

NOTES TO THE FINANCIAL STATEMENTS

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Insurance Australia Group Limited (IAG, Parent or Company) is a company limited by shares, incorporated and domiciled in Australia whose shares are 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 is for the current reporting period ended 30 June 2010 and includes separate financial statements for IAG as an individual entity and consolidated financial statements for the Company and its subsidiaries (IAG Group, Group or Consolidated entity).

This general purpose financial report was authorised by the board of directors for issue on 26 August 2010.

A. STATEMENT OF COMPLIANCE

This general purpose financial report has been prepared in accordance with the Corporations Act 2001, Australian Accounting Standards (AASBs) (including Australian Interpretations) adopted by the Australian Accounting Standards Board, other authoritative pronouncements of the Australian Accounting Standards Board and the ASX Listing Rules.

International Financial Reporting Standards (IFRS) refer to the overall framework of standards and pronouncements approved by the International Accounting Standards Board. IFRS forms the basis of the Australian Accounting Standards. This financial report of the Parent and the Consolidated entity complies with IFRS.

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

B. BASIS OF PREPARATION OF THE FINANCIAL REPORT

The significant accounting policies adopted in the preparation of this financial report are set out below. The accounting policies adopted in the preparation of this financial report have been applied consistently by the Parent and are the same as those applied for the previous reporting period unless otherwise noted. 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 for the Consolidated entity 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.

The presentation currency used for the preparation of this financial report is Australian dollars.

The balance sheet is prepared using the liquidity format in which the assets and liabilities are 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). For those assets and liabilities that comprise both current and non-current amounts, information regarding the amount of the item that is expected to be outstanding longer than 12 months is included within the relevant note to the financial statements.

I. Australian accounting standards 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 period.

None of these standards have been early adopted and applied in the current reporting period. These standards will be adopted in the year commencing 1 July after the operative date. For example, AASB 2009-5 will be operative in the financial year commencing 1 July 2010.

TITLE	DESCRIPTION	OPERATIVE DATE	NOTE
AASB 2009-5	Further amendments to Australian Accounting Standards arising from the annual improvement project	1 January 2010	A
AASB 9	Financial Instruments	1 January 2013	C
AASB 2009-11	Amendments to Australian Accounting Standards—Accounting Standards arising from AASB 9	1 January 2013	D
AASB 2009-12	Amendments to Australian Accounting Standards	1 January 2011	B
AASB 2009-13	Amendments to Australian Accounting Standards arising from Interpretation 19	1 July 2010	A
AASB 2010-3	Amendments to Australian Accounting Standards arising from the annual improvements project	1 July 2010	B
AASB 2010-4	Further amendments to Australian Accounting Standards arising from the annual improvement project	1 January 2011	B

TABLE NOTES

- A These changes are not expected to have a significant, if any, financial impact.
- B These changes will only impact disclosures when preparing the annual financial report.
- C These changes may have financial impact. However, the assessment of the impact is not completed yet and the impact cannot be reasonably estimated.
- D This standard gives effect to consequential changes arising from the issuance of AASB 9. This standard is required to be adopted in the same reporting period when AASB 9 is adopted.

II. Changes in accounting policies

There were a number of Australian Accounting Standards and Interpretations, applicable for the current reporting period. Adopting some of these standards and interpretations resulted in changes in accounting policies. However, none of these changes have a material financial impact on the IAG Group.

The adoption of the following AASBs impacted the financial report disclosure for the current reporting period.

a. AASB 101 REVISED PRESENTATION OF FINANCIAL STATEMENTS

The adopted standard requires the presentation of a statement of comprehensive income by amalgamating the previously disclosed income statement and statement of recognised income and expense.

b. AASB 8 OPERATING SEGMENTS

The adopted standard requires the adoption of a 'management approach' to reporting on financial performance of operating segments. The information to be reported will be based on information used internally by key decision makers to evaluate performance of operating segments. A single set of operating segments replaces the business and geographical segments.

