which was $4.51 and $5.40 respectively. The cash ROE portion of the EPRs grants is first exercisable after the performance period concludes on 30 June 2019. The value of the relative TSR portion of the EPRs granted on 2 November 2016 and 24 March 2017 is the fair value at grant date, calculated using the Monte Carlo simulation, which was $2.24 and $3.00 respectively. The relative TSR portion of the EPRs is first exercisable on 30 September 2020. The amount is allocated to remuneration over the years ending 30 June 2017 to 30 June 2021. The value of the NARs granted during the year is the fair value at grant date calculated using the Black-Scholes valuation model. The value of the annual NARs granted on 15 November 2016 and 15 January 2017 was $5.15 and $5.95. This amount is allocated to remuneration over year ended 30 June 2017.

(3) Rights vested and exercised during the financial year. The value of the rights exercised is based on the weighted average share price for the year ended 30 June 2017, which was $5.89.

(4) Mark Milliner received 150,000 DARs in November 2016 as compensation for incentives foregone on leaving his previous employer. As EPRs relate to future performance, Mr Milliner received two allocations of EPRs in the year ended 30 June 2017: 224,100 EPRs in relation to his first year of employment, being the year ending 30 June 2016 under the terms of the 2015/2016 Series 6 EPR and 229,400 EPRs in relation to the year ending 30 June 2017 under the terms of the 2016/2017 Series 6 EPR.

(5) The rights on issue at 30 June for Claire Rawlins represents the balance as at 7 December 2016.

### I. LTI awards outstanding during the year ended 30 June 2017

Details of outstanding LTI awards made to Executives in the year ended 30 June 2017 are shown in the table below:

TABLE 17 - LTI AWARDS OUTSTANDING DURING THE YEAR ENDED 30 JUNE 2017

| AWARD | GRANT DATE | BASE DATE | FIRST TEST DATE | LAST TEST DATE | PERFORMANCE HURDLE ACHIEVEMENT | LAST EXERCISE DATE |
|---|---|---|---|---|---|---|
| 2016/2017 Series 6 - TSR[a] | 24/03/2017 | 30/09/2016 | 30/09/2020 | | N/A | 31/03/2024 |
| 2016/2017 Series 6 - ROE[a] | 24/03/2017 | 01/07/2016 | 30/06/2019 | | N/A | 31/03/2024 |
| 2016/2017 Series 6 - TSR[a] | 02/11/2016 | 30/09/2016 | 30/09/2020 | | N/A | 02/11/2023 |
| 2016/2017 Series 6 - ROE[a] | 02/11/2016 | 01/07/2016 | 30/06/2019 | | N/A | 02/11/2023 |
| 2015/2016 Series 6 - TSR[a] | 31/03/2016 | 30/09/2015 | 30/09/2019 | | N/A | 31/03/2023 |
| 2015/2016 Series 6 - ROE[a] | 31/03/2016 | 01/07/2015 | 30/06/2018 | | N/A | 31/03/2023 |
| 2015/2016 Series 6 - TSR[a] | 02/11/2015 | 30/09/2015 | 30/09/2019 | | N/A | 02/11/2022 |
| 2015/2016 Series 6 - ROE[a] | 02/11/2015 | 01/07/2015 | 30/06/2018 | | N/A | 02/11/2022 |
| 2014/2015 Series 6 - TSR[a] | 03/11/2014 | 30/09/2014 | 30/09/2018 | | N/A | 03/11/2021 |
| 2014/2015 Series 6 - ROE[a][b] | 03/11/2014 | 01/07/2014 | 30/06/2017 | | N/A | 03/11/2021 |
| 2013/2014 Series 6 - TSR[a] | 01/11/2013 | 30/09/2013 | 30/09/2017 | | N/A | 01/11/2020 |
| 2013/2014 Series 6 - ROE[a] | 01/11/2013 | 01/07/2013 | 30/06/2016 | | 100% | 01/11/2020 |
| 2012/2013 Series 5 - TSR | 26/10/2012 | 30/09/2012 | 30/09/2015 | 30/09/2017 | 56% | 26/10/2019 |
| 2012/2013 Series 5 - ROE | 26/10/2012 | 01/07/2012 | 30/06/2015 | | 100% | 26/10/2019 |

(a) Terms and conditions for EPR Plans from 2013/2014 to 2016/2017 are the same; therefore, they are all referred to as Series 6.

(b) The cash ROE portion of EPR Plan 2014/2015 has been tested and is expected to vest in full. Vesting details will be included in the Remuneration Report for the year ended 30 June 2018.

## APPENDIX 4. RELATED PARTY INTERESTS

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

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

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

TABLE 18 - MOVEMENT IN TOTAL NUMBER OF ORDINARY SHARES HELD

| | SHARES HELD AT 1 JULY | SHARES RECEIVED ON EXERCISE OF DAR | SHARES RECEIVED ON EXERCISE OF EPR | NET MOVEMENT OF SHARES DUE TO OTHER CHANGES[a] | TOTAL SHARES HELD AT 30 JUNE | SHARES HELD NOMINALLY AT 30 JUNE[b] |
|---|---|---|---|---|---|---|
| | Number | Number | Number | Number | Number | Number |
| **2017** | | | | | | |
| NON-EXECUTIVE DIRECTORS AND EXECUTIVES | | | | | | |
| Elizabeth Bryan | 32,725 | - | - | 1,509 | 34,234 | 34,234 |
| Duncan Boyle[c] | - | - | - | 32,679 | 32,679 | 32,679 |
| Alison Deans | 37,742 | - | - | - | 37,742 | 37,742 |
| Hugh Fletcher | 82,032 | - | - | 1,520 | 83,552 | 46,991 |
| Jonathan Nicholson | 11,468 | - | - | 23,121 | 34,589 | 24,162 |
| Helen Nugent[c] | 540 | - | - | - | 540 | 540 |
| Tom Pockett | 32,251 | - | - | 177 | 32,428 | - |
| Philip Twyman | 15,522 | - | - | - | 15,522 | 12,780 |
| Peter Harmer | 655,967 | 51,400 | 118,421 | - | 825,788 | 172,800 |
| Julie Batch | 182,907 | 19,600 | 18,923 | (122,500) | 98,930 | 277 |
| Chris Bertuch | 53,880 | 22,950 | 21,615 | 164 | 98,609 | 544 |
| Ben Bessell | 464 | 14,600 | 36,116 | (8,400) | 42,780 | 277 |
| Duncan Brain | 234,758 | 38,800 | 104,550 | (210,000) | 168,108 | - |
| David Harrington | 1,387 | 20,050 | 20,900 | 202 | 42,539 | 953 |
| Nicholas Hawkins | 220,000 | 58,350 | 118,421 | (176,771) | 220,000 | - |
| Jacki Johnson[d] | 592,760 | 42,950 | 106,250 | - | 741,960 | 592,760 |
| Anthony Justice | - | 12,750 | - | - | 12,750 | - |
| Mark Milliner | - | - | - | - | - | - |
| Craig Olsen | 123,403 | 13,150 | 13,394 | - | 149,947 | 14,800 |
| Clayton Whipp | 101,314 | 27,250 | 21,000 | (23,607) | 125,957 | 688 |

| | SHARES HELD AT 1 JULY | SHARES RECEIVED ON EXERCISE OF DAR | SHARES RECEIVED ON EXERCISE OF EPR | NET MOVEMENT OF SHARES DUE TO OTHER CHANGES[(a)] | TOTAL SHARES HELD AT 30 JUNE | SHARES HELD NOMINALLY AT 30 JUNE[(b)] |
|---|---|---|---|---|---|---|
| | Number | Number | Number | Number | Number | Number |
| **NON-EXECUTIVE DIRECTORS AND EXECUTIVES WHO CEASED AS KEY MANAGEMENT PERSONNEL[(e)]** | | | | | | |
| Raymond Lim | 35,000 | - | - | (35,000) | - | - |
| Claire Rawlins | - | - | - | - | - | - |

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

(b) Shares nominally held are included in the column headed total shares held at 30 June and include those held by the KMP's related parties, inclusive of domestic partner, dependants and entities controlled, jointly controlled or significantly influenced by the KMP.

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

(d) The opening balance for Jacki Johnson is 366,827 shares higher than the closing balance in the year ended 30 June 2016. This is a result of the overstatement of the number of shares disposed of in the year ended 30 June 2016 by this amount.

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

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

On 1 July 2016, Philip Twyman had an indirect holding of 5,109 convertible preference shares. On 22 December 2016 Mr Twyman's total holding of convertible preference shares were bought back by IAG. No other key management personnel had any interest directly or nominally in convertible preference shares during the financial year (2016-nil).

### III. Movements in total number of capital notes held

During the year ended 30 June 2017 Philip Twyman indirectly purchased 5,109 capital notes (2016-nil). No other key management personnel had any interest directly or nominally in capital notes during the financial year (2016-nil).

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

No key management personnel had any interest directly or nominally in reset exchangeable securities of IAG Finance (New Zealand) Limited at any time during the financial year (2016-nil).

### V. Relevant interest of each director and their related parties in listed securities of the IAG Group in accordance with the Corporations Act 2001

TABLE 19 - HOLDINGS OF SHARES, CAPITAL NOTES AND RESET EXCHANGEABLE SECURITIES

| | ORDINARY SHARES | | CAPITAL NOTES | | RESET EXCHANGEABLE SECURITIES | |
|---|---|---|---|---|---|---|
| | Held directly[(a)] | Held indirectly[(b)] | Held directly | Held indirectly | Held directly | Held indirectly |
| Elizabeth Bryan | - | 34,234 | - | - | - | - |
| Duncan Boyle | - | 32,679 | - | - | - | - |
| Alison Deans | - | 37,742 | - | - | - | - |
| Hugh Fletcher | 36,561 | 46,991 | - | - | - | - |
| Jonathan Nicholson | 10,427 | 24,162 | - | - | - | - |
| Helen Nugent | - | 540 | - | - | - | - |
| Tom Pockett | 32,428 | - | - | - | - | - |
| Philip Twyman | 2,742 | 12,780 | - | 5,109 | - | - |
| Peter Harmer | 652,988 | 172,800 | - | - | - | - |

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

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

## APPENDIX 5. KEY TERMS AND DEFINITIONS

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

| TERM | DEFINITION |
|---|---|
| Actual remuneration | The dollar value of remuneration actually received by the Executives in the financial year. This is the sum of fixed pay plus the cash STI earned in the reported financial year plus the value of DARs vested during the financial year plus the value of EPRs vested during the year. |
| At-risk remuneration | Remuneration that is dependent on a combination of the financial performance of the Group, the Executives' performance against individual measures (financial and non-financial) and continuing employment. At-risk remuneration typically includes STI (cash and deferred remuneration) and LTI. |
| Base salary | The cash component of fixed pay. |
| Cash return on equity (ROE) | Calculated as cash earnings divided by average total shareholders' equity during the financial year. Cash earnings is defined as net profit after tax attributable to IAG shareholders plus amortisation and impairment of acquired identifiable intangible assets and adjusted for unusual items after tax (non-recurring in nature). Cash ROE is used to calculate one half of the outcome in the LTI plan. |
| Cash STI | The two thirds portion of an Executive's STI outcome that is paid in the form of cash, following the end of year assessment and approval by the Board. |
| Deferred STI/Deferred Award Rights (DARs) | The one third portion of an Executive's STI that is deferred over a period of two years and awarded in the form of DARs. |
| Executive Team | The Executives who form part of the Group Leadership Team, comprising: Chief Executive, Australian Consumer Division; Chief Executive, Australian Business Division; Chief Executive, New Zealand; Chief Executive, Asia; Chief Financial Officer; Chief Operating Officer; Chief Risk Officer; Chief Customer Officer; Group Executive, Office of the CEO; Group General Counsel and Company Secretary; and Group Executive, People, Performance and Reputation. |
| Executives | The Group CEO and the Executive Team. |
| Fixed pay | Base salary plus superannuation. Individuals can determine the mix of base salary and superannuation they receive in line with legislative requirements. |
| Group Balanced Scorecard | The Group Balanced Scorecard sets out the objectives that have to be achieved to meet key strategic priorities of the organisation. The Group Balance Scorecard uses goals set against financial and non-financial objectives. Achievement against these objectives is measured and this informs the Board's determination of STI outcomes. |
| Group CEO | IAG's Managing Director and Chief Executive Officer. |
| IAG Spirit | The IAG Spirit 'Closer, Braver, Faster' is a set of statements that capture a shared view across IAG of how we work together, what we stand for and what makes us unique. |
| Key management personnel (KMP) | Persons having authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, including any Director (whether Executive or otherwise) of that entity. |
| Long term incentive (LTI)/Executive Performance Rights (EPRs) | A grant of rights in the form of EPRs that are exercisable for IAG ordinary shares or cash as determined by the Board. Vesting occurs between three and four years after the grant date if performance hurdles are achieved. |
| Malus | The Board has the ability to reduce the value of deferred remuneration before it has vested, including down to zero. |
| Non-Executive Director Award Right (NAR) | The NARs Plan provides directors with the opportunity to build their shareholding in IAG and is provided in the form of NARs. Participation in the plan is voluntary. |
| People and Remuneration Committee (PARC) | The Board committee which oversees IAG's remuneration practices. |
| Short term incentive (STI) | The part of annual at risk remuneration that is designed to motivate and reward for annual performance. STI results are determined by performance against a balanced scorecard, based on goals which reflect financial and non-financial measures. For Executives, one third of STI is deferred for a period of two years and two thirds is paid in cash in September following the end of the performance year. |
| Total shareholder return (TSR) | TSR combines share price movements and dividends paid to show total return to shareholders. IAG uses relative TSR performance against other companies in the peer group to calculate one half of the LTI outcome. |
| WACC | The weighted average cost of capital (WACC) is the rate that a company is expected to pay on average to all its security holders to finance its assets. |

## ROUNDING OF AMOUNTS

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

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

Signed at Sydney this 23rd day of August 2017 in accordance with a resolution of the Directors.

**Peter Harmer**
Director

# LEAD AUDITOR'S INDEPENDENCE DECLARATION

## UNDER SECTION 307C OF THE CORPORATIONS ACT 2001

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

I declare that, to the best of my knowledge and belief, in relation to the audit of Insurance Australia Group Limited for the financial year ended 30 June 2017 there have been:

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

KPMG

**KPMG**

**Andrew Yates**
Partner

Sydney
23 August 2017

# CONSOLIDATED FINANCIAL STATEMENTS

# CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

## FOR THE YEAR ENDED 30 JUNE 2017

| | NOTE | 2017 $m | 2016 $m |
|---|---|---|---|
| Gross earned premium | 2.1 | **11,692** | 11,411 |
| Outwards reinsurance premium expense | | **(3,227)** | (3,883) |
| Net earned premium (i) | | **8,465** | 7,528 |
| Claims expense | | **(8,638)** | (8,500) |
| Reinsurance and other recoveries revenue | 2.1 | **3,375** | 3,798 |
| Net claims expense (ii) | 2.2 | **(5,263)** | (4,702) |
| Commission expense | | **(1,065)** | (1,039) |
| Underwriting expense | | **(1,835)** | (1,822) |
| Reinsurance commission revenue | 2.1 | **715** | 745 |
| Net underwriting expense (iii) | | **(2,185)** | (2,116) |
| Underwriting profit (i) + (ii) + (iii) | | **1,017** | 710 |
| Investment income on assets backing insurance liabilities | 2.3 | **257** | 484 |
| Investment expenses on assets backing insurance liabilities | | **(16)** | (21) |
| Insurance profit before capitalised software accelerated amortisation and impairment | | **1,258** | 1,173 |
| Capitalised software accelerated amortisation and impairment expense | 5.1 | **-** | (198) |
| Insurance profit | | **1,258** | 975 |
| Investment income on shareholders' funds | 2.3 | **262** | 113 |
| Fee and other income | | **182** | 204 |
| Share of net profit of associates | | **19** | 17 |
| Finance costs | | **(93)** | (99) |
| Fee based, corporate and other expenses | | **(290)** | (285) |
| Net loss attributable to non-controlling interests in unitholders' funds | | **(4)** | (5) |
| Profit before income tax | | **1,334** | 920 |
| Income tax expense | 5.2 | **(329)** | (218) |
| Profit for the year | | **1,005** | 702 |
| **OTHER COMPREHENSIVE INCOME/(EXPENSE)** | | | |
| **Items that may be reclassified subsequently to profit or loss:** | | | |
| Net movement in foreign currency translation reserve, net of tax | | **(16)** | 65 |
| **Items that will not be reclassified to profit or loss:** | | | |
| Remeasurements of defined benefit plans, net of tax | | **25** | (32) |
| Other comprehensive income, net of tax | | **9** | 33 |
| Total comprehensive income for the year, net of tax | | **1,014** | 735 |
| **PROFIT FOR THE YEAR ATTRIBUTABLE TO** | | | |
| Shareholders of the Parent | | **929** | 625 |
| Non-controlling interests | | **76** | 77 |
| Profit for the year | | **1,005** | 702 |
| **TOTAL COMPREHENSIVE INCOME FOR THE YEAR ATTRIBUTABLE TO** | | | |
| Shareholders of the Parent | | **938** | 658 |
| Non-controlling interests | | **76** | 77 |
| Total comprehensive income for the year, net of tax | | **1,014** | 735 |

| | NOTE | 2017 cents | 2016 cents |
|---|---|---|---|
| **EARNINGS PER SHARE** | | | |
| Basic earnings per ordinary share | 4.3 | **39.03** | 25.79 |
| Diluted earnings per ordinary share | 4.3 | **37.72** | 25.34 |

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

# CONSOLIDATED BALANCE SHEET

## AS AT 30 JUNE 2017

| | NOTE | 2017 $m | 2016 $m |
|---|---|---|---|
| **ASSETS** | | | |
| Cash held for operational purposes | 8.1 | **424** | 263 |
| Investments | 2.3 | **12,136** | 12,946 |
| Trade and other receivables | 2.6 | **4,153** | 4,321 |
| Current tax assets | | **66** | 54 |
| Reinsurance and other recoveries on outstanding claims | 2.2 | **5,258** | 4,689 |
| Deferred insurance expenses | 2.5 | **2,770** | 2,778 |
| Deferred levies and charges | | **105** | 131 |
| Deferred tax assets | 5.2 | **545** | 603 |
| Property and equipment | | **182** | 204 |
| Other assets | | **121** | 145 |
| Investment in joint venture and associates | 6.3 | **505** | 486 |
| Goodwill and intangible assets | 5.1 | **3,332** | 3,410 |
| Total assets | | **29,597** | 30,030 |
| **LIABILITIES** | | | |
| Trade and other payables | 2.7 | **2,434** | 2,346 |
| Current tax liabilities | | **169** | 5 |
| Unearned premium liability | 2.4 | **6,331** | 6,220 |
| Outstanding claims liability | 2.2 | **11,371** | 11,741 |
| Non-controlling interests in unitholders' funds | | **219** | 247 |
| Provisions | 5.3 | **329** | 370 |
| Other liabilities | | **328** | 354 |
| Interest bearing liabilities | 4.1 | **1,624** | 1,962 |
| Total liabilities | | **22,805** | 23,245 |
| Net assets | | **6,792** | 6,785 |
| **EQUITY** | | | |
| Share capital | 4.2 | **7,082** | 7,275 |
| Treasury shares held in trust | | **(38)** | (43) |
| Reserves | | **17** | 32 |
| Retained earnings | | **(499)** | (701) |
| Parent interest | | **6,562** | 6,563 |
| Non-controlling interests | | **230** | 222 |
| Total equity | | **6,792** | 6,785 |

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

# CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

**FOR THE YEAR ENDED 30 JUNE 2017**

| | SHARE CAPITAL $m | TREASURY SHARES HELD IN TRUST $m | FOREIGN CURRENCY TRANSLATION RESERVE $m | SHARE BASED REMUN-ERATION RESERVE $m | RETAINED EARNINGS $m | NON-CONTROLLING INTERESTS $m | TOTAL EQUITY $m |
|---|---|---|---|---|---|---|---|
| **2017** | | | | | | | |
| Balance at the beginning of the financial year | **7,275** | **(43)** | **(3)** | **35** | **(701)** | **222** | **6,785** |
| Profit for the year | **-** | **-** | **-** | **-** | **929** | **76** | **1,005** |
| Other comprehensive income/(expense) | **-** | **-** | **(16)** | **-** | **25** | **-** | **9** |
| Total comprehensive income/(expense) for the year | **-** | **-** | **(16)** | **-** | **954** | **76** | **1,014** |
| **Transactions with owners in their capacity as owners** | | | | | | | |
| Off-market share buy-back, including transaction costs | **(193)** | **-** | **-** | **-** | **(123)** | **-** | **(316)** |
| Share based remuneration | **-** | **5** | **-** | **1** | **(3)** | **-** | **3** |
| Purchase of non-controlling interest | **-** | **-** | **-** | **-** | **(3)** | **-** | **(3)** |
| Dividends determined and paid | **-** | **-** | **-** | **-** | **(623)** | **(68)** | **(691)** |
| Balance at the end of the financial year | **7,082** | **(38)** | **(19)** | **36** | **(499)** | **230** | **6,792** |
| 2016 | | | | | | | |
| Balance at the beginning of the financial year | 7,275 | (83) | (68) | 30 | (337) | 201 | 7,018 |
| Profit for the year | - | - | - | - | 625 | 77 | 702 |
| Other comprehensive income/(expense) | - | - | 65 | - | (32) | - | 33 |
| Total comprehensive income for the year | - | - | 65 | - | 593 | 77 | 735 |
| **Transactions with owners in their capacity as owners** | | | | | | | |
| Share based remuneration | - | 40 | - | 5 | (12) | - | 33 |
| Dividends determined and paid | - | - | - | - | (948) | (56) | (1,004) |
| Dividends received on treasury shares held in trust | - | - | - | - | 3 | - | 3 |
| Balance at the end of the financial year | 7,275 | (43) | (3) | 35 | (701) | 222 | 6,785 |

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

# CONSOLIDATED CASH FLOW STATEMENT

## FOR THE YEAR ENDED 30 JUNE 2017

| | NOTE | 2017 $m | 2016 $m |
|---|---|---|---|
| **CASH FLOWS FROM OPERATING ACTIVITIES** | | | |
| Premium received | | **11,793** | 11,310 |
| Reinsurance and other recoveries received | | **3,129** | 2,170 |
| Claims costs paid | | **(8,995)** | (9,447) |
| Outwards reinsurance premium expense paid | | **(3,329)** | (4,029) |
| Dividends, interest and trust distributions received | | **458** | 525 |
| Finance costs paid | | **(86)** | (95) |
| Income taxes paid | | **(137)** | (388) |
| Other operating receipts | | **1,566** | 1,582 |
| Other operating payments | | **(3,763)** | (3,574) |
| Net cash flows from operating activities | 8.1 | **636** | (1,946) |
| **CASH FLOWS FROM INVESTING ACTIVITIES** | | | |
| Net cash flows on acquisition of subsidiaries and associates | | **37** | 5 |
| Net cash flows from sale/(purchase) of investments and plant and equipment | | **1,081** | 2,362 |
| Net cash flows from investing activities | | **1,118** | 2,367 |
| **CASH FLOWS FROM FINANCING ACTIVITIES** | | | |
| Outlays for repurchase of shares, including transaction costs | | **(316)** | - |
| Proceeds from borrowings, net of transaction costs | | **394** | 326 |
| Repayment of borrowings | | **(727)** | (131) |
| Net cash flow from issue and redemption of trust units | | **(38)** | 45 |
| Dividends paid to IAG shareholders | | **(623)** | (948) |
| Dividends paid to non-controlling interests | | **(68)** | (56) |
| Dividends received on treasury shares | | **-** | 3 |
| Net cash flows from financing activities | | **(1,378)** | (761) |
| Net movement in cash held | | **376** | (340) |
| Effects of exchange rate changes on balances of cash held in foreign currencies | | **-** | 11 |
| Cash and cash equivalents at the beginning of the financial year | | **1,104** | 1,433 |
| Cash and cash equivalents at the end of the financial year | 8.1 | **1,480** | 1,104 |

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

# NOTES TO THE FINANCIAL STATEMENTS

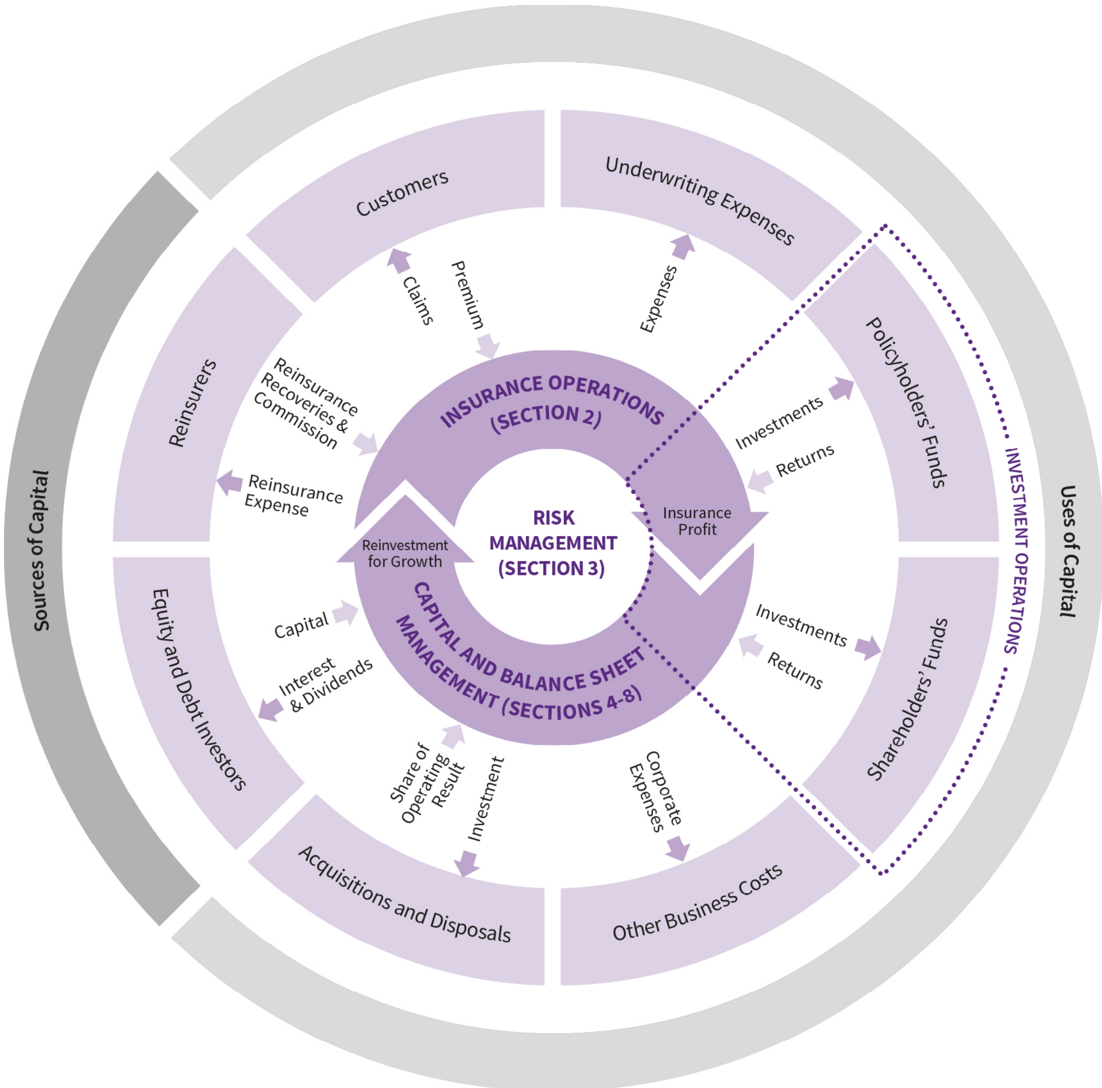
## 1. OVERVIEW

### NOTE 1.1 INTRODUCTION

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

The financial report has been organised into the following sections:

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



## NOTE 1.2 ABOUT THIS REPORT

### A. CORPORATE INFORMATION

Insurance Australia Group Limited (IAG, Parent or Company), the ultimate parent entity in the Consolidated entity, is a for-profit company, incorporated and domiciled in Australia and limited by shares publicly traded on the Australian Securities Exchange (ASX). Its registered office and principal place of business is Level 26, 388 George Street, Sydney, NSW 2000, Australia. This financial report covers the consolidated financial statements for the Company and its subsidiaries (Group or Consolidated entity) for the year ended 30 June 2017.

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

### B. STATEMENT OF COMPLIANCE

This general purpose financial report was authorised by the Board of Directors for issue on 23 August 2017 and complies with International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB), the Corporations Act 2001, Australian Accounting Standards (AASBs) adopted by the Australian Accounting Standards Board (AASB), other authoritative pronouncements of the AASB and the ASX Listing Rules.

The current IFRS standard for insurance contracts does not include a comprehensive set of recognition and measurement criteria. The IASB has recently issued a new standard (IFRS 17 Insurance Contracts) that does include such criteria, however this standard will not come into effect until 1 January 2021. Until this standard takes effect, the financial reports of insurers in different countries that comply with IFRS may not be comparable in terms of the recognition and measurement of insurance contracts.

### C. BASIS OF PREPARATION

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

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

#### I. Basis of consolidation

The consolidated financial statement incorporates the assets and liabilities of all entities controlled by the Company as at 30 June 2017. A list of significant controlled entities is set out in Note 6.1 Details of subsidiaries. IAG controls an investee if it has (i) power over the investee; (ii) exposure, or rights, to variable returns from its involvement with the investee; and (iii) the ability to use its power over the investee to affect the amount of those returns. Where an entity either began or ceased to be controlled during a financial year, the results are included from the date control commenced or up to the date control ceased. The financial information of all subsidiaries is prepared for consolidation for the same reporting year as the Parent. In preparing the consolidated financial statements, all inter-company balances and transactions, including income, expenses, and profits and losses resulting from intra-Group transactions, have been eliminated.

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

#### II. Presentation and foreign currency

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

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

### D. SIGNIFICANT ACCOUNTING POLICIES ADOPTED

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

#### I. Changes in accounting policies

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

#### II. Critical accounting estimates and judgements

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

| AREAS OF CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS | REFERENCE |
|---|---|
| Claims and reinsurance and other recoveries on outstanding claims | Note 2.2 |
| Liability adequacy test | Note 2.4 |
| Intangible assets and goodwill impairment testing, initial measurement and useful life | Note 5.1 |
| Income tax and related assets and liabilities | Note 5.2 |
| Investment in joint venture and associates impairment testing | Note 6.3 |

## NOTE 1.3 SEGMENT REPORTING

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

### A. REPORTABLE SEGMENTS

The Consolidated entity has general insurance operations in Australia, New Zealand and Asia, with the reportable segments for the period ended 30 June 2017 comprising the following business divisions:

#### I. Consumer division (Australia)

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

#### II. Business division (Australia)

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

#### III. New Zealand

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

#### IV. Asia

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

#### V. Corporate and other

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

## B. FINANCIAL INFORMATION

| | AUSTRALIA CONSUMER DIVISION | AUSTRALIA BUSINESS DIVISION | NEW ZEALAND | ASIA | CORPORATE AND OTHER | TOTAL |
|---|---|---|---|---|---|---|
| | $m | $m | $m | $m | $m | $m |
| **2017** | | | | | | |
| **I. Financial performance** | | | | | | |
| Total external revenue[a] | **8,162** | **4,241** | **3,276** | **531** | **292** | **16,502** |
| Underwriting profit/(loss) | **816** | **141** | **80** | **(21)** | **1** | **1,017** |
| Net investment income on assets backing insurance liabilities | **125** | **63** | **45** | **9** | **(1)** | **241** |
| Insurance profit/(loss) | **941** | **204** | **125** | **(12)** | **-** | **1,258** |
| Net investment income on shareholders' funds | **-** | **-** | **-** | **-** | **249** | **249** |
| Share of net profit/(loss) of associates | **-** | **(1)** | **-** | **22** | **(2)** | **19** |
| Finance costs | **-** | **-** | **-** | **-** | **(93)** | **(93)** |
| Other net operating result | **-** | **(28)** | **-** | **-** | **(71)** | **(99)** |
| Total segment result | **941** | **175** | **125** | **10** | **83** | **1,334** |
| Income tax expense | | | | | | **(329)** |
| Profit for the year | | | | | | **1,005** |
| **II. Other segment information** | | | | | | |
| Capital expenditure[b] | **-** | **-** | **-** | **-** | **109** | **109** |
| Depreciation and amortisation expense | **53** | **54** | **52** | **3** | **1** | **163** |
| 2016 | | | | | | |
| **I. Financial performance** | | | | | | |
| Total external revenue[a] | 7,956 | 4,563 | 2,791 | 513 | 949 | 16,772 |
| Underwriting profit/(loss) | 544 | 41 | 128 | 2 | (5) | 710 |
| Net investment income on assets backing insurance liabilities | 261 | 189 | 7 | 5 | 1 | 463 |
| Insurance profit/(loss) before capitalised software accelerated amortisation and impairment | 805 | 230 | 135 | 7 | (4) | 1,173 |
| Capitalised software accelerated amortisation and impairment expense | - | - | - | - | (198) | (198) |
| Net investment income on shareholders' funds | - | - | - | - | 97 | 97 |
| Share of net profit/(loss) of associates | - | 1 | - | 19 | (3) | 17 |
| Finance costs | - | - | - | - | (99) | (99) |
| Other net operating result | - | 4 | 1 | - | (75) | (70) |
| Total segment result | 805 | 235 | 136 | 26 | (282) | 920 |
| Income tax expense | | | | | | (218) |
| Profit for the year | | | | | | 702 |
| **II. Other segment information** | | | | | | |
| Capital expenditure[b] | - | - | - | - | 189 | 189 |
| Depreciation, amortisation and impairment expense | 57 | 87 | 49 | 3 | 198 | 394 |

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

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

# 2. INSURANCE DISCLOSURES

**SECTION INTRODUCTION**

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

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

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

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

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

## NOTE 2.1 GENERAL INSURANCE REVENUE

| | **2017** | 2016 |
|---|---|---|
| | **$m** | $m |
| **A. COMPOSITION** | | |
| Gross written premium | **11,805** | 11,367 |
| Movement in unearned premium liability | **(113)** | 44 |
| Gross earned premium | **11,692** | 11,411 |
| Reinsurance and other recoveries revenue | **3,375** | 3,798 |
| Reinsurance commission revenue | **715** | 745 |
| Total general insurance revenue | **15,782** | 15,954 |

**B. RECOGNITION AND MEASUREMENT**

**I. Premium revenue**

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

**II. Reinsurance and other recoveries**

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

**III. Reinsurance commission revenue**

Reinsurance commission revenue includes reimbursements by reinsurers to cover a share of IAG’s operating costs and, where applicable, fee income which reinsurers pay for accessing IAG's franchise. These income items are recognised broadly in line with the reference premium over the term of the reinsurance agreements. Where applicable, the reinsurance commission revenue also includes income which is based on the expected profitability of the covered business ceded to the reinsurer. The final value of the variable commission revenue recognised is subject to the achievement of a specified underlying profitability hurdle rate over time. This variable revenue is recognised over the term of the reinsurance contract on a straight line, or other systematic basis, in accordance with the terms of the contract, and is reassessed at each reporting date.