III. Reclassifications of comparatives

Certain items have been reclassified from the Consolidated entity's prior year financial report to conform to the current period's presentation. The reclassifications are:

- There was a change in fire service levies administration in Australia in the prior financial year ended 30 June 2009. The fire service levies are required to be prepaid based on estimated gross written premium on property insurance policies in Australia. The prepaid amount in June 2009 of \$63 million is reclassified as prepayment from trade and other payables. There is no impact to the profit/(loss) for the period.
- A reallocation of \$91 million between fee and other income and fee based, corporate and other expense as at 30 June 2009 due to an incorrect classification related to the United Kingdom fee based business in the prior period. There is no impact to the profit/(loss) for the period.
- The premium receivable on New Zealand's coinsurance arrangements and the corresponding payable to third party reinsurers is derecognised due to the premium only being passed onto third parties once received. The change resulted in a reduction of premium receivable and trade and other payables of \$18 million. There is no impact to the profit/(loss) for the period.

IV. Rounding

Amounts in this financial report have been rounded to the nearest million dollars, unless otherwise stated. The Company is the kind of company referred to in the class order 98/100 dated 10 July 1998 issued by the Australian Securities & Investments Commission. All rounding has been conducted in accordance with that class order.

V. Presentation of Parent financial statements

Parent entity financial statements have been included in the consolidated financial statements in this financial report for the year ended 30 June 2010. The Company is the kind of company referred to in the class order 10/654 dated 26 July 2010 issued by the Australian Securities & Investments Commission.

C. PRINCIPLES OF CONSOLIDATION

I. Subsidiaries

Consolidation is the incorporation of the assets and liabilities of the Parent and all subsidiaries as at the reporting date and the results of the Parent and all subsidiaries for the period then ended as if they had operated as a single entity. The balances and effects of intragroup transactions are eliminated from the consolidation. Subsidiaries are those entities controlled by the Parent. Control exists when one company has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. Control is presumed to exist when more than half of the voting power of an entity is owned either directly or indirectly. In assessing control, potential voting rights that are exercisable or convertible are taken into account. Where an entity either began or ceased to be controlled during a financial reporting period, the results are included only from the date control commenced or up to the date control ceased.

The financial statements of all subsidiaries are prepared for consolidation for the same reporting period as the Parent, using consistent accounting policies. 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.

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 where the subsidiary is a trust or similar entity for which the core equity is presented as a liability (this is the case with the IAG Asset Management Wholesale Trusts that are subsidiaries, refer to the details of subsidiaries note) in which case the third party interest is presented separately on the consolidated balance sheet as a liability.

II. Associates

Associates, those entities over which significant influence is exercised and which are not intended for sale in the near future, are accounted for using equity accounting principles. Significant influence is presumed to exist where between 20% and 50% of the voting rights of an entity are held, but can also arise where less than 20% is held through active involvement and influencing policy decisions affecting the entity. The investment in associates is initially recognised at cost (fair value of consideration provided plus directly attributable costs) and is subsequently adjusted for the post-acquisition change in the investor's share of net assets of the investee (generally referred to as the equity method). 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 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 investments are reviewed annually for impairment.

Where an entity either began or ceased to be an associate during the current financial reporting period, 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.

III. Lloyd's syndicates

The nature of Lloyd's syndicates is such that even when one party provides the majority of capital, the syndicate as a whole is still not controlled for accounting purposes. Members of Lloyd's accept insurance business through syndicates on a separate basis for their own profit and are not jointly responsible for each other's losses. Hence, even where the IAG Group contributes the majority of capital for a syndicate, only the portion of the syndicate represented by the capital contribution is recognised in the consolidated financial report.

SIGNIFICANT ACCOUNTING POLICIES RELATED TO GENERAL INSURANCE CONTRACTS

All of the general insurance products and reinsurance products on offer, or utilised, meet the definition of an insurance contract (a contract under which one party, the insurer, accepts significant insurance risk from another party, the policyholder, by agreeing to compensate the policyholder if a specified uncertain future event, the insured event, adversely affects the policyholder) and none of the contracts contains embedded derivatives or is required to be unbundled. Insurance contracts that meet the definition of a financial guarantee contract are accounted for as insurance contracts. This means that all of the general insurance products are accounted for in the same manner.