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

### A. NET CLAIMS EXPENSE

| | Current year | Prior years | 2017 Total | Current year | Prior years | 2016 Total |
|---|---|---|---|---|---|---|
| | $m | $m | $m | $m | $m | $m |
| Gross claims - undiscounted | **9,637** | **(1,012)** | **8,625** | 8,934 | (786) | 8,148 |
| Discount | **(135)** | **148** | **13** | (165) | 517 | 352 |
| Gross claims - discounted | **9,502** | **(864)** | **8,638** | 8,769 | (269) | 8,500 |
| Reinsurance and other recoveries - undiscounted | **(3,449)** | **25** | **(3,424)** | (3,128) | (949) | (4,077) |
| Discount | **66** | **(17)** | **49** | 302 | (23) | 279 |
| Reinsurance and other recoveries - discounted | **(3,383)** | **8** | **(3,375)** | (2,826) | (972) | (3,798) |
| Net claims expense | **6,119** | **(856)** | **5,263** | 5,943 | (1,241) | 4,702 |

### B. NET OUTSTANDING CLAIMS LIABILITY

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

| | 2017 | 2016 |
|---|---|---|
| | $m | $m |
| Gross central estimate - discounted | **9,224** | 9,548 |
| Reinsurance and other recoveries - discounted | **(4,358)** | (4,009) |
| Net central estimate - discounted | **4,866** | 5,539 |
| Claims handling costs - discounted | **362** | 384 |
| Risk margin | **885** | 1,129 |
| Net outstanding claims liability - discounted | **6,113** | 7,052 |

The gross outstanding claims liability includes $6,488 million (2016-$6,940 million) which is expected to be settled more than 12 months from the reporting date.

The carrying value of reinsurance and other recoveries includes $3,151 million (2016-$2,694 million) which is expected to be settled more than 12 months from the reporting date.

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

| | 2017 | 2016 |
|---|---|---|
| | $m | $m |
| Net outstanding claims liability at the beginning of the financial year | **7,052** | 8,974 |
| Movement in the prior year central estimate | **(387)** | (580) |
| Current year claims incurred, net of reinsurance and other recoveries | **5,871** | 5,474 |
| Claims paid, net of reinsurance and other recoveries received | **(6,208)** | (6,703) |
| Movement in discounting | **40** | 224 |
| Movement in risk margin | **(244)** | (431) |
| Net foreign currency movements | **(11)** | 94 |
| Net outstanding claims liability at the end of the financial year | **6,113** | 7,052 |
| Reinsurance and other recoveries on outstanding claims liability | **5,258** | 4,689 |
| Gross outstanding claims liability at the end of the financial year | **11,371** | 11,741 |

**III. Maturity analysis**

Refer to Note 3.1 Risk and capital management for details of the maturity profile of the estimated net discounted outstanding claims liability based on the remaining term to payment at the reporting date.

**IV. Development table**

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

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

| | | | | | | | | | | | ACCIDENT YEAR | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 2007 and prior $m | 2008 $m | 2009 $m | 2010 $m | 2011 $m | 2012 $m | 2013 $m | 2014 $m | 2015 $m | 2016 $m | **2017 $m** | Total $m |
| NET ULTIMATE CLAIM PAYMENTS | | | | | | | | | | | | |
| Development | | | | | | | | | | | | |
| At end of accident year | | **4,691** | **4,707** | **4,653** | **5,001** | **5,206** | **5,174** | **5,633** | **6,317** | **4,961** | **5,343** | |
| One year later | | **4,651** | **4,741** | **4,627** | **5,117** | **5,281** | **5,098** | **5,638** | **6,244** | **4,938** | | |
| Two years later | | **4,644** | **4,677** | **4,525** | **5,160** | **5,222** | **5,017** | **5,552** | **6,182** | | | |
| Three years later | | **4,622** | **4,669** | **4,474** | **5,192** | **5,132** | **4,938** | **5,411** | | | | |
| Four years later | | **4,602** | **4,583** | **4,422** | **5,402** | **5,080** | **4,858** | | | | | |
| Five years later | | **4,532** | **4,530** | **4,369** | **5,474** | **5,019** | | | | | | |
| Six years later | | **4,521** | **4,485** | **4,334** | **5,484** | | | | | | | |
| Seven years later | | **4,506** | **4,448** | **4,304** | | | | | | | | |
| Eight years later | | **4,487** | **4,444** | | | | | | | | | |
| Nine years later | | **4,471** | | | | | | | | | | |
| Current estimate of net ultimate claim payments | | **4,471** | **4,444** | **4,304** | **5,484** | **5,019** | **4,858** | **5,411** | **6,182** | **4,938** | **5,343** | |
| Cumulative payments made to date | | **4,430** | **4,390** | **4,230** | **5,158** | **4,868** | **4,585** | **4,892** | **5,454** | **4,178** | **3,371** | |
| Net undiscounted outstanding claims liability | **155** | **41** | **54** | **74** | **326** | **151** | **273** | **519** | **728** | **760** | **1,972** | **5,053** |
| Discount to present value | **(10)** | **(3)** | **(3)** | **(5)** | **(7)** | **(9)** | **(14)** | **(21)** | **(28)** | **(33)** | **(54)** | **(187)** |
| Net discounted outstanding claims liability | **145** | **38** | **51** | **69** | **319** | **142** | **259** | **498** | **700** | **727** | **1,918** | **4,866** |
| Reconciliation | | | | | | | | | | | | |
| Claims handling costs | | | | | | | | | | | | **362** |
| Risk margin | | | | | | | | | | | | **885** |
| Net outstanding claims liability | | | | | | | | | | | | **6,113** |

## C. RECOGNITION AND MEASUREMENT

**I. Outstanding claims liability and claims expense**

Claims expense represents claim payments and the movement in the closing outstanding claims liability from one financial period to the next. Current year claims relate to loss events that occurred during the current financial year. Prior year claims represent the movement on the estimates held for claims that occurred in all previous financial periods. Allowance has been made for potential remediation costs resulting from the past sale by a subsidiary company of add-on insurance through car and motorcycle dealers.

The outstanding claims liability is determined based on three building blocks:

- a central estimate of the future cash flows;
- discounting for the effect of the time value of money; and
- a risk margin for uncertainty.

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

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

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

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

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

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

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

| | **2017** | 2016 |
|---|---|---|
| | **%** | % |
| The percentage risk margin applied to the net outstanding claims liability | **17** | 19 |
| The probability of adequacy of the risk margin | **90** | 90 |

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

## D. SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS

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

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

| ASSUMPTION | AUSTRALIA | | | |
|---|---|---|---|---|
| | CONSUMER DIVISION | BUSINESS DIVISION | NEW ZEALAND | ASIA |
| **2017** | | | | |
| Discounted average term to settlement | **2.1 years** | **2.0 year** | **1.0 years** | **0.4 years** |
| Inflation rate | **2.4%-4.1%** | **0.0%-4.3%** | **2.0%** | **0.0%-4.0%** |
| Superimposed inflation rate | **0.0%-5.0%** | **0.0%-5.0%** | **0.0%** | **0.0%** |
| Discount rate | **1.5%-4.5%** | **1.5%-4.4%** | **1.8%-3.5%** | **0.0%** |
| Claims handling costs ratio | **4.1%** | **4.4%** | **4.1%** | **1.6%** |
| 2016 | | | | |
| Discounted average term to settlement | 2.9 years | 2.5 years | 0.9 years | 0.3 years |
| Inflation rate | 2.2%-4.0% | 0.0%-4.5% | 1.7% | 0.0%-4.0% |
| Superimposed inflation rate | 0.0%-5.0% | 0.0%-5.0% | 0.0% | 0.0% |
| Discount rate | 1.5%-4.5% | 1.6%-3.2% | 1.8%-2.3% | 0.0% |
| Claims handling costs ratio | 4.1% | 4.6% | 4.2% | 1.9% |

a. DISCOUNTED AVERAGE TERM TO SETTLEMENT

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

b. INFLATION RATE AND SUPERIMPOSED INFLATION

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

c. DISCOUNT RATE

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

d. CLAIMS HANDLING COSTS RATIO

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

**II. Reinsurance and other recoveries on outstanding claims**

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

**E. SENSITIVITY ANALYSIS**

The impact on the divisional net outstanding claims liabilities (net of reinsurance recoveries) before income tax to changes in key actuarial assumptions is summarised below. Each change has been calculated in isolation of the other changes, and without regard to other balance sheet changes that may occur simultaneously. The movements are stated in absolute terms where the base assumption is a percentage or average term.

| ASSUMPTION | MOVEMENT IN ASSUMPTION | AUSTRALIA CONSUMER DIVISION | AUSTRALIA BUSINESS DIVISION | NEW ZEALAND | ASIA |
|---|---|---|---|---|---|
| | | $m | $m | $m | $m |
| **2017** | | | | | |
| Discounted average term to settlement | **+10%** | **(14)** | **(9)** | **(1)** | **-** |
| | **-10%** | **14** | **9** | **1** | **-** |
| Inflation rate | **+1%** | **61** | **40** | **5** | **-** |
| | **-1%** | **(59)** | **(39)** | **(5)** | **-** |
| Discount rate | **+1%** | **(61)** | **(39)** | **(5)** | **-** |
| | **-1%** | **65** | **42** | **5** | **-** |
| Claims handling costs ratio | **+1%** | **53** | **41** | **7** | **2** |
| | **-1%** | **(53)** | **(41)** | **(7)** | **(2)** |
| 2016 | | | | | |
| Discounted average term to settlement | +10% | (21) | (11) | (1) | - |
| | -10% | 21 | 11 | 1 | - |
| Inflation rate | +1% | 101 | 56 | 4 | - |
| | -1% | (96) | (53) | (4) | - |
| Discount rate | +1% | (99) | (54) | (3) | - |
| | -1% | 107 | 58 | 3 | - |
| Claims handling costs ratio | +1% | 56 | 42 | 6 | 2 |
| | -1% | (56) | (42) | (6) | (2) |

## NOTE 2.3 INVESTMENTS

| | 2017 | 2016 |
|---|---|---|
| | $m | $m |
| **A. INVESTMENT INCOME** | | |
| Dividend revenue | **46** | 34 |
| Interest revenue | **378** | 448 |
| Trust revenue | **19** | 26 |
| Realised net gains/(losses) | **88** | (74) |
| Unrealised net (losses)/gains | **(12)** | 163 |
| Total investment income | **519** | 597 |
| **Represented by** | | |
| Investment income on assets backing insurance liabilities | **257** | 484 |
| Investment income on shareholders' funds | **262** | 113 |
| | **519** | 597 |
| **B. INVESTMENT COMPOSITION** | | |
| **I. Interest bearing investments** | | |
| Cash and short term money | **1,056** | 841 |
| Government and semi-government bonds | **1,034** | 1,671 |
| Corporate bonds and notes | **6,311** | 6,826 |
| Subordinated securities | **1,768** | 1,636 |
| Other | **199** | 160 |
| | **10,368** | 11,134 |
| **II. Equity investments (includes exposure to convertible securities)** | | |
| Listed | **1,099** | 1,045 |
| Unlisted | **479** | 446 |
| | **1,578** | 1,491 |
| **III. Other investments** | | |
| Other trusts | **158** | 291 |
| Derivatives | **32** | 30 |
| | **190** | 321 |
| Total investments | **12,136** | 12,946 |

## C. RECOGNITION AND MEASUREMENT

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

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

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

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

### I. Level 1 quoted prices

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

### II. Level 2 other observable inputs

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

### III. Level 3 unobservable inputs

The fair value is determined using valuation techniques in which a number of the significant inputs are not based on observable market data. Level 3 investments are primarily unlisted private equity funds where the fair value of investments is determined on the basis of published redemption values of those funds. This category also includes IAG's unlisted equity interest in Bohai Property Insurance Company Limited (Bohai). The fair value of Bohai is supported by comparable transaction multiples observed in the local market.

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

| | LEVEL 1<br>$m | LEVEL 2<br>$m | LEVEL 3<br>$m | TOTAL<br>$m |
|---|---|---|---|---|
| **2017** | | | | |
| Interest bearing investments | **2,085** | **8,282** | **1** | **10,368** |
| Equity investments | **1,076** | **340** | **162** | **1,578** |
| Other investments | **4** | **185** | **1** | **190** |
| | **3,165** | **8,807** | **164** | **12,136** |
| 2016 | | | | |
| Interest bearing investments | 2,047 | 9,086 | 1 | 11,134 |
| Equity investments | 1,021 | 313 | 157 | 1,491 |
| Other investments | 14 | 306 | 1 | 321 |
| | 3,082 | 9,705 | 159 | 12,946 |

## NOTE 2.4 UNEARNED PREMIUM LIABILITY

| | 2017 $m | 2016 $m |
|---|---|---|
| **A. RECONCILIATION OF MOVEMENTS** | | |
| Unearned premium liability at the beginning of the financial year | **6,220** | 6,156 |
| Deferral of premiums written during the financial year | **6,097** | 5,866 |
| Earning of premiums written in previous financial years | **(5,984)** | (5,910) |
| Additions through business acquisition | **-** | 20 |
| Net foreign exchange movements | **(2)** | 88 |
| Unearned premium liability at the end of the financial year | **6,331** | 6,220 |

The carrying value of unearned premium liability includes $172 million (2016-$236 million) which is expected to be earned more than 12 months from reporting date.

### B. RECOGNITION AND MEASUREMENT

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

### C. ADEQUACY OF UNEARNED PREMIUM LIABILITY

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

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

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

The LAT at reporting date resulted in a surplus for the Group (2016-surplus for the Group), with the table below providing details of the net premium liabilities (net of reinsurance and adjusted for appropriate risk margin) used in the LAT:

| | 2017 $m | 2016 $m |
|---|---|---|
| Net central estimate of present value of expected future cash flows from future claims | **3,416** | 3,564 |
| Risk margin of the present value of expected future cash flows | **77** | 82 |
| | **3,493** | 3,646 |
| Risk margin percentage | **2.3%** | 2.3% |
| Probability of adequacy | **60.0%** | 60.0% |

#### II. Significant accounting estimates and judgements

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

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

## NOTE 2.5 DEFERRED INSURANCE EXPENSES

| | DEFERRED ACQUISITION COSTS[(a)] | | DEFERRED OUTWARDS REINSURANCE EXPENSE[(b)] | | TOTAL DEFERRED INSURANCE EXPENSES | |
|---|---|---|---|---|---|---|
| | **2017** | 2016 | **2017** | 2016 | **2017** | 2016 |
| | **$m** | $m | **$m** | $m | **$m** | $m |
| **A. RECONCILIATION OF MOVEMENTS** | | | | | | |
| At the beginning of the financial year | **1,051** | 1,015 | **1,727** | 1,823 | **2,778** | 2,838 |
| Costs deferred | **1,843** | 1,769 | **3,251** | 3,744 | **5,094** | 5,513 |
| Amortisation charged to profit | **(1,873)** | (1,749) | **(3,227)** | (3,883) | **(5,100)** | (5,632) |
| Net foreign exchange movements | **(1)** | 16 | **(1)** | 43 | **(2)** | 59 |
| Deferred costs at the end of the financial year | **1,020** | 1,051 | **1,750** | 1,727 | **2,770** | 2,778 |

(a) The carrying value of deferred acquisition costs includes $54 million (2016-$90 million) which is expected to be amortised more than 12 months from reporting date.