D. PREMIUM REVENUE

Premium revenue comprises amounts charged to policyholders (direct premium) or other insurers (inwards reinsurance premium) for insurance contracts. Premium includes amounts collected for levies and charges for which the amount to be paid by the insurer does not depend on the amounts collected, such as for fire services levies in Australia, but excludes stamp duties and taxes collected on behalf of third parties, including the goods and services tax in Australia. Premium is recognised as earned from the date of attachment of risk (generally the date a contract is agreed to but may be earlier if persuasive evidence of an arrangement exists) over the period of the related insurance contracts in accordance with the pattern of the incidence of risk expected under the contracts. The pattern of the risks underwritten is generally matched by the passing of time. Premium for unclosed business (business written close to reporting date where attachment of risk is prior to reporting date and there is insufficient information to accurately identify the business) is brought to account based on previous experience with due allowance for any changes in the pattern of new business and renewals. The unearned portion of premium is recognised as an unearned premium liability on the balance sheet.

Premium receivable is recognised as the amount due and is normally settled between 30 days and 12 months. The recoverability of premium receivable is assessed and provision is made for impairment based on objective evidence and having regard to past default experience. Premium receivable is presented on the balance sheet net of any provision for impairment.

E. OUTWARDS REINSURANCE

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

F. CLAIMS

The outstanding claims liability is measured as the central estimate of the present value of expected future payments relating to claims incurred at the reporting date with an additional risk margin to allow for the inherent uncertainty in the central estimate. The liability is measured based on the advice of/valuations performed by, or under the direction of, the Appointed Actuary. The expected future payments include those in relation to claims reported but not yet paid or not yet paid in full, claims incurred but not enough reported (IBNER), claims incurred but not reported (IBNR) and the anticipated direct and indirect claims handling costs. The liability is discounted to present value using a risk free rate.

Claims expense represents claim payments adjusted for the movement in the outstanding claims liability.

The estimation of the outstanding claims liability involves a number of key assumptions and is the most critical accounting estimate. All reasonable steps are taken to ensure that the information used regarding claims exposures is appropriate. However, given the uncertainty in establishing the liability, it is likely that the final outcome will be different from the original liability established. Changes in claims estimates are recognised in profit or loss in the reporting period in which the estimates are changed.

G. REINSURANCE AND OTHER RECOVERIES

Reinsurance and other recoveries received or receivable on paid claims and on outstanding claims (notified and not yet notified) are recognised as income. Reinsurance recoveries on paid claims are presented as part of trade and other receivables net of any provision for impairment based on objective evidence for individual receivables. Reinsurance and other recoveries receivable on outstanding claims are measured as the present value of the expected future receipts calculated on the same basis as the outstanding claims liability. Reinsurance does not relieve the originating insurer of its liabilities to policyholders and is presented separately on the balance sheet.

H. ACQUISITION COSTS

Costs associated with obtaining and recording general insurance contracts are referred to as acquisition costs. These costs include advertising expenses, commissions or brokerage paid to agents or brokers, premium collection costs, risk assessment costs and other administrative costs. Profit commission received from third party names relating to providing managing agency services to Lloyd's syndicates is also included in acquisition costs. Such costs are capitalised where they relate to the acquisition of new business or the renewal of existing business, are presented as deferred acquisition costs, and are amortised on the same basis as the earning pattern of the premium over the period of the related insurance contracts. The balance of the deferred acquisition costs at the reporting date represents the capitalised acquisition costs relating to unearned premium.

I. LIABILITY ADEQUACY TEST

The liability adequacy test is an assessment of the carrying amount of the unearned premium liability and is conducted at each reporting date. If current estimates of the present value of the expected future cash flows relating to future claims arising from the rights and obligations under current general insurance contracts, plus an additional risk margin to reflect the inherent uncertainty in the central estimate, exceed the unearned premium liability (net of reinsurance) less related deferred acquisition costs, then the unearned premium liability is deemed to be deficient. The test is performed at the level of a portfolio of contracts that are subject to broadly similar risks and that are managed together as a single portfolio. Any deficiency arising from the test is recognised 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, with any remaining balance being recognised on the balance sheet as an unexpired risk liability.

J. LEVIES AND CHARGES

Levies and charges, for which the amount paid does not depend on the amounts collected, as is the case with fire services levies in Australia, are expensed on the same basis as the recognition of premium revenue. The portion relating to unearned premium is treated as a prepayment and presented as deferred levies and charges on the balance sheet. A liability for levies and charges payable is recognised on business written to the reporting date. Other levies and charges that are simply collected on behalf of third parties are not recognised as income or expense in profit or loss.

SIGNIFICANT ACCOUNTING POLICIES APPLICABLE TO OTHER ACTIVITIES

K. FEE AND OTHER INCOME

Fee based revenue is brought to account on an accruals basis being recognised as revenue on a straight line basis in accordance with the passage of time as the services are provided. Other income is recognised on an accruals basis.

L. LEASES

The majority of leases entered into are operating leases, where the lessor retains substantially all the risks and benefits of ownership of the leased items. The majority of the lease arrangements are entered into as lessee for which the lease payments are recognised as an expense on a straight line basis over the term of the lease. Certain sublease arrangements are entered into as the lessor for which the lease payments are recognised as revenue on a straight line basis over the term of the lease.

Lease incentives relating to the agreement of a new or renewed operating lease are recognised as an integral part of the net consideration agreed for the use of the leased asset. Operating lease incentives received are initially recognised as a liability, are presented as trade and other payables, and are subsequently reduced through recognition in profit or loss as an integral part of the total lease expense (lease payments are allocated between rental expense and reduction of the liability) on a straight line basis over the period of the lease.

M. TAXATION

I. Income tax

Income tax on the result for a reporting period 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 equity, in which case it is recognised in equity.

Current tax expense is the expected tax 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. Deferred tax expense is the change in deferred tax assets and liabilities between the reporting periods.

Deferred tax assets and liabilities are recognised using the balance sheet method for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes, except in the following 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.

The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at reporting date. Deferred tax assets are recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised.

II. 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.

Current tax expense/income and deferred tax assets and liabilities arising from temporary differences of the members of the tax-consolidated group are recognised in the separate financial statements of the members of the tax-consolidated group using the 'separate taxpayer within group' approach by reference to the carrying amounts in the separate financial statements of each entity and the tax values applying under tax consolidation.

Any current tax liabilities (or assets) and deferred tax assets arising from unused tax losses of the subsidiaries are assumed by the head entity in the tax-consolidated group and are recognised as amounts receivable/(payable) from/(to) other entities in the tax-consolidated group in conjunction with any tax funding arrangement amounts (refer below). Any difference between these amounts is recognised by IAG as an equity contribution or distribution.

IAG recognises deferred tax assets arising from unused tax losses of the tax-consolidated group to the extent that it is probable that future taxable profits of the tax-consolidated group will be available against which the asset can be utilised.

NATURE OF TAX FUNDING ARRANGEMENTS AND TAX SHARING ARRANGEMENTS

The head entity, in conjunction with members of the tax-consolidated group, has entered into a tax funding arrangement which sets out the funding obligations of members of the tax-consolidated group with respect to tax amounts. The tax funding arrangements require payments to/(from) the head entity equal to the current tax liability/(asset) assumed by the head entity and any tax loss deferred tax assets (associated with tax losses of the wholly owned subsidiaries) assumed by the head entity. This results in the head entity recognising an intercompany receivable/(payable) equal in amount to the tax liability/(asset) assumed. The intercompany amount receivable/(payable) is at call.

Contributions to fund the current tax liabilities are payable as per the tax funding arrangement and reflect the timing of the head entity's obligation to make payments for tax liabilities to the relevant tax authorities.

The head entity, in conjunction with members of the tax-consolidated group, has also entered into a tax sharing agreement. The tax sharing agreement provides for the determination of the allocation of income tax liabilities between the entities of the tax-consolidated group should the head entity default on its tax payment obligations. No amounts have been recognised in the financial statements in respect of this agreement as payment of any amounts under the tax sharing agreement is considered remote.

III. Goods and services tax

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

Receivables and payables are stated inclusive of GST. The net amount of GST recoverable from, or payable to, the ATO is included as part of other receivables and payables on the balance sheet. Cash flows are included in the cash flow statement on a gross basis. The GST components of cash flows arising from investing and financing activities, which are recoverable from, or payable to, the ATO are classified as operating cash flows.