(b) The carrying value of deferred outwards reinsurance expense includes $42 million (2016-$28 million) which is expected to be amortised more than 12 months from reporting date.

### B. RECOGNITION AND MEASUREMENT

#### I. Acquisition costs

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

#### II. Outwards reinsurance expense

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

## NOTE 2.6 TRADE AND OTHER RECEIVABLES

| | **2017** | 2016 |
|---|---|---|
| | **$m** | $m |
| **A. COMPOSITION** | | |
| **I. Premium receivable** | | |
| Gross premium receivable | **3,402** | 3,370 |
| Provision for impairment | **(39)** | (36) |
| Net premium receivable | **3,363** | 3,334 |
| **II. Trade and other receivables[(a)]** | | |
| Reinsurance recoveries on paid claims | **242** | 658 |
| Loan to associates[(b)] | **90** | 99 |
| Investment related receivables | **280** | 98 |
| Trade and other debtors | **178** | 132 |
| Trade and other receivables | **790** | 987 |
| | **4,153** | 4,321 |

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

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

### B. RECOGNITION AND MEASUREMENT

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

## NOTE 2.7 TRADE AND OTHER PAYABLES

| | 2017 $m | 2016 $m |
|---|---|---|
| **A. COMPOSITION** | | |
| **I. Reinsurance premium payable[(a)]** | **712** | 848 |
| **II. Trade creditors[(b)]** | | |
| Commissions payable | **268** | 257 |
| Stamp duty payable | **123** | 116 |
| GST payable on premium receivable | **157** | 147 |
| Corporate treasury derivatives payable | **-** | 22 |
| Other[(c)] | **472** | 543 |
| | **1,020** | 1,085 |
| **III. Other payables[(b)]** | | |
| Other creditors and accruals | **378** | 371 |
| Investment creditors | **310** | 27 |
| Interest payable on interest bearing liabilities | **14** | 15 |
| | **702** | 413 |
| | **2,434** | 2,346 |

(a) Under the agreement with National Indemnity Company (NICO), a Berkshire Hathaway (BH) company, the Group has a right of offset, and settles on a net basis. This balance includes reinsurance premium payable to BH of $1,166 million (2016-$1,126 million), which has been offset with receivables due under the contract of $677 million (2016-$620 million). The relevant cash flows pertaining to the contract have been presented on a gross basis within the cash flow statement.

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

(c) Other trade creditors include $6 million (2016-$25 million) reinsurance collateral arrangements with various reinsurers to secure the Group reinsurance recoveries. The balance is anticipated to reduce through the settlement of amounts from reinsurers as they fall due. This payable is interest bearing.

### B. RECOGNITION AND MEASUREMENT

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

# 3. RISK

### SECTION INTRODUCTION

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

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

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

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

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

## NOTE 3.1 RISK AND CAPITAL MANAGEMENT

### A. RISK MANAGEMENT OVERVIEW

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

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

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

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

Other key documents within the Group's RMF include:

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

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

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

## B. STRATEGIC RISK

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

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

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

## C. INSURANCE RISK

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

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

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

### I. Acceptance and pricing of risk

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

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

Business divisions underwrite to set criteria as contained in the Insurance Business Licence. Maximum limits are set for the acceptance of risk both on an individual insurance contract basis and for classes of business and specific risk groupings.

Management information systems are maintained to provide up to date, reliable data on the risks to which the business is exposed at any point in time.  Statistical models that combine historical and projected data (pricing, claims and market conditions) are used to calculate premiums and monitor claims patterns for each class of business.

**II. Claims management and provisioning**

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

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

**III. Concentrations of insurance risk**

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

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

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

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

| | **2017** | 2016 |
|---|---|---|
| | **%** | % |
| a. REGION | | |
| Australia | **77** | 77 |
| New Zealand | **20** | 19 |
| Asia | **3** | 4 |
| | **100** | 100 |
| b. PRODUCT | | |
| Motor | **32** | 32 |
| Home | **27** | 27 |
| Short tail commercial | **22** | 22 |
| CTP (motor liability) | **8** | 8 |
| Liability | **5** | 5 |
| Other short tail | **3** | 3 |
| Workers' compensation | **3** | 3 |
| | **100** | 100 |

## D. REINSURANCE RISK

Reinsurance risk is defined as the risk of:

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

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

The Group purchases catastrophe reinsurance protection to the greater of:

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

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

Dynamic financial analysis modelling is used to determine the optimal level at which reinsurance should be purchased for capital efficiency, compared with the cost and benefits of covers available in the market.

To facilitate the reinsurance process, manage counterparty exposure and create economies of scale, the Group has established captive reinsurance operations across Australia, Singapore and Labuan. The captives act as the reinsurer for the Group by being the buyer of the Group's outwards reinsurance program. While the majority of business ceded by the Consolidated entity's subsidiaries is reinsured with the Group's captive reinsurance operations, some individual businesses are required by their regulator to purchase reinsurance locally. This is monitored by the captives.

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

### I. Current reinsurance program

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

- a 20% whole-of-account quota share;
- a Group catastrophe cover which is placed in line with the strategy of buying to the level of a 1-in-250 years event on a whole-of-portfolio basis. IAG's catastrophe reinsurance protection runs to a calendar year and operates on an excess of loss basis, with the Group retaining the first $250 million ($200 million post-quota share) of each loss. It covers all territories in which IAG operates. The limit of catastrophe cover purchased was $7 billion placed to 80%. Should a loss event occur that is greater than $7 billion, the Group could potentially incur a net loss greater than the retention. The Group holds capital to mitigate the impact of this possibility;
- additional $1 billion catastrophe cover in excess of $7 billion placed to 80%. The reinsurance protection runs for a period of 19 months, commencing 1 June 2017. The existing $7 billion remains in force and will be renewed in January 2018;
- an aggregate sideways cover which protects against a frequency of attritional event losses in Australia, New Zealand and Asia, and operates below the Group catastrophe cover;
- excess of loss reinsurances which provide 'per risk' protection for retained exposures of the commercial property and engineering businesses in Australia, New Zealand, Thailand, Malaysia, Vietnam and Indonesia;
- excess of loss reinsurance for all casualty portfolios including CTP, public liability, workers' compensation and home owners warranty products;
- quota share protection for agency distributed financial lines products including surety and trade credit;
- quota share protection for cyber;
- excess of loss reinsurance for all marine portfolios;
- excess of loss reinsurance cover for retained natural peril losses;
- crop quota share & stop loss;
- adverse development cover (ADC) and quota share protection on the CTP portfolio;
- ADC for the February 2011 Canterbury earthquake event; and
- ADC for policies issued prior to 31 December 2015 covering IAG's exposure to asbestos relating to legacy general liability and/or workers' compensation policies.

## E. FINANCIAL RISK

Financial risk is defined as the risk of:

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

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

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

### I. Market risk

#### a. FOREIGN EXCHANGE RISK

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

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

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

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

| IMPACT OF 10% DEPRECIATION OF AUSTRALIAN DOLLAR | **2017** | 2016 |
|---|---|---|
| | **$m** | $m |
| | **Impact directly to equity** | Impact directly to equity |
| Net investments in foreign operations and related hedge arrangements | | |
| New Zealand dollar | **66** | 65 |
| Malaysian ringgit | **18** | 15 |
| Other currencies where considered significant | **13** | 14 |
| | **97** | 94 |

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

#### b. PRICE RISK

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

| IMPACT OF CHANGE IN EQUITY VALUE | | **2017** | 2016 |
|---|---|---|---|
| | | **$m** | $m |
| | | **Impact to profit** | Impact to profit |
| Investments – equity and trust securities and related equity derivatives | +10% | **108** | 115 |
| | -10% | **(107)** | (115) |

c. INTEREST RATE RISK

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

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

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

| IMPACT OF CHANGE IN FIXED INTEREST BEARING SECURITIES VALUE | | **2017** | 2016 |
|---|---|---|---|
| | | **$m** | $m |
| | | **Impact to profit** | Impact to profit |
| Investments - interest bearing securities and related interest rate derivatives | +1% | **(200)** | (228) |
| | -1% | **213** | 245 |

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

**II. Credit risk**

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

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

a. INVESTMENTS

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

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

| CREDIT RATING OF INTEREST BEARING INVESTMENTS | **2017** | 2016 |
|---|---|---|
| | **$m** | $m |
| AAA | **3,794** | 4,747 |
| AA | **3,776** | 3,820 |
| A | **433** | 972 |
| BBB and below | **2,365** | 1,595 |
| | **10,368** | 11,134 |

b. REINSURANCE RECOVERIES ON PAID CLAIMS

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

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

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

| CREDIT RATING OF REINSURANCE RECOVERIES ON OUTSTANDING CLAIMS | | **2017** | | 2016 |
|---|---|---|---|---|
| | **$m** | **% of total** | $m | % of total |
| AA | **3,367** | **86** | 2,826 | 85 |
| A | **526** | **14** | 501 | 15 |
| BBB and below | **12** | **-** | 10 | - |
| Total | **3,905** | **100** | 3,337 | 100 |

Of these, approximately $1,001 million (2016-$1,127 million) is secured directly as follows, reducing the credit risk:

- deposits held in trust: $144 million (2016-$210 million);
- letters of credit: $854 million (2016-$907 million); and
- loss deposits: $3 million (2016-$10 million).

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

| | NOT OVERDUE | | OVERDUE | | TOTAL |
|---|---|---|---|---|---|
| | | <30 days | 30-120 days | >120 days | |
| | $m | $m | $m | $m | $m |
| **2017** | | | | | |
| Reinsurance recoveries on paid claims | **128** | **11** | **44** | **59** | **242** |
| 2016 | | | | | |
| Reinsurance recoveries on paid claims | 531 | 63 | 14 | 50 | 658 |

c. PREMIUM RECEIVABLE

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

| | NOT OVERDUE | | OVERDUE | | TOTAL |
|---|---|---|---|---|---|
| | | <30 days | 30-120 days | >120 days | |
| | $m | $m | $m | $m | $m |
| **2017** | | | | | |
| Premium receivable | **2,771** | **308** | **273** | **50** | **3,402** |
| Provision for impairment | **(5)** | **(3)** | **(7)** | **(24)** | **(39)** |
| | **2,766** | **305** | **266** | **26** | **3,363** |
| 2016 | | | | | |
| Premium receivable | 2,745 | 272 | 317 | 36 | 3,370 |
| Provision for impairment | (5) | (3) | (6) | (22) | (36) |
| | 2,740 | 269 | 311 | 14 | 3,334 |

### III. Liquidity risk

The Group's liquidity position is derived from operating cash flows, access to liquidity through related bodies corporate and interest bearing liabilities (with some denominated in different currencies and with different maturities). The Group complies with its liquidity risk management practices, which include a Group policy, and has the framework and procedures in place to ensure an adequate and appropriate level of monitoring and management of liquidity.

a. OUTSTANDING CLAIMS LIABILITY AND INVESTMENTS

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

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

| MATURITY ANALYSIS | NET DISCOUNTED OUTSTANDING CLAIMS LIABILITY | | INVESTMENTS | |
|---|---|---|---|---|
| | **2017** | 2016 | **2017** | 2016 |
| | **$m** | $m | **$m** | $m |
| Floating interest rate (at call) | **-** | - | **944** | 723 |
| Within 1 year or less | **2,776** | 2,806 | **2,255** | 1,592 |
| Within 1 to 2 years | **1,182** | 1,510 | **880** | 2,109 |
| Within 2 to 5 years | **1,601** | 1,759 | **2,550** | 3,366 |
| Over 5 years | **554** | 977 | **3,739** | 3,344 |
| Total | **6,113** | 7,052 | **10,368** | 11,134 |

b. INTEREST BEARING LIABILITIES

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

| | CARRYING VALUE | MATURITY DATES OF CONTRACTUAL UNDISCOUNTED CASH FLOWS | | | | | |
|---|---|---|---|---|---|---|---|
| | | Within 1 year | 1 - 2 years | 2 - 5 years | Over 5 years | Perpetual | Total |
| | $m | $m | $m | $m | $m | $m | $m |
| **2017** | | | | | | | |
| Principal repayments[(a)] | **1,638** | **-** | **-** | **-** | **684** | **954** | **1,638** |
| Contractual interest payments[(a)] | | **73** | **73** | **220** | **-** | **-** | **366** |
| Total contractual undiscounted payments | | **73** | **73** | **220** | **684** | **954** | **2,004** |
| 2016 | | | | | | | |
| Principal repayments[(a)] | 1,969 | - | - | - | 1,042 | 927 | 1,969 |
| Contractual interest payments[(a)] | | 93 | 89 | 230 | - | - | 412 |
| Total contractual undiscounted payments | | 93 | 89 | 230 | 1,042 | 927 | 2,381 |

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

### IV. Capital management risk

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

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

The target level of capitalisation (risk appetite) for the Group is assessed by consideration of factors including:
- the probability of financial ruin over the next one to three years;
- the probability of falling below the APRA prescribed capital amount (PCA) over the next one to three years;
- other stakeholder perspectives on capitalisation, including rating agency capital models and associated ratings; and
- domestic and international levels of capitalisation.

a. REGULATORY CAPITAL

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

The Group's long term target capital ranges set out below remain unchanged:
- a total regulatory capital position equivalent to 1.4 to 1.6 times the PCA, compared to a regulatory requirement of 1.0 times; and
- Common Equity Tier 1 capital of 0.9 to 1.1 times the PCA, compared to a regulatory requirement of 0.6 times.

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

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

| REGULATORY CAPITAL POSITION | **2017** | 2016 |
|---|---|---|
| | **$m** | $m |
| Common Equity Tier 1 capital (CET1 capital) | **2,888** | 2,838 |
| Additional Tier 1 capital | **679** | 707 |
| Total Tier 1 capital | **3,567** | 3,545 |
| Tier 2 capital | **959** | 1,074 |
| Total regulatory capital | **4,526** | 4,619 |
| Total PCA | **2,661** | 2,682 |
| PCA multiple | **1.70** | 1.72 |
| CET1 multiple | **1.09** | 1.06 |

At 30 June 2017, the Group's Insurance Concentration Risk Charge (ICRC) from a catastrophe event was $200 million (2016-$200 million).

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

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

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

b. CAPITAL COMPOSITION

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

| CAPITAL MIX | **Target** | **2017** | 2016 |
|---|---|---|---|
| | % | % | % |
| Ordinary equity less goodwill and intangible assets | **60-70** | **68.1** | 63.2 |
| Interest bearing liabilities - hybrid securities and debt | **30-40** | **31.9** | 36.8 |
| Total capitalisation | | **100.0** | 100.0 |

## F. OPERATIONAL RISK

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

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

IAG's Operational Risk Framework, inclusive of the Group Operational Risk Policy, operates within IAG's RMF. The Operational Risk Framework and supporting Operational Risk Policy and procedures aim to ensure that consistent governance mechanisms and practices are in place, and that activities undertaken which involve operational risk are continually assessed and managed with appropriate regard to the Group's RAS and the achievement of IAG's objectives. The Operational Risk Framework is supported by aligned frameworks, policies and procedures for key aspects of operational risk. For example, Fraud and Business Continuity Frameworks and policies are in place as are various other operational risk policies.

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

**G. REGULATORY RISK AND COMPLIANCE**

Regulatory Risk and Compliance is defined as failure or inability to comply with applicable laws, regulations or codes excluding failure of staff to adhere to internal policies/procedures and meeting contractual obligations. Regulatory Risk and Compliance has recently been established as a standalone risk category to give it more focus and distinguish it from the risks associated with identification and management of regulatory change to the control environment and management compliance. The Group's general insurance operations are subject to regulatory supervision in the jurisdictions in which they operate, with various regulatory frameworks continuing to evolve. The Group works closely with regulators and regularly monitors developments across its international operations to assess potential impacts on its ongoing ability to meet the various regulatory requirements.