N. INVESTMENTS

Investments comprise assets held to back insurance liabilities (also referred to as technical reserves) and assets that represent equity holders' funds. All investments are managed and performance evaluated on a fair value basis for both external and internal reporting purposes in accordance with a documented risk management strategy.

All investments are designated as fair value through profit or loss upon initial recognition. They are initially recorded at fair value (being the cost of acquisition excluding transaction costs) and are subsequently remeasured to fair value at each reporting date. Changes in the fair value from the previous reporting date (or cost of acquisition excluding transaction costs if acquired during the financial period) are recognised as realised or unrealised investment gains or losses in profit or loss. 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 and presented in the statement of comprehensive income as investment expenses on assets backing insurance liabilities and fee based, corporate and other expenses for investments that represent equity holders' funds. 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.

For securities traded in an active market, fair value is determined by reference to published bid price quotations. For trust securities this generally means using the redemption price provided by the trustee. For securities not traded, and for securities traded in a market that is not active, fair value is determined using valuation techniques with the most common technique being reference to observable market data by reference to the fair values of recent arm's length transactions involving the same or similar instruments. An alternative valuation technique that is used for a small number of investments is a discounted cash flow methodology.

Investment revenue, comprising dividends, trust distributions and interest, is brought to account on an accruals basis. Revenue on investment 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. Dividend revenue from Australian equities is received net of any franking credits.

O. INVESTMENT IN SUBSIDIARIES

Investment in subsidiaries is initially recognised at cost (fair value of consideration provided plus directly attributable costs) and is subsequently carried in the Parent's financial statements at the lower of cost and recoverable amount. Costs incurred in investigating and evaluating an acquisition up to the point of formal commitment to an acquisition are expensed as incurred. Where the carrying value exceeds the recoverable amount, an impairment charge is recognised in profit or loss which can subsequently be reversed in certain conditions.

Where an additional interest is purchased in an existing subsidiary, the acquisition is treated as a transaction between owners and has no impact on the statement of comprehensive income.

Income from these investments, comprising dividends and trust distributions, is brought to account on an accruals basis. Dividend revenue is accrued on the date the dividends are declared.

P. INVESTMENT IN JOINT VENTURES AND ASSOCIATES

Investment in joint ventures and associates is initially recognised at cost (fair value of consideration provided plus directly attributable costs) by the entity holding the ownership interest, including attributed goodwill, and is subsequently carried in the entity's financial statements at the lower of cost and recoverable amount.

Q. DERIVATIVES

A variety of derivatives are used for the sole purpose of managing risk exposures. Derivatives are not held for trading or speculative purposes but are mandatorily classified for accounting purposes as held for trading.

Derivatives are initially recognised at fair value (generally the transaction price; the fair value of the consideration given or received) on the date a derivative contract is entered into and are subsequently remeasured to fair value at each reporting date. The fair value is determined by reference to current market quotes (current bid price for derivatives presented as assets and the current ask price for derivatives presented as liabilities) or generally accepted valuation principles. The derivatives become favourable (assets) or unfavourable (liabilities) as a result of fluctuations in market rates relative to their terms. The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. Transaction costs for purchases of derivatives are expensed as incurred and presented in the statement of comprehensive income as investment expenses on assets backing insurance liabilities and fee based, corporate and other expenses for assets representing equity holders' funds.

I. Investment operations

All of the derivatives managed in conjunction with the investment operations are recognised on the balance sheet (presented together with the underlying investments) at fair value with movements in fair value being recognised as part of investment income in profit or loss. None of the derivatives is designated for hedge accounting. This matches the accounting for the derivatives with the accounting for the underlying investments.

II. Corporate treasury operations

Derivatives are used to hedge exposure to foreign currency and interest rate movements in relation to corporate treasury transactions, including interest bearing liabilities. While there are a number of economic hedges in place, not all of these transactions have been selected for hedge accounting. Where hedge accounting is not applied the derivative and the hedged item are recognised and measured independently as if there was no hedging relationship with the derivative being recognised on the balance sheet at fair value with movements in fair value being recognised in profit or loss. The derivatives are classified as assets and presented as receivables when the fair value is positive, or as liabilities and presented as payables when the fair value is negative, except for cross currency swaps relating to interest bearing liabilities, which are presented together with the interest bearing liabilities.

III. Hedge accounting

Where derivatives are designated for hedge accounting, they are classified as:

- hedge of the change in fair value of recognised assets or liabilities or firm commitments (fair value hedge); or
- hedge of the variability in highly probable future cash flows attributable to a recognised asset or liability, or a forecast transaction (cash flow hedge); or
- hedge of a net investment in a foreign operation (net investment hedge).

Hedge accounting may be applied to derivatives designated as hedging instruments provided certain criteria are met. Certain transactions have been designated as either a cash flow hedge or a net investment hedge.

To qualify for hedge accounting, at the inception of the hedge and throughout its life, each hedge must be expected to be highly effective (prospective effectiveness). Actual effectiveness (retrospective effectiveness) in the range of 80% to 125% must also be demonstrated on an ongoing basis. At the inception of a hedging relationship, the relationship between the hedging instruments and hedged items is documented, as well as the risk management objective and strategy for undertaking the hedge. When it is determined that a derivative for which hedge accounting has been designated is not (or ceases to be) highly effective, hedge accounting is discontinued prospectively from the date of ineffectiveness.

a. CASH FLOW HEDGE

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in reserves as part of equity. Any gain or loss relating to an ineffective portion is immediately recognised in profit or loss.

When the forecast transaction that is hedged results in the recognition of a financial asset or a financial liability, the associated gains and losses that had been deferred in equity are transferred into profit or loss in the same period or periods during which the asset acquired or liability assumed affects profit or loss. When the forecast transaction that is hedged results in the recognition of a non financial asset or a non financial liability, the associated gains and losses that had been deferred in equity are transferred from equity and included in the initial measurement of the cost of the asset or liability.

More specifically, derivatives are used to hedge a forecast acquisition of a business only when the derivative is expected to reduce exposure to the risks being hedged, is designated prospectively so that it is clear when a forecast transaction has or has not occurred, and it is probable the forecast transaction will occur. Hedge accounting is applied where such hedges meet the hedge accounting requirements. Gains or losses on the derivative arising up to the date of the forecast transaction, together with any costs arising at the time of entering into the derivative, are deferred and included in the measurement of the transaction (typically cost of acquisition of a business). Any gains or losses on the derivative after the transaction date are recognised in profit or loss. If the transaction does not occur as anticipated, the costs are immediately expensed.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity until the forecast transaction is ultimately recognised in profit or loss. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to profit or loss.

b. NET INVESTMENT HEDGE

Hedges of net investments in foreign operations are accounted for similarly to cash flow hedges. Any gain or loss on the hedging instrument 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.

IV. Embedded derivatives

Derivatives embedded in other financial instruments or other non financial host contracts are treated separately when their risks and characteristics are not closely related to those of the host contract and the host contract is not carried at fair value with movements recognised in profit or loss. Where an embedded derivative is required to be separated, it is measured at fair value.

Embedded derivatives are assessed for separation from their host contract when the entity first becomes a party to the contract and are not reassessed unless there is a significant change in the terms of the contract.

R. TRADE AND OTHER RECEIVABLES

Trade and other receivables are stated at the amounts to be received in the future and are presented net of any provision for impairment. 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 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.

S. PROPERTY AND EQUIPMENT

Property and equipment is initially recorded at cost which is the fair value of consideration provided plus incidental costs directly attributable to the acquisition (for land and buildings held as at 30 June 2004, the fair value at that date has been used as the deemed cost). The cost of equipment that is located on certain leased premises is increased by the present value of the estimated future cost for dismantling and removing the items when the relevant alterations are made to the premises with a corresponding recognition of a lease provision (refer to section Y of the summary of significant accounting policies note). All items of property and equipment are carried at cost less accumulated depreciation and accumulated impairment charges. Items other than land are depreciated using the straight line method at rates based on the expected useful lives of the assets taking into account estimated residual values. Depreciation rates and residual values are reviewed annually and any changes are accounted for prospectively.