# 4. CAPITAL STRUCTURE

## SECTION INTRODUCTION

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

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

## NOTE 4.1 INTEREST BEARING LIABILITIES

| | | **2017** | | 2016 | |
|---|---|---|---|---|---|
| | Section | **Carrying Value $m** | **Fair Value $m** | Carrying Value $m | Fair Value $m |
| **A. COMPOSITION** | | | | | |
| **I. Capital nature**[(a)] | | | | | |
| a. ADDITIONAL TIER 1 REGULATORY CAPITAL[(b)] | | | | | |
| Convertible preference shares | B. I | **-** | **-** | 377 | 383 |
| Reset exchangeable securities | B. II | **550** | **569** | 550 | 550 |
| Capital notes | B. III | **404** | **431** | - | - |
| b. TIER 2 REGULATORY CAPITAL | | | | | |
| GBP subordinated term notes | B. IV | **-** | **-** | 178 | 177 |
| NZD subordinated bonds | B. V | **-** | **-** | 179 | 180 |
| AUD subordinated convertible term notes | B. VI | **350** | **356** | 350 | 352 |
| NZD subordinated convertible term notes[(c)] | B. VII | **334** | **337** | 335 | 329 |
| **II. Operational nature** | | | | | |
| Other interest bearing liabilities | | **2** | **2** | 2 | 2 |
| Less: capitalised transaction costs | | **(16)** | | (9) | |
| | | **1,624** | | 1,962 | |

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

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

(c) At the reporting date, the Company recognised accrued interest of $1 million (2016-$1 million) which is presented within trade and other payables.

## B. SIGNIFICANT TERMS AND CONDITIONS

### I. Convertible preference shares (CPS)

The CPS had a face value of $377 million and were issued by the Company. On 22 December 2016, IAG bought back and cancelled $224 million of CPS with the remaining CPS bought back and cancelled on 1 May 2017.

### II. Reset exchangeable securities (RES)

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

### III. Capital notes

- face value of $404 million and issued by the Company on 22 December 2016;
- all remain outstanding as at the reporting date;
- non-cumulative floating rate distribution payable quarterly and expected to be fully franked;
- distribution rate equals the sum of three month bank bill swap rate (BBSW) plus margin of 4.70% per annum multiplied by (1 – tax rate);
- payments of distributions can only be made subject to meeting certain conditions. If no distribution is made, no dividends can be paid and no returns of capital can be made on ordinary shares until the next distribution payment date;
- IAG may exchange or redeem capital notes on the exchange date, or upon occurrence of certain events, subject to APRA approval. The first optional exchange date is 15 June 2023;
- the capital notes are scheduled for conversion into a variable number of IAG ordinary shares (subject to a maximum number of 140.6 million shares) on 16 June 2025 and at each subsequent distribution payment date provided the mandatory conversion conditions are satisfied; and
- the capital notes must be converted into a variable number of IAG ordinary shares (subject to a maximum of 351.1 million shares) or written off if APRA determines the Company to be non-viable.

### IV. GBP subordinated term notes

The GBP subordinated term notes were issued with a face value of £250 million (equivalent to $625 million at date of issue) by the Company. A total of £150 million of the notes had been bought back prior to the current financial year with the remaining £100 million of the notes ($171 million as of the redemption date) being redeemed on 21 December 2016.

### V. NZD subordinated bonds

The NZD subordinated bonds were issued with a face value of NZ$325 million (equivalent to $246 million at date of issue) by the Company. A total of NZ$138 million of the bonds had been bought back prior to the current financial year with the remaining NZ$187 million of the bonds ($179 million as of the redemption date) redeemed on 15 December 2016.

### VI. AUD subordinated convertible term notes

- face value of $350 million and issued by Insurance Australia Limited (IAL), a wholly owned subsidiary of the Company on 19 March 2014;
- all remain outstanding as at the reporting date;
- floating interest rate equal to the three month bank bill swap rate (BBSW) plus a margin of 2.80% per annum is payable quarterly;
- the notes mature on 19 March 2040 unless converted or redeemed earlier, subject to rights of conversion or redemption;
- IAL has an option to redeem the securities at face value between years five and six and for certain tax and regulatory events (in each case subject to APRA's prior written approval);
- the securities are convertible into IAG ordinary shares at the option of holders on certain dates from year eight;
- if APRA determines IAG or IAL to be non-viable, the securities will convert into IAG ordinary shares or, if that is not possible, the securities will be written off; and
- the number of IAG ordinary shares received on conversion will be based on a volume-weighted average price (VWAP) over a certain period, less a discount of 1%. The number of IAG ordinary shares will be capped to a maximum number by reference to the VWAP at the issue date (50% of that VWAP for conversion at the holder's option and 20% of that VWAP for conversion on non-viability).

### VII. NZD subordinated convertible term notes

- face value of NZ$350 million (equivalent to $332 million at date of issue) and issued by the Company on 15 June 2016;
- all remain outstanding as at the reporting date;
- fixed interest rate of 5.15% per annum, payable quarterly;
- the notes mature on 15 June 2043 with the issuer having the option to redeem at par from and including 15 June 2022 and at each subsequent interest payment date to and including 15 June 2023, subject to approval from APRA;
- if the notes are not redeemed on 15 June 2022, the interest rate will become the applicable three month bank bill rate (BKBM) plus margin of 2.60% per annum;

- the notes can be converted into a variable number of IAG ordinary shares (subject to a maximum of 114.0 million shares) at the option of holders from and including 15 June 2025 and at each subsequent interest payment date and the maturity date of 15 June 2043; and
- the notes must be converted into a variable number of IAG ordinary shares (subject to a maximum of 284.9 million shares) or written off if APRA determines the Company to be non-viable.

### C. RECOGNITION AND MEASUREMENT

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

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

| | 2017 | 2016 | 2017 | 2016 |
|---|---|---|---|---|
| | Number of shares in millions | Number of shares in millions | $m | $m |
| **A. SHARE CAPITAL** | | | | |
| Balance at the beginning of the financial year | **2,431** | 2,431 | **7,275** | 7,275 |
| Off-market share buy-back, including transaction costs | **(64)** | - | **(193)** | - |
| Balance at the end of the financial year | **2,367** | 2,431 | **7,082** | 7,275 |

### B. STRATEGIC RELATIONSHIP WITH BH

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

#### I. Put option

IAG had an option to place up to a further 121,569,233 new shares at a maximum issue price of $6.50 per share to NICO within 24 months after the date of the Subscription Agreement. This option was not exercised as at 16 June 2017 and lapsed. Under standstill terms of the Subscription Agreement, NICO can only increase its shareholding in IAG above 14.9% with majority Board agreement and receipt of requisite regulatory approvals.

#### II. Anti-dilution right

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

### C. NATURE AND PURPOSE OF EQUITY

#### I. Ordinary shares

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

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

#### II. Treasury shares held in trust

To satisfy obligations under the various share based remuneration plans, shares are generally bought on-market at or near grant date of the relevant arrangement and are managed using in-house trusts, one for Australia and one for New Zealand, which are controlled by the Consolidated entity. The shares are measured at cost and are presented as a deduction from equity. No gain or loss is recognised in profit or loss on the sale, cancellation or reissue of the shares. The shares are derecognised as treasury shares held in trust when the shares vest or are released to the participant. The total number of treasury shares acquired on-market during the financial year was 3 million (2016-54 thousand) at an average price per share of $5.47 (2016-$5.50).

#### III. Foreign currency translation reserve

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

#### IV. Share based remuneration reserve

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

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

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

## NOTE 4.3 EARNINGS PER SHARE

| | **2017 cents** | 2016 cents |
|---|---|---|
| **A. REPORTING PERIOD VALUES** | | |
| Basic earnings per ordinary share[(a)] | **39.03** | 25.79 |
| Diluted earnings per ordinary share[(b)] | **37.72** | 25.34 |

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

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

| | **2017 $m** | 2016 $m |
|---|---|---|
| **B. RECONCILIATION OF EARNINGS USED IN CALCULATING EARNINGS PER SHARE** | | |
| Profit attributable to shareholders of the Parent which is used in calculating basic and diluted earnings per share | **929** | 625 |
| Finance costs of convertible securities, net of tax | **37** | 25 |
| Profit attributable to shareholders of the Parent which is used in calculating diluted earnings per share | **966** | 650 |

| | **2017 Number of shares in millions** | 2016 Number of shares in millions |
|---|---|---|
| **C. RECONCILIATION OF WEIGHTED AVERAGE NUMBER OF ORDINARY SHARES USED IN CALCULATING EARNINGS PER SHARE** | | |
| Weighted average number of ordinary shares on issue (adjusted for treasury shares held in trust) used in the calculation of basic earnings per share | **2,380** | 2,423 |
| **Weighted average number of dilutive potential ordinary shares relating to:** | | |
| Convertible securities | **175** | 134 |
| Unvested share based remuneration rights supported by treasury shares held in trust | **6** | 8 |
| | **2,561** | 2,565 |

## NOTE 4.4 DIVIDENDS

| | **2017 $m** | 2016 $m |
|---|---|---|
| **A. ORDINARY SHARES** | | |
| 2017 interim dividend (paid 30 March 2017): $0.13 (2016-$0.13) per ordinary share fully franked at 30%[(a)] | **307** | 316 |
| Dividend component of off-market share buy-back (paid 17 October 2016): $1.92 (2016-nil) per ordinary share fully franked at 30% | **123** | - |
| 2016 final dividend (paid 5 October 2016): $0.13 (2015-$0.16) per ordinary share fully franked at 30% | **316** | 389 |
| Special dividend: nil (2016-$0.10) per ordinary share fully franked at 30% | **-** | 243 |
| | **746** | 948 |

(a) Of the total 2017 interim dividend declared of $308 million, right and entitlement of $1 million (2016-nil) to dividends on unallocated treasury shares was waived during the year by the trustee of the IAG Share and Rights Plans Trust.

| | 2017 | 2016 |
|---|---|---|
| | $m | $m |
| **B. DIVIDEND NOT RECOGNISED AT REPORTING DATE** | | |
| 2017 final dividend: $0.20 (2016: $0.13) per ordinary share fully franked at 30% to be paid on 9 October 2017 | **474** | 316 |
| **C. DIVIDEND FRANKING AMOUNT** | | |
| Franking credits available for subsequent financial periods based on a tax rate of 30% | **115** | 212 |

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

The Company, immediately after payment of the final dividend, has no further franking credits available for distribution.

### D. DIVIDEND REINVESTMENT

A Dividend Reinvestment Plan (DRP) operates which allows shareholders with ordinary shares to elect to receive their dividend entitlement in the form of IAG shares. The price of DRP shares is the VWAP, less a discount if determined by the Directors, calculated over the pricing period (which is at least five trading days) as determined by the Directors for each dividend payment date.
A copy of the terms and conditions for the DRP is available at www.iag.com.au/shareholder-centre/dividends/reinvestment.
The DRP for the 2017 interim dividend paid on 30 March 2017 was settled with the on-market purchase of 8.0 million shares priced at $6.13 per share (based on a VWAP for 10 trading days from 6 March 2017 to 17 March 2017 inclusive, with no discount applied).

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

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

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

### F. RECOGNITION AND MEASUREMENT

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

## NOTE 4.5 DERIVATIVES

### A. REPORTING DATE POSITIONS

| | 2017 | | | 2016 | | |
|---|---|---|---|---|---|---|
| | Notional contract amount | Fair value asset | Fair value liability | Notional contract amount | Fair value asset | Fair value liability |
| | $m | $m | $m | $m | $m | $m |
| **I. Net investment hedges (hedge accounting applied)** | | | | | | |
| Forward foreign exchange contracts | **922** | **14** | **(3)** | 1,627 | 7 | (21) |
| **II. Investment related derivatives (derivatives without hedge accounting applied)** | | | | | | |
| Bond futures | **2,913** | **-** | **-** | 1,920 | - | - |
| Share price index futures | **(44)** | **-** | **-** | 40 | - | - |
| Forward foreign exchange contracts | **2,827** | **29** | **-** | 1,624 | 30 | (7) |
| Options | **(48)** | **3** | **(1)** | - | - | - |
| **III. Treasury related derivatives (derivatives without hedge accounting applied)** | | | | | | |
| Forward foreign exchange contracts | **1,160** | **11** | **(4)** | 1,851 | 20 | (30) |
| Interest rate swaps | **334** | **-** | **(5)** | 335 | 2 | - |

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

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

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

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

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

**II. Derivatives without hedge accounting applied**
For derivatives that do not qualify for hedge accounting, the changes in fair value are immediately recognised in profit or loss. Transaction costs for purchases of derivatives are expensed as incurred.

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

# 5. OTHER BALANCE SHEET DISCLOSURES

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

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

## NOTE 5.1 GOODWILL AND INTANGIBLE ASSETS

| | GOODWILL | SOFTWARE DEVELOPMENT EXPENDITURE | DISTRIBUTION CHANNELS | CUSTOMER RELATIONSHIPS | BRANDS AND OTHER | TOTAL |
|---|---|---|---|---|---|---|
| | $m | $m | $m | $m | $m | $m |
| **2017** | | | | | | |
| **A. COMPOSITION** | | | | | | |
| Cost | **2,947** | **798** | **157** | **190** | **125** | **4,217** |
| Accumulated amortisation and impairment | **-** | **(690)** | **(93)** | **(105)** | **(29)** | **(917)** |
| Net foreign exchange movements | **27** | **(9)** | **2** | **5** | **7** | **32** |
| Balance at the end of the financial year | **2,974** | **99** | **66** | **90** | **103** | **3,332** |
| **B. RECONCILIATION OF MOVEMENTS** | | | | | | |
| Balance at the beginning of the financial year | **2,982** | **132** | **96** | **93** | **107** | **3,410** |
| Additions acquired and developed | **20** | **22** | **-** | **21** | **-** | **63** |
| Disposal through sale of businesses | **(26)** | **-** | **(1)** | **-** | **-** | **(27)** |
| Amortisation | **-** | **(54)** | **(29)** | **(24)** | **(4)** | **(111)** |
| Net foreign exchange movements | **(2)** | **(1)** | **-** | **-** | **-** | **(3)** |
| Balance at the end of the financial year | **2,974** | **99** | **66** | **90** | **103** | **3,332** |
| 2016 | | | | | | |
| **C. COMPOSITION** | | | | | | |
| Cost | 2,953 | 776 | 158 | 169 | 125 | 4,181 |
| Accumulated amortisation and impairment | - | (636) | (64) | (81) | (25) | (806) |
| Net foreign exchange movements | 29 | (8) | 2 | 5 | 7 | 35 |
| Balance at the end of the financial year | 2,982 | 132 | 96 | 93 | 107 | 3,410 |
| **D. RECONCILIATION OF MOVEMENTS** | | | | | | |
| Balance at the beginning of the financial year | 2,890 | 343 | 114 | 114 | 100 | 3,561 |
| Additions acquired and developed | 44 | 62 | 11 | 2 | 7 | 126 |
| Disposal through sale of businesses | (6) | - | (5) | (2) | - | (13) |
| Amortisation | - | (80) | (28) | (23) | (3) | (134) |
| Accelerated amortisation and impairment | - | (198) | - | - | - | (198) |
| Net foreign exchange movements | 54 | 5 | 4 | 2 | 3 | 68 |
| Balance at the end of the financial year | 2,982 | 132 | 96 | 93 | 107 | 3,410 |

**E. IMPAIRMENT**

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

**I. Impairment testing of goodwill**

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

Goodwill is allocated to the following CGUs:

| | **2017** | 2016 |
|---|---|---|
| | **$m** | $m |
| Consumer Division - Australia | **771** | 771 |
| Business Division - Australia | **1,479** | 1,496 |
| New Zealand | **667** | 658 |
| Asia | **57** | 57 |
| | **2,974** | 2,982 |

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

- Cash flow forecasts are based on ten year valuation forecasts for growth and profitability. Twenty year periods are used only in emerging markets, to enable appropriate phasing to terminal values. The forecast durations reflect the insurance business life cycle and the growth trajectories of portfolios within each of the established and emerging markets.
- Terminal value is calculated using a perpetuity growth formula based on the cash flow forecast at the end of the relevant valuation forecast period, terminal growth rate in profit or premium and, where appropriate, terminal insurance margin. Terminal growth rates and insurance margins are based on past performance and management's expectations for future performance in each segment and country. The terminal growth rate assumptions used in the Group's impairment assessment for significant CGUs as at 30 June 2017 are: Australian Consumer Division 4.5% (2016-4.5%), Australian Business Division 4.5% (2016-4.3%) and New Zealand 3.5% (2016-3.5%).
- Discount rates reflect a beta and equity risk premium appropriate to the Group, with risk adjustments for individual segments and countries where applicable. The post-tax discount rates used for significant CGUs as at 30 June 2017 are: Australian Consumer Division 9.7% (2016-9.7%), Australian Business Division 9.7% (2016-9.7%) and New Zealand 10.3% (2016-10.3%).

**II. Impairment testing of identified intangible assets**

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

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

## F. RECOGNITION AND MEASUREMENT

All of the goodwill and intangible assets, other than components of capitalised software development expenditure (internally generated), have been acquired.