The carrying amount of each class of property and equipment is reviewed each reporting date by determining whether there is an indication that the carrying value of a class may be impaired. If any such indication exists, the item is tested for impairment by comparing the recoverable amount of the asset or its cash generating unit to the carrying value. An impairment charge is recognised whenever the carrying value exceeds the recoverable amount. Impairment charges are recognised in profit or loss and may be reversed where there has been an indication that the loss may no longer exist and/or there is a change in the estimates used to determine the recoverable amount.

The net gain or loss on disposal of items of property and equipment is recognised in profit or loss and is calculated as the difference between the carrying amount of the asset at the time of disposal and the net proceeds on disposal including transaction costs and other expenses associated with the disposal.

T. BUSINESS COMBINATIONS

Business combinations are accounted for using the acquisition method. Business combinations occur when control is obtained over an entity or business.

The accounting for an acquisition involves the cost of the business combination being allocated to the individual assets acquired (tangible and intangible) and the individual liabilities assumed (including contingent liabilities) based on their separate fair values determined at the acquisition date. Goodwill represents the excess of the purchase consideration over the fair value of the net identifiable assets and contingent liabilities acquired. If the cost of acquisition is less than the fair value of the net identifiable assets and contingent liabilities acquired, the difference is recognised immediately in profit.

Where settlement of any part of cash consideration is deferred, the amounts payable in the future are discounted to their present value at the date of exchange. The discount rate used is the incremental borrowing rate, being the rate at which a similar borrowing could be obtained from an independent financier under comparable terms and conditions.

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

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

Where a business combination is achieved in stages (commonly referred to as a step acquisition), the acquirer shall remeasure its previously held non-controlling interests in the acquiree at its acquisition date fair value, any profit or loss on the change in fair value is recognised in the statement of comprehensive income. Goodwill is only recognised on the additional controlling interest in the same way as other business combinations where control is gained at acquisition. Before qualifying as a business combination, a transaction may qualify as an investment in an associate (refer to section 1.C of the summary of significant accounting policies note).

Acquisitions and disposals (where control is retained) of non-controlling interests are treated as transactions between equity holders. Therefore, any difference between the acquisition cost of the non-controlling interests and the carrying amount of the non-controlling interests is recognised as an increase or decrease in equity.

U. INTANGIBLE ASSETS

I. Acquired intangible assets

Acquired intangible assets are initially recorded at their cost at the date of acquisition being the fair value of the consideration provided and, for assets acquired separately, incidental costs directly attributable to the acquisition. Intangible assets with finite useful lives are amortised on a straight line basis (unless the pattern of usage of the benefits is significantly different) over the estimated useful lives of the assets being the period in which the related benefits are expected to be realised (shorter of legal duration and expected economic life). Amortisation rates and residual values are reviewed annually and any changes are accounted for prospectively.

The carrying amount of intangible assets with finite useful lives is reviewed each reporting date by determining whether there is an indication that the carrying value may be impaired. If any such indication exists, the item is tested for impairment by comparing the recoverable amount of the asset or its cash generating unit to the carrying value. Where the recoverable amount is determined by the value in use, the projected net cash flows are discounted using a pre tax discount rate. For assets with indefinite useful lives, 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. An impairment charge is recognised when the carrying value exceeds the calculated recoverable amount. Impairment charges are recognised in profit or loss and may be reversed where there has been a change in the estimates used to determine the recoverable amount.

II. Software development expenditure

Software development expenditure that meets the criteria for recognition as an intangible asset is capitalised on the balance sheet and amortised over its expected useful life, subject to impairment testing. Costs incurred in researching and evaluating a project up to the point of formal commitment to a project are treated as research costs and are expensed as incurred. Only software development projects with total budgeted expenditure of more than \$2 million are considered for capitalisation or where such services are provided under a comprehensive outsourcing agreement. Smaller projects and other costs are treated as maintenance costs, being an ongoing part of maintaining effective computer systems, and are expensed as incurred.

All such capitalised costs are deemed to have an expected useful life of three years unless it can be clearly demonstrated for a specific project that the majority of the net benefits are to be generated over a longer period. The capitalised costs are amortised on a straight line basis over the period following completion of a project or implementation of part of a project. The recoverability of the carrying amount of the asset is assessed in the same manner as for acquired intangible