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

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

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

## NOTE 5.2 INCOME TAX

| | 2017 $m | 2016 $m |
|---|---|---|
| **A. INCOME TAX EXPENSE** | | |
| Current tax | **352** | 291 |
| Deferred tax | **13** | - |
| Over provided in prior year | **(36)** | (73) |
| Income tax expense | **329** | 218 |
| **Deferred income tax expense/(credit) included in income tax comprises** | | |
| Decrease in deferred tax assets | **54** | 4 |
| Decrease in deferred tax liabilities | **(41)** | (4) |
| | **13** | - |
| **B. RECONCILIATION OF PRIMA FACIE TAX TO INCOME TAX EXPENSE** | | |
| Profit for the year before income tax | **1,334** | 920 |
| Income tax calculated at 30% (2016-30%) | **400** | 276 |
| **Amounts which are not deductible/(taxable) in calculating taxable income** | | |
| Difference in tax rate | **(32)** | 19 |
| Rebateable dividends | **(5)** | (8) |
| Interest on capital notes and convertible preference shares | **6** | 5 |
| Other | **(4)** | (1) |
| Income tax expense applicable to current year | **365** | 291 |
| Adjustment relating to prior year | **(36)** | (73) |
| Income tax expense attributable to profit for the year after impact of tax consolidation | **329** | 218 |
| **C. DEFERRED TAX ASSETS** | | |
| **I. Composition** | | |
| a. AMOUNTS RECOGNISED IN PROFIT | | |
| Property and equipment | **88** | 119 |
| Employee benefits | **85** | 83 |
| Insurance provisions | **119** | 118 |
| Investments | **31** | 47 |
| Provisions | **4** | 17 |
| Tax losses | **433** | 447 |
| Other | **-** | 7 |
| | **760** | 838 |
| b. AMOUNTS RECOGNISED DIRECTLY IN OTHER COMPREHENSIVE INCOME | | |
| Defined benefit superannuation plans | **12** | 23 |
| | **772** | 861 |
| c. AMOUNTS SET-OFF AGAINST DEFERRED TAX LIABILITIES | **(227)** | (258) |
| | **545** | 603 |
| **II. Reconciliation of movements** | | |
| Balance at the beginning of the financial year | **861** | 782 |
| Charged to profit or loss | **(54)** | (4) |
| (Charged)/credited to equity | **(11)** | 14 |
| Adjustments relating to prior year | **(23)** | 35 |
| Foreign exchange differences | **(1)** | 34 |
| Balance at the end of the financial year prior to set-off | **772** | 861 |

**III. Tax losses**

The deferred tax assets on tax losses primarily relates to those incurred in IAG's New Zealand business as a result of the Christchurch earthquake events that occurred in 2010 and 2011 and the 2016 Kaikoura earthquake. Subsequent revisions to the associated ultimate expected losses relating to the Christchurch events have offset the strong underlying performance of IAG's New Zealand business since the 2011 financial year. In the context of the New Zealand Income Tax Act, tax losses carried forward do not expire after a particular period and remain available to offset against future income tax liabilities, provided the 49% continuity of shareholding requirement is met at the listed holding company level.

| | **2017** | 2016 |
|---|---|---|
| | **$m** | $m |
| **D. DEFERRED TAX LIABILITIES** | | |
| **I. Composition** | | |
| a. AMOUNTS RECOGNISED IN PROFIT | | |
| Investments | **80** | 90 |
| Intangible assets | **26** | 34 |
| Other | **114** | 129 |
| | **220** | 253 |
| b. AMOUNTS RECOGNISED DIRECTLY IN OTHER COMPREHENSIVE INCOME | | |
| Hedges | **7** | 5 |
| | **227** | 258 |
| c. AMOUNTS SET-OFF AGAINST DEFERRED TAX ASSETS | **(227)** | (258) |
| | **-** | - |
| **II. Reconciliation of movements** | | |
| Balance at the beginning of the financial year | **258** | 283 |
| Credited to profit or loss | **(41)** | (4) |
| Charged/(credited) to equity | **2** | (22) |
| Acquisitions of subsidiaries | **-** | 1 |
| Adjustments relating to prior year | **8** | - |
| Balance at the end of the financial year prior to set-off | **227** | 258 |

**E. RECOGNITION AND MEASUREMENT**

**I. Income tax**

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

**II. Current tax**

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

**III. Deferred tax**

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

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

- temporary differences if they arose in a transaction, other than a business combination, that at the time of the transaction did not affect either accounting profit or taxable profit or loss;
- temporary differences between the carrying amount and tax bases of investments in subsidiaries where it is probable that the differences will not reverse in the foreseeable future; and
- temporary differences relating to the initial recognition of goodwill.

**IV. Tax consolidation**

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

## NOTE 5.3 PROVISIONS

| | 2017 | 2016 |
|---|---|---|
| | $m | $m |
| **A. EMPLOYEE BENEFITS** | | |
| **I. Expense recognised in the consolidated statement of comprehensive income** | | |
| Defined contribution superannuation plans | **111** | 122 |
| Defined benefit superannuation plans | **1** | 8 |
| Share based remuneration | **25** | 29 |
| Salaries and other employee benefits expense | **1,487** | 1,530 |
| | **1,624** | 1,689 |
| **II. Provision recognised on the consolidated balance sheet** | | |
| Annual leave | **92** | 97 |
| Long service leave | **91** | 90 |
| Cash based incentive arrangements | **98** | 88 |
| Defined benefit superannuation plans | **18** | 61 |
| Other employee benefits | **7** | 8 |
| | **306** | 344 |

The employee benefits provision includes $76 million (2016-$122 million) which is expected to be settled after more than 12 months from reporting date.

| | 2017 | 2016 |
|---|---|---|
| | $m | $m |
| **B. RESTRUCTURING PROVISION** | | |
| Balance at the beginning of the financial year | **26** | 59 |
| Additions | **25** | 25 |
| Amounts settled | **(28)** | (58) |
| Balance at the end of the financial year | **23** | 26 |

The provision primarily comprises redundancy costs in respect of IAG's prospective withdrawal from the NSW workers' compensation scheme. All provision outstanding at the reporting date is expected to be settled within 12 months (2016–all).

### C. RECOGNITION AND MEASUREMENT

#### I. Annual leave

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

#### II. Long service leave

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

#### III. Short term incentive plan

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

#### IV. Superannuation

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

#### V. Restructuring provision

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

# 6. GROUP STRUCTURE

## SECTION INTRODUCTION

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

## NOTE 6.1 DETAILS OF SUBSIDIARIES

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

| | COUNTRY OF INCORPORATION/ FORMATION | EXTENT OF BENEFICIAL INTEREST IF NOT 100% | |
|---|---|---|---|
| | | **2017** | 2016 |
| | | **%** | % |
| **A. ULTIMATE PARENT** | | | |
| Insurance Australia Group Limited | Australia | | |
| **B. SUBSIDIARIES** | | | |
| **I. Australian general insurance operations** | | | |
| CGU Insurance Limited[a] | Australia | | |
| CGU-VACC Insurance Limited[a] | Australia | | |
| HBF Insurance Pty Ltd[a] | Australia | | |
| IAG Re Australia Limited[a] | Australia | | |
| Insurance Australia Limited | Australia | | |
| Insurance Manufacturers of Australia Pty Limited | Australia | **70.00** | 70.00 |
| Mutual Community General Insurance Proprietary Limited[a] | Australia | | |
| Swann Insurance (Aust) Pty Ltd[a] | Australia | | |
| WFI Insurance Limited[a] | Australia | | |
| **II. New Zealand general insurance operations** | | | |
| AMI Insurance Limited | New Zealand | | |
| IAG New Zealand Limited | New Zealand | | |
| Lumley General Insurance (NZ) Limited | New Zealand | | |
| **III. International insurance operations** | | | |
| AAA Assurance Corporation | Vietnam | **63.17** | 63.17 |
| IAG Re Labuan (L) Berhad | Malaysia | | |
| IAG Re Singapore Pte Ltd | Singapore | | |
| PT Asuransi Parolamas | Indonesia | **80.00** | 80.00 |
| Safety Insurance Public Company Limited | Thailand | **98.61** | 98.61 |
| **IV. Corporate operations** | | | |
| IAG Finance (New Zealand) Limited | Australia | | |

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

## NOTE 6.2 NON-CONTROLLING INTERESTS

### A. SUMMARISED FINANCIAL INFORMATION

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

| | INSURANCE MANUFACTURERS OF AUSTRALIA PTY LIMITED | |
|---|---|---|
| | **2017** | 2016 |
| | **$m** | $m |
| **I. Summarised statement of comprehensive income** | | |
| Net premium revenue | **2,935** | 2,806 |
| Profit after tax attributable to IAG shareholders | **179** | 181 |
| Profit after tax attributable to non-controlling interest | **77** | 78 |
| Other comprehensive income | **3** | (3) |
| Total comprehensive income | **259** | 256 |
| **II. Summarised balance sheet** | | |
| Total assets | **3,791** | 3,601 |
| Total liabilities | **(3,039)** | (2,876) |
| Net assets | **752** | 725 |
| Carrying amount of non-controlling interest | **226** | 218 |
| **III. Summarised cash flow** | | |
| Net cash flows from operating and investing activities | **217** | 247 |
| Dividends paid to other Group entities | **(163)** | (128) |
| Dividends paid to non-controlling interest | **(68)** | (56) |
| Total net cash flows | **(14)** | 63 |

## NOTE 6.3 INVESTMENT IN JOINT VENTURE AND ASSOCIATES

### A. INTERESTS IN JOINT VENTURE AND ASSOCIATES

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

| | COUNTRY OF INCORPORATION/ FORMATION | PRINCIPAL ACTIVITY | CARRYING VALUE | | OWNERSHIP INTEREST | |
|---|---|---|---|---|---|---|
| | | | **2017** | 2016 | **2017** | 2016 |
| | | | **$m** | $m | **%** | % |
| AmGeneral Holdings Berhad (AmGeneral) | Malaysia | Insurance underwriting | **353** | 360 | **49.00** | 49.00 |
| SBI General Insurance Company Limited (SBI General) | India | Insurance underwriting | **138** | 111 | **26.00** | 26.00 |
| Other | | | **14** | 15 | | |
| | | | **505** | 486 | | |

The Malaysian general insurance industry has historically operated under a tariff structure for Motor and Fire insurance products. The operating landscape is expected to evolve with regulatory-driven liberalisation over the next few years, beginning with the phased implementation of detariffication of motor insurance from 1 July 2017. Whilst AmGeneral is well prepared for the tariff reform, this uncertainty presents additional risk to the business.

**B. SUMMARISED FINANCIAL INFORMATION**
Summarised financial information of material associates is provided below. The summarised financial information represents the financial position and performance of the entities as a whole (100% stand-alone basis) and not just IAG's share. The financial statements below are for the year ended 31 March 2017.

| | **2017** | | 2016 | |
|---|---|---|---|---|
| | **AmGeneral Holdings Berhad $m** | **SBI General Insurance Company Limited $m** | AmGeneral Holdings Berhad $m | SBI General Insurance Company Limited $m |
| **I. Summarised statement of comprehensive income** | | | | |
| Revenue | **543** | **580** | 573 | 483 |
| Profit/(loss) after tax | **53** | **30** | 59 | (25) |
| Other comprehensive income | **1** | **-** | - | - |
| Total comprehensive income | **54** | **30** | 59 | (25) |
| Dividends received from associate | **-** | **-** | 23 | - |
| **II. Summarised balance sheet** | | | | |
| Total assets | **1,643** | **957** | 1,849 | 713 |
| Total liabilities | **(1,024)** | **(736)** | (1,206) | (572) |
| Net assets as at reporting date | **619** | **221** | 643 | 141 |
| Group's ownership interest | **303** | **58** | 315 | 37 |
| Other adjustments* | **50** | **80** | 45 | 74 |
| Carrying value as at 30 June | **353** | **138** | 360 | 111 |

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

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

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

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

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

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

## NOTE 6.4 PARENT ENTITY DISCLOSURES

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

| | PARENT | |
|---|---|---|
| | **2017** | 2016 |
| | **$m** | $m |
| **A. FINANCIAL RESULTS** | | |
| Profit for the year | **467** | 439 |
| Total comprehensive income for the year, net of tax | **467** | 439 |
| **B. FINANCIAL POSITION** | | |
| Current assets | **16** | 287 |
| Total assets | **12,221** | 13,704 |
| Current liabilities | **171** | 28 |
| Total liabilities | **3,619** | 4,630 |
| **C. SHAREHOLDERS' EQUITY** | | |
| Share capital | **7,082** | 7,275 |
| Retained earnings | **1,520** | 1,799 |
| Total shareholders' equity | **8,602** | 9,074 |

**D. CONTINGENT LIABILITIES**

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

**Recognition and measurement**

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

**E. COMMITMENTS**

The Parent has no material commitments.

# 7. UNRECOGNISED ITEMS

### SECTION INTRODUCTION

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

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

## NOTE 7.1 CONTINGENCIES

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

The Consolidated entity conducts fiduciary activities in the form of investment management as it operates as manager, custodian or trustee for a number of investments and trusts. The funds managed on behalf of third parties which are not included in the Consolidated entity's balance sheet had a fair value as at the reporting date of $335 million (2016-$289 million).

## NOTE 7.2 COMMITMENTS

| | 2017 $m | 2016 $m |
|---|---|---|
| **A. OPERATING LEASE COMMITMENTS** | | |
| **I. Property** | | |
| Due within 1 year | **120** | 128 |
| Due within 1 to 2 years | **104** | 107 |
| Due within 2 to 5 years | **257** | 254 |
| Due after 5 years | **642** | 519 |
| | **1,123** | 1,008 |
| **II. Equipment** | | |
| Due within 1 year | **31** | 20 |
| Due within 1 to 2 years | **22** | 21 |
| Due within 2 to 5 years | **6** | 22 |
| | **59** | 63 |
| | **1,182** | 1,071 |

### B. RECOGNITION AND MEASUREMENT

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

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

## NOTE 7.3 EVENTS SUBSEQUENT TO REPORTING DATE

As the following events occurred after reporting date and did not relate to conditions existing at reporting date, no account has been taken of them in the financial statements for the current reporting year ended 30 June 2017. These include:

- Effective 19 July 2017, IAG announced the creation of a single Australian division to be led by Mark Milliner as CEO Australia. The Australian division simplifies IAG's operating model by bringing together the former Australian Consumer, Australian Business, Operations and Satellite divisions. There has been no change to the reportable segments in the current financial year as financial information was prepared and reviewed by the chief operating decision maker based on the pre-existing segment structure for Australia.
- On 1 August 2017, IAG consolidated its nine Australian Insurance licences into two licences following Federal Court approval received in July 2017. The consolidation transferred the insurance assets and liabilities of seven entities into a related entity, Insurance Australia Limited, with no impact to the Group's consolidated financial performance or position. Following the transfer, IAG retains two authorised insurers in Australia being Insurance Australia Limited and Insurance Manufacturers of Australia Pty Limited. The transfer is part of IAG's focus on becoming a simpler, more efficient and agile business.
- On 23 August 2017, the Board determined to pay a final dividend of 20 cents per share, 100% franked. The dividend will be paid on 9 October 2017. The dividend reinvestment plan will operate by acquiring shares on market for participants with no discount applied.

# 8. ADDITIONAL DISCLOSURES

**SECTION INTRODUCTION**

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

## NOTE 8.1 NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT

| | 2017 $m | 2016 $m |
|---|---|---|
| **A. COMPOSITION OF CASH AND CASH EQUIVALENTS** | | |
| Cash held for operational purposes | **424** | 263 |
| Cash and short term money held in investments | **1,056** | 841 |
| Cash and cash equivalents | **1,480** | 1,104 |
| **B. RECONCILIATION OF PROFIT FOR THE YEAR TO NET CASH FLOWS FROM OPERATING ACTIVITIES** | | |
| Profit for the year | **1,005** | 702 |
| **I. Non-cash items** | | |
| Net gains on investments | **(76)** | (89) |
| Amortisation and impairment of intangible assets and goodwill | **111** | 332 |
| Depreciation of property and equipment | **52** | 62 |
| Other non-cash items | **11** | (76) |
| **II. Movement in operating assets and liabilities** | | |
| Insurance assets | **(577)** | (994) |
| Insurance liabilities | **(411)** | (1,470) |
| Net movement in other operating assets and liabilities | **352** | (137) |
| Net movement in tax assets and liabilities | **210** | (263) |
| Provisions | **(41)** | (13) |
| Net cash flows from operating activities | **636** | (1,946) |

**C. SIGNIFICANT NON-CASH TRANSACTIONS RELATING TO FINANCING AND INVESTING TRANSACTIONS**

There were no financing or investing transactions during the year which have had a material effect on the assets and liabilities that did not involve cash flows.

**D. RECOGNITION AND MEASUREMENT**

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

## NOTE 8.2 RELATED PARTY DISCLOSURES

**A. KEY MANAGEMENT PERSONNEL**

**I. Details of compensation**

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

| | 2017 $000 | 2016 $000 |
|---|---|---|
| Short term employee benefits | **19,074** | 20,012 |
| Post-employment benefits | **533** | 499 |
| Other long term benefits | **145** | 53 |
| Termination benefits | **600** | 3,736 |
| Share based payments | **8,974** | 19,082 |
| | **29,326** | 43,382 |

**II. Other benefits**

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

## NOTE 8.3 REMUNERATION OF AUDITORS

| | 2017 $000 | 2016 $000 |
|---|---|---|
| **A. KPMG** | | |
| Audit of the financial statements prepared for the Parent and subsidiaries | **8,098** | 7,853 |
| Audit of statutory returns in accordance with regulatory requirements | **1,059** | 1,047 |
| Other assurance services | **126** | 151 |
| Advisory services | **1,233** | 1,369 |
| | **10,516** | 10,420 |
| **B. OTHER AUDITORS** | | |
| Audit of the financial statements prepared for subsidiaries | **-** | 26 |
| Total remuneration of auditors | **10,516** | 10,446 |

## NOTE 8.4 NET TANGIBLE ASSETS

| | 2017 $ | 2016 $ |
|---|---|---|
| Net tangible assets per ordinary share | **1.36** | 1.30 |

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

## NOTE 8.5 IMPACT OF NEW AUSTRALIAN ACCOUNTING STANDARDS ISSUED

### A. ISSUED AND EFFECTIVE

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

| TITLE | DESCRIPTION |
|---|---|
| AASB 1057 | Application of Australian Accounting Standards |
| AASB 2014-3 | Amendments to Australian Accounting Standards - Accounting for Acquisitions of Interests in Joint Operations |
| AASB 2014-4 | Amendments to Australian Accounting Standards - Clarification of Acceptable Methods of Depreciation and Amortisation |
| AASB 2014-9 | Amendments to Australian Accounting Standards - Equity Method in Separate Financial Statements |
| AASB 2015-1 | Amendments to Australian Accounting Standards - Annual Improvements to Australian Accounting Standards 2012-2014 Cycle |
| AASB 2015-2 | Amendments to Australian Accounting Standards - Disclosure Initiative: Amendments to AASB 101 |
| AASB 2015-9 | Amendments to Australian Accounting Standards - Scope and Application Paragraphs |

### B. ISSUED BUT NOT YET EFFECTIVE

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

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

| TITLE | DESCRIPTION | OPERATIVE DATE | NOTE |
|---|---|---|---|
| AASB 9 | Financial Instruments | 1 January 2018 | A |
| AASB 15 | Revenue from Contracts with Customers | 1 January 2018 | A |
| AASB 16 | Leases | 1 January 2019 | A |
| AASB 17 | Insurance Contracts | 1 January 2021 | B |
| AASB 2010-7 | Amendments to Australian Accounting Standards arising from AASB 9 | 1 January 2018 | A |
| AASB 2014-1 (Part E) | Amendments to Australian Accounting Standards – Financial Instruments | 1 January 2018 | A |
| AASB 2014-7 | Amendments to Australian Accounting Standards arising from AASB 9 (December 2014) | 1 January 2018 | A |
| AASB 2014-10 | Amendments to Australian Accounting Standards – Sale or Contribution of Assets between an Investor and its Associate or Joint Venture | 1 January 2018 | A |
| AASB 2015-8 | Amendments to Australian Accounting Standards – Effective Date of AASB 15 | 1 January 2018 | A |
| AASB 2015-10 | Amendments to Australian Accounting Standards – Effective Date of Amendments to AASB 10 and AASB 128 | 1 January 2018 | A |

| TITLE | DESCRIPTION | OPERATIVE DATE | NOTE |
|---|---|---|---|
| AASB 2016-1 | Amendments to Australian Accounting Standards – Recognition of Deferred Tax Assets for Unrealised Losses | 1 January 2017 | A |
| AASB 2016-2 | Amendments to Australian Accounting Standards – Disclosure Initiative: Amendments to AASB 107 | 1 January 2017 | A |
| AASB 2016-3 | Amendments to Australian Accounting Standards – Clarifications to AASB 15 | 1 January 2018 | A |
| AASB 2016-5 | Amendments to Australian Accounting Standards – Classification and Measurement of Share based Payment Transactions | 1 January 2018 | B |
| AASB 2016-6 | Amendments to Australian Accounting Standards – Applying AASB 9 Financial Instruments with AASB 4 Insurance Contracts | 1 January 2018 | A |
| IFRIC Interpretation 22 | Foreign Currency Transactions and Advance Consideration | 1 January 2018 | B |

TABLE NOTE

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

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

The Australian Accounting Standards and amendments detailed in the table above are not mandatory for the Group until the operative dates stated, however, early adoption is permitted. The Group currently plans to apply the standards and amendments detailed above for the reporting periods beginning on or after the operative dates set out above, except for AASB 9 as detailed below. An initial assessment of the financial impact of the standards and amendments has been undertaken and they are not expected to have a material impact on the Group's financial statements.

AASB 9 was issued during 2014 and will replace existing accounting requirements for financial instruments. Currently, the Group's investments are designated as at fair value through profit or loss on initial recognition and are subsequently remeasured to fair value at each reporting date, reflecting the business model applied by the Group to manage and evaluate its investment portfolio. Under this business model, the adoption of AASB 9 is not expected to result in significant changes to accounting for investments. Other changes to the accounting for the Group's financial instruments arising from the application of AASB 9 are expected to be minimal. The Group plans to defer the adoption of AASB 9 to align with the implementation of AASB 17 Insurance Contracts (effective 1 January 2021), which is permissible under the standard.

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

AASB 16 was issued during 2016 and will replace existing accounting requirements for leases. Under current requirements, leases are classified based on their nature as either finance leases, which are recognised on the balance sheet, or operating leases, which are not recognised on the balance sheet. The application of AASB 16 will result in the recognition of all leases on the balance sheet in the form of a right-of-use asset and a corresponding lease liability, except for leases of low value assets and leases with a term of 12 months or less. As a result, the new standard is expected to impact leases which are currently classified by the Group as operating leases, primarily, leases over premises and equipment. Based on preliminary assessments, the resulting amount to be recognised, in effect as a gross up to the balance sheet, is expected to be approximately $780 million.

AASB 17 Insurance Contracts was released on 18 May 2017, with an expected effective date of 1 January 2021. The implementation date for IAG will be for the year ending 30 June 2022, with the comparative period the year ended 30 June 2021. A detailed impact assessment is currently underway.

# DIRECTORS' DECLARATION

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

- the financial statements and notes 1 to 8.5, including all the remuneration disclosures that are contained in the Remuneration Report of the Directors' Report, are in accordance with the Corporations Act 2001 including:
  - giving a true and fair view of the financial position of the Company and Consolidated entity as at 30 June 2017 and of their performance, as represented by the results of their operations and their cash flows, for the year ended on that date;
  - complying with Australian Accounting Standards and the Corporations Regulations 2001; and
  - the financial report also complies with International Financial Reporting Standards as disclosed in Note 1.2.B; and
- the Remuneration Report of the Directors' Report complies with the Corporations Act 2001 and Australian Accounting Standards; and
- there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.

The Directors have been given the declaration required by section 295A of the Corporations Act 2001 from the Chief Executive Officer and the Chief Financial Officer for the financial year ended 30 June 2017.

Signed at Sydney this 23rd day of August 2017 in accordance with a resolution of the Directors.

**Peter Harmer**
Director

# INDEPENDENT AUDITOR'S REPORT

## TO THE SHAREHOLDERS OF INSURANCE AUSTRALIA GROUP LIMITED

### REPORT ON THE AUDIT OF THE FINANCIAL REPORT

**Opinion**

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

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

- giving a true and fair view of the Group's financial position as at 30 June 2017 and of its financial performance for the year ended on that date; and
- complying with *Australian Accounting Standards* and the *Corporations Regulations 2001*.

The Financial Report comprises:

- Consolidated balance sheet as at 30 June 2017;
- Consolidated statement of comprehensive income, Consolidated statement of changes in equity, and Consolidated cash flow statement for the year then ended;
- Notes including a summary of significant accounting policies; and
- Directors' declaration.

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

**Basis for opinion**

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

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

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

**Key Audit Matters**

The Key Audit Matters we identified are:

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

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

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

**Valuation of Gross outstanding claims liability ($11,371 million)**

Refer to Note 2.2 of the Financial Report

**The key audit matter**

Gross outstanding claims liability is a key audit matter as a result of significant complexity relating to:

***Valuation of gross outstanding claims liability***

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

- judgement is required by us to consider the central estimate of the gross outstanding claims liability which is a significant estimate as the eventual outcomes of incurred but unsettled claims at the balance sheet date are inherently uncertain;
- there is a lower level of information available and a greater level of uncertainty inherent in assessing estimations of claims that have been incurred by the balance sheet date but have not yet been reported to the Group, including where there has been a recent natural catastrophe, such as the Kaikoura earthquake in November 2016 and Cyclone Debbie in late March 2017;
- judgement is required when considering the application of historical experience of claims development to determine current estimates, including the greater variability between the original estimation and the ultimate settlement of claims where there is a long time delay between the claim being incurred and the ultimate settlement. Examples include claims arising from Workers' Compensation, Liability, Compulsory Third Party (CTP) and the main Canterbury earthquakes of September 2010 and February 2011;
- the claims estimation uses an actuarial modelling process which involves complex and subjective actuarial methodologies, judgements and assumptions about future events and developments, both within and external to the Group, and for which small changes can have significant implications to the quantification, as outlined in Note 2.2(E);
- the Canterbury earthquake claims require judgement and technical actuarial expertise to evaluate the attribution of claims costs between the September 2010 and the February 2011 Canterbury earthquake events;
- judgement is required to assess the estimation of the periods the claims are expected to be settled in;
- the estimation of claims at year end relies on the integrity of the underlying data, including claim payments and individual estimates of unsettled claims, which is gathered from many different systems; and
- we involve senior resources, with deep industry experience, together with our actuarial specialists in evaluating the Group's estimations of outstanding claims.

**How the matter was addressed in our audit**

Our procedures included:

***Valuation of gross outstanding claims liability***

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

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

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

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

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

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

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

- using our IT specialists, we tested the general IT environment as well as tested the reconciliations between data on the claims systems (underlying data) and data used in the actuarial modelling processes by evaluating the Group's automated comparison programs which they apply to assess the consistency of the data.

| | |
|---|---|
| ***Risk margins and Probability of Adequacy*** | ***Risk margins and Probability of Adequacy*** |
| The evaluation of the risk margins and Probability of Adequacy is significant to the Key Audit Matter as it is complex and necessitated a significant level of judgement by us in our audit.<br><br>Outstanding claims include statistically determined risk margins developed by the Group to make allowance for the inherent uncertainty in estimating ultimate claim settlements. The risk margins are included to achieve a specified Probability of Adequacy for the total outstanding claims reserves.<br><br>We involved senior resources and our actuarial specialists to focus on the complex statistical processes and parameters used by the Group to establish the risk margins. | With the assistance of our actuarial specialists we evaluated the appropriateness of the statistical processes to establish the Group's risk margins. In particular, our procedures included:<br>- assessing the statistical processes' suitability by critically studying these and comparing them to known industry practices, our industry knowledge and other observable trends in industry discussion forums and Actuaries Institute papers;<br>- assessing the risk margin parameters for significant portfolios by comparing these with external sources of data including published statistics (e.g. APRA-published data), prior periods and our industry knowledge;<br>- checking the central estimates of outstanding claims, that were tested in the valuation of gross outstanding claims liability processes, and which are a key input into the risk margin model, to the underlying financial records; and<br>- critically evaluating the Group's judgement in the execution of the statistical processes by comparing the judgements and overall results to our expectations based on the Group's historical experience, our industry knowledge and independent observable trends (e.g. listed competitors). |

**Valuation of Reinsurance and other recoveries on outstanding claims ($5,258 million)**

Refer to Note 2.2 of the Financial Report

| The key audit matter | How the matter was addressed in our audit |
|---|---|
| Reinsurance and other recoveries on outstanding claims is a Key Audit Matter as:<br>- reinsurance and other recoveries, similar to the valuation of gross outstanding claims, are quantified from claims case estimates, paid claims data and estimates of ultimate claims settlement amounts. As such, the rationale for identifying it as a key audit matter is the same as that highlighted for valuation of gross outstanding claims;<br>- the Group has extensive reinsurance arrangements designed to protect its aggregate exposure to catastrophic claim events. Evaluating the reinsurance transactions accounting across the three reinsurance captive companies, and in the respective insurance companies within the Group requires significant consideration by our senior resources with deep industry knowledge and specialised technical skills; and<br>- the Group also has a range of significant reinsurance contracts, including the Whole of Account Quota Share, the Catastrophe excess of loss program, Adverse Development Covers in the form of excess of loss contracts, and other Quota Share arrangements, that form part of its capital management. Our consideration of the accounting treatment and recoverability of balances owed by the reinsurer counterparties requires our senior resources, deep industry experience and specialised technical skills. | In addition to the audit procedures undertaken to assess the valuation of gross outstanding claims liability, our procedures included:<br>- testing, for a sample of contracts, how the reinsurance and other recoveries on outstanding claims were accounted for, including their processing through the Group's captive reinsurance companies. We referred to the terms of the captive reinsurance contracts, board meeting minutes, our expectations based on the Group's past experience, our industry knowledge, and the insurance accounting standard;<br>- independently evaluating a sample of reinsurance balances and other recoveries due to the Group arising from the Whole of Account Quota Share contract. We referred to the terms of the reinsurance contract, and applied it to the original underlying claims estimates and paid claims data to recalculate the reinsurance and other recoveries due. These independently generated results were compared to the amounts processed by the Group;<br>- evaluating a sample of the transactions processed relating to the reinsurance contracts. We tested the consistency of the contract terms to the criteria for the recognition of the transaction contained in those requirements; and<br>- assessing the recoverability of balances owed by reinsurer counterparties by considering their credit worthiness and capital strength, based on external sources of information, payment history of amounts and evaluation of information for indicators of disputes. |

**Valuation of Goodwill ($2,974 million) and Investment in joint venture and associates ($505 million)**

Refer to Notes 5.1 and 6.3 of the Financial Report

| The key audit matter | How the matter was addressed in our audit |
|---|---|
| Valuation of goodwill and investment in joint venture and associates is a Key Audit Matter as:<br>▪ judgement is involved in considering the appropriateness of the cash generating units identified by the Group;<br>▪ the evaluation of potential impairment involves judgement in relation to forecast cash flows and key variables. Instances where judgement is required include interest rates, risk premium, growth rates, profit measures and terminal growth rates. We focused specifically on those cash generating units and associates where the valuation showed potential impairment indicators, or where there was a significant reduction in the valuation in the period;<br>▪ the assessment of the valuation of goodwill, and investment in joint venture and associates, requires the involvement of senior resources from the audit team together with our valuation specialists; and<br>▪ the Group uses complex models to perform their annual testing of goodwill for impairment. The models are largely internally developed, use adjusted historical performance, and a range of internal and external sources as inputs to the assumptions. Complex modelling, particularly those containing highly judgemental allocations of corporate assets and costs to cash generating units, using forward-looking assumptions tend to be prone to greater risk for potential bias, error and inconsistent application. These conditions necessitate additional scrutiny by us, in particular to address the objectivity of sources used for assumptions, and their consistent application. | With the assistance of our valuation specialists, our procedures included:<br>▪ evaluating the Group's determination of their cash generating units based on our understanding of the industries in which the Group operates, and our knowledge of the business, including internal management reporting, against the accounting standard requirements;<br>▪ performing sensitivity testing, using the Group's models, to evaluate the impact of varying key assumptions. This enabled us to critically challenge the Group's quantification of assumptions and focus our testing to the most sensitive assumptions;<br>▪ assessing the Group's quantification of key variables by comparing them to external, observable metrics (e.g. GDP growth and inflation incl. forecasts provided by Oxford Economics and IBIS World), our knowledge of the markets, and current market practice;<br>▪ comparing the forecast cash flows to Board approved budgets and business plans, and performing an examination of the accuracy of past budgets to actual cash flows in order to challenge the Group's current forecasts;<br>▪ comparing the valuations for certain joint venture and associates to external, independent and observable valuations for broadly similar enterprises, and investigate significant outliers;<br>▪ assessing the Group's allocation of corporate assets to cash generating units for consistency based on the requirements of the accounting standards;<br>▪ assessing the Group's allocation of corporate costs to the forecasted cash flows contained in the value in use model, based on a reasonable and consistent basis using our understanding of the business; and<br>▪ involving our specialists, we evaluated the internally prepared discounted cash flow model. This included:<br>– assessing the reasonableness of the valuation approach and methodology against market and industry practices and accounting standards; and<br>– assessing the integrity of the models used, including the accuracy of the underlying calculation formulas.<br><br>Using our IT specialists, we tested the general IT environment as well as specific system controls in relation to the underlying data used in the valuation models to assess the consistency of the data. |

**Other Information**

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

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

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

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

**Responsibilities of the Directors for the Financial Report**

The Directors are responsible for:

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

**Auditor's responsibilities for the audit of the Financial Report**

Our objective is:

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

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

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

A further description of our responsibilities for the Audit of the Financial Report is located at the Auditing and Assurance Standards Board website at www.auasb.gov.au/auditors_files/ar2.pdf. This description forms part of our Auditor's Report.

**REPORT ON THE REMUNERATION REPORT**

**Opinion**

In our opinion, the Remuneration Report of Insurance Australia Group Limited for the year ended 30 June 2017, complies with *Section 300A* of the *Corporations Act 2001*.

**Directors' responsibilities**

The Directors of the Company are responsible for the preparation and presentation of the Remuneration Report in accordance with *Section 300A* of the *Corporations Act 2001*.

**Our responsibilities**

We have audited the Remuneration Report included in pages 16 to 37 of the Directors' report for the year ended 30 June 2017.

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

KPMG

**KPMG**

**Andrew Yates**
Partner

Sydney
23 August 2017

**Ian Moyser**
Partner

# SHAREHOLDER INFORMATION

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

## ASX CODES

Insurance Australia Group Limited's shares are listed on the ASX under IAG (ordinary shares).

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

## ANNUAL REPORT

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

## ANNUAL GENERAL MEETING

The 2017 annual general meeting (AGM) of Insurance Australia Group Limited will be held on 20 October 2017 commencing at 10am at Wesley Conference Centre, 220 Pitt Street, Sydney, NSW 2000. The AGM will be webcast live on the internet at www.iag.com.au/shareholder-centre/annual-meetings and an archive version will be placed on the website to enable the AGM to be viewed at a later time.

## ONLINE VOTING

Shareholders can lodge voting instructions electronically either as a direct vote or by appointing a proxy for the 2017 AGM at www.iag.com.au. The information required to log on and use online voting is shown on your voting form.

## SHAREHOLDER QUESTIONS

If you would like to submit a written question to the Company or the Company's auditor with regard to the AGM or any of the resolutions to be discussed, please use the form supplied and return it with your completed Voting Form in the pre-addressed envelope provided or by fax to +61 (0)3 9473 2555. Please note your questions for the auditor must be received by 5pm on 13 October 2017.

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

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

## DIVIDEND PAYMENT METHODS

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

**IAG ordinary shares**

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

## MANAGE YOUR HOLDING

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

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

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

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

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

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

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

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

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

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

## EMAIL ALERT SERVICE

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

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

## EMAIL ENQUIRIES

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

## ORDINARY SHARES INFORMATION

| IMPORTANT DATES* | 2017 |
|---|---|
| IAG year end | 30 June |
| Full year results and dividend announced | 23 August |
| Annual report and notice of meeting mailout commences | 5 September |
| Record date for final dividend | 7 September |
| Final dividend paid | 9 October |
| Written questions for the auditor close (5pm) | 13 October |
| Proxy return close (10am) | 18 October |
| Annual general meeting (10am) | 20 October |
| IAG half year end | 31 December |

* Please note that some dates are subject to change.

| TWENTY LARGEST ORDINARY SHAREHOLDERS AS AT 18 JULY 2017 | NUMBER OF SHARES | % OF ISSUED CAPITAL |
|---|---|---|
| HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED | **591,416,570** | **24.98** |
| J P MORGAN NOMINEES AUSTRALIA LIMITED | **303,326,503** | **12.81** |
| CITICORP NOMINEES PTY LIMITED | **170,938,621** | **7.22** |
| NATIONAL INDEMNITY COMPANY | **89,766,607** | **3.79** |
| NATIONAL NOMINEES LIMITED | **73,858,127** | **3.12** |
| BNP PARIBAS NOMINEES PTY LTD <AGENCY LENDING DRP A/C> | **64,314,110** | **2.72** |
| BNP PARIBAS NOMS PTY LTD <DRP> | **36,261,130** | **1.53** |
| CITICORP NOMINEES PTY LIMITED <COLONIAL FIRST STATE INV A/C> | **35,362,620** | **1.49** |
| AMP LIFE LIMITED | **12,149,996** | **0.51** |
| NATIONAL NOMINEES LIMITED <N A/C> | **7,517,500** | **0.32** |
| HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED <NT-COMNWLTH SUPER CORP A/C> | **6,759,504** | **0.29** |
| ARGO INVESTMENTS LIMITED | **6,281,075** | **0.27** |
| MILTON CORPORATION LIMITED | **5,847,282** | **0.25** |
| IAG SHARE PLAN NOMINEE PTY LIMITED <IAG DAP UNALLOCATED ACCOUNT> | **5,022,679** | **0.21** |
| AUSTRALIAN FOUNDATION INVESTMENT COMPANY LIMITED | **4,129,215** | **0.17** |
| HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED-GSCO ECA | **4,128,913** | **0.17** |
| BKI INVESTMENT COMPANY LIMITED | **3,157,370** | **0.13** |
| RBC INVESTOR SERVICES AUSTRALIA NOMINEES PTY LTD <BKMINI A/C> | **2,919,890** | **0.12** |
| IOOF INVESTMENT MANAGEMENT LIMITED <IPS SUPER A/C> | **2,907,735** | **0.12** |
| RBC INVESTOR SERVICES AUSTRALIA NOMINEES PTY LTD <VFA A/C> | **2,661,931** | **0.11** |
| Total for top 20 | **1,428,727,378** | **60.33** |

| RANGE OF ORDINARY SHAREHOLDERS AS AT 18 JULY 2017 | NUMBER OF HOLDERS | NUMBER OF SHARES | % OF ISSUED CAPITAL |
|---|---|---|---|
| 1-1,000 | **408,161** | **217,581,959** | **9.19** |
| 1,001-5,000 | **268,988** | **490,707,549** | **20.73** |
| 5,001-10,000 | **13,148** | **90,233,703** | **3.81** |
| 10,001-100,000 | **4,560** | **88,680,188** | **3.75** |
| 100,001 and over | **125** | **1,480,320,945** | **62.52** |
| Total | **694,982** | **2,367,524,344** | **100.00** |
| Shareholders with less than a marketable parcel of 75 shares as at 18 July 2017 | **2,327** | **67,501** | |

**DIVIDEND DETAILS**

| SHARE CLASS | DIVIDEND | FRANKING | AMOUNT PER SHARE | DRP ISSUE PRICE | PAYMENT DATE |
|---|---|---|---|---|---|
| Ordinary | Interim | Fully franked | 13 cents | $6.1300 | 30 March 2017 |
| Ordinary | Final | Fully franked | 20 cents | * | 9 October 2017 |

* The DRP issue price for the final dividend is scheduled to be announced on 28 September 2017.

## SUBSTANTIAL SHAREHOLDINGS AS AT 18 JULY 2017

| SUBSTANTIAL SHAREHOLDERS AS AT 18 JULY 2017 | NUMBER OF SHARES | % OF ISSUED CAPITAL |
|---|---|---|
| BLACKROCK GROUP | **118,550,980** | **5.00** |

## IAGPD CAPITAL NOTES INFORMATION

| TWENTY LARGEST CONVERTIBLE PREFERENCE SHAREHOLDERS AS AT 18 JULY 2017 | NUMBER OF SHARES | % OF ISSUED CAPITAL |
|---|---|---|
| HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED | **449,700** | **11.13** |
| J P MORGAN NOMINEES AUSTRALIA LIMITED | **218,384** | **5.40** |
| NATIONAL NOMINEES LIMITED | **102,808** | **2.54** |
| IOOF INVESTMENT MANAGEMENT LIMITED <IPS SUPER A/C> | **92,279** | **2.28** |
| BNP PARIBAS NOMS PTY LTD <DRP> | **88,469** | **2.19** |
| HSBC CUSTODY NOMINEES (AUSTRALIA) LIMITED - A/C 2 | **74,514** | **1.84** |
| NAVIGATOR AUSTRALIA LTD <MLC INVESTMENT SETT A/C> | **51,346** | **1.27** |
| RBC INVESTOR SERVICES AUSTRALIA NOMINEES PTY LIMITED <BKCUST A/C> | **44,708** | **1.11** |
| BNP PARIBAS NOMINEES PTY LTD HUB24 CUSTODIAL SERV LTD DRP | **43,608** | **1.08** |
| NULIS NOMINEES (AUSTRALIA) LIMITED <NAVIGATOR MAST PLAN SETT A/C> | **40,302** | **1.00** |
| NAVIGATOR AUSTRALIA LTD <JB WERE LIST FIX INT SMA A/C> | **37,290** | **0.92** |
| SANDHURST TRUSTEES LTD <DMP ASSET MANAGEMENT A/C> | **35,393** | **0.88** |
| AUSTRALIAN EXECUTOR TRUSTEES LIMITED <NO 1 ACCOUNT> | **31,279** | **0.77** |
| THE WALTER AND ELIZA HALL INSTITUTE OF MEDICAL RESEARCH | **20,000** | **0.49** |
| IOOF INVESTMENT MANAGEMENT LIMITED <IPS IDPS A/C> | **17,085** | **0.42** |
| CITICORP NOMINEES PTY LIMITED | **16,800** | **0.42** |
| THE WYATT BENEVOLENT INSTITUTION INC | **15,517** | **0.38** |
| BT PORTFOLIO SERVICES LIMITED <THE AL'N'ALL A/C> | **13,788** | **0.34** |
| P A W PTY LTD <WEIR&HARRIS SUPER FUND A/C> | **13,500** | **0.33** |
| INVIA CUSTODIAN PTY LIMITED < RISF A/C> | **12,500** | **0.31** |
| Total for top 20 | **1,419,270** | **35.10** |

| RANGE OF CONVERTIBLE PREFERENCE SHAREHOLDERS AS AT 18 JULY 2017 | NUMBER OF HOLDERS | NUMBER OF SHARES | % OF ISSUED CAPITAL |
|---|---|---|---|
| 1-1,000 | **4,333** | **1,445,330** | **35.76** |
| 1,001-5,000 | **418** | **877,537** | **21.71** |
| 5,001-10,000 | **34** | **231,437** | **5.73** |
| 10,001-100,000 | **23** | **716,069** | **17.72** |
| 100,001 and over | **3** | **770,892** | **19.08** |
| Total | **4,811** | **4,041,265** | **100.00** |
| Capital note holders with less than a marketable parcel of 5 shares as at 18 July 2017 | **2** | **2** | |

# CORPORATE DIRECTORY

## SHARE REGISTRY

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

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

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

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

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

## REGISTERED OFFICE

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

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

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

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

# FIVE YEAR FINANCIAL SUMMARY

| | 2017 $m | 2016 $m | 2015 $m | 2014 $m | 2013 $m |
|---|---|---|---|---|---|
| Gross written premium | **11,805** | 11,367 | 11,440 | 9,779 | 9,498 |
| Gross earned premium | **11,692** | 11,411 | 11,525 | 9,721 | 9,135 |
| Outwards reinsurance premium expense | **(3,227)** | (3,183) | (1,196) | (1,077) | (817) |
| Net premium revenue | **8,465** | 8,228 | 10,329 | 8,644 | 8,318 |
| Net claims expense | **(5,263)** | (5,397) | (6,941) | (5,201) | (4,982) |
| Underwriting expenses | **(2,185)** | (2,116) | (2,847) | (2,303) | (2,178) |
| Underwriting profit[(a)] | **1,017** | 715 | 541 | 1,140 | 1,158 |
| Net investment income on assets backing insurance liabilities | **241** | 463 | 562 | 439 | 270 |
| Management reported insurance profit[(a)] | **1,258** | 1,178 | 1,103 | 1,579 | 1,428 |
| Net investment income from shareholders' funds | **249** | 97 | 223 | 396 | 347 |
| Other income | **182** | 204 | 187 | 199 | 175 |
| Share of net profit/(loss) of associates[(b)] | **19** | 17 | 6 | (8) | (29) |
| Finance costs | **(93)** | (99) | (107) | (98) | (95) |
| Corporate and administration expenses[(c)] | **(224)** | (423) | (383) | (255) | (208) |
| Amortisation expense and impairment charges of acquired intangible assets and goodwill | **(57)** | (54) | (80) | (11) | (25) |
| Profit before income tax | **1,334** | 920 | 949 | 1,802 | 1,593 |
| Income tax expense | **(329)** | (218) | (119) | (472) | (424) |
| Profit after tax from continuing operations | **1,005** | 702 | 830 | 1,330 | 1,169 |
| Loss after tax from discontinued operation | **-** | - | - | - | (287) |
| Net profit attributable to non-controlling interests | **(76)** | (77) | (102) | (97) | (106) |
| Net profit attributable to IAG shareholders | **929** | 625 | 728 | 1,233 | 776 |
| Ordinary shareholders' equity ($ million) | **6,562** | 6,563 | 6,817 | 6,568 | 4,786 |
| Total assets ($ million)[(d)] | **29,597** | 30,030 | 31,402 | 29,748 | 24,859 |
| **KEY RATIOS** | | | | | |
| Gross written premium growth | **3.9 %** | (0.6)% | 17.0 % | 3.0% | 11.8 % |
| Loss ratio[(e)] | **62.2 %** | 65.6 % | 67.2 % | 60.2 % | 59.9 % |
| Expense ratio[(f)] | **25.8 %** | 25.7 % | 27.6 % | 26.7 % | 26.2 % |
| Combined ratio[(g)] | **88.0 %** | 91.3 % | 94.8 % | 86.9 % | 86.1 % |
| Insurance margin[(h)] | **14.9 %** | 14.3 % | 10.7 % | 18.3 % | 17.2 % |
| **SHARE INFORMATION** | | | | | |
| Dividends per ordinary share - fully franked (cents) | **33.00** | 36.00 | 29.00 | 39.00 | 36.00 |
| Basic earnings per ordinary share (cents) | **39.03** | 25.79 | 31.22 | 56.09 | 37.57 |
| Diluted earnings per ordinary share (cents) | **37.72** | 25.34 | 30.45 | 53.62 | 36.44 |
| Ordinary share price at 30 June ($) (ASX: IAG) | **6.78** | 5.45 | 5.58 | 5.84 | 5.44 |
| Convertible preference share price at 30 June ($) (ASX: IAGPC) | **-** | 101.50 | 101.60 | 106.44 | 101.88 |
| Capital notes price at 30 June ($) (ASX: IAGPD) | **106.53** | - | - | - | - |
| Reset exchangeable securities price at 30 June ($) (ASX: IANG) | **103.40** | 100.00 | 103.10 | 107.00 | 102.80 |
| Issued ordinary shares (million) | **2,367** | 2,431 | 2,431 | 2,341 | 2,079 |
| Issued convertible preference shares (million) | **-** | 4 | 4 | 4 | 4 |
| Issued capital notes (million) | **4** | - | - | - | - |
| Market capitalisation (ordinary shares) at 30 June ($ million) | **16,048** | 13,249 | 13,565 | 13,671 | 11,310 |
| Net tangible asset backing per ordinary share ($)[(d)] | **1.36** | 1.30 | 1.34 | 1.27 | 1.38 |

(a) The amounts for 2016 financial year are presented on a management reported (non-IFRS) basis which is not directly comparable to the equivalent statutory (IFRS) figure. A reconciliation between the two is outlined in the Operating and Financial Review section of the Directors' Report.
(b) Share of net profit/(loss) of associates includes regional support and development costs.
(c) Includes a $198 million impairment of capitalised software for 2016 and a $60 million impairment of the investment in Bohai Insurance for 2015.
(d) The financial information for 2014 has been restated to reflect the fair value adjustments to the net assets acquired in respect of the former Wesfarmers business in 2014.
(e) The loss ratio refers to the net claims expense as a percentage of net premium revenue.
(f) The expense ratio refers to underwriting expenses as a percentage of net premium revenue.
(g) The combined ratio refers to the sum of the loss ratio and expense ratio.
(h) Insurance margin is a ratio of insurance profit over net premium revenue.

PEFC™
PEFC/21-31-119

Pacesetter Laser Recycled is 30% recycled and made
up from elemental chlorine free bleached pulp which
is PEFC™ certified sourced from sustainably managed
sources. It is manufactured by an ISO 14001 certified mill.

iag

## AUSTRALIA

NRMA Insurance, SGIO, SGIC, Swann Insurance

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

## NEW ZEALAND

State, NZI, AMI Insurance, Lumley

## VIETNAM

AAA Assurance[3]

## THAILAND

Safety Insurance[4] NZI[4]

## INDIA

SBI General Insurance[5]

## MALAYSIA

AmAssurance[6] Kurnia Insurans[6]

## INDONESIA

Asuransi Parolamas[7]

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

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

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

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

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

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

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

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

All ownership percentages are as at 30 June 2017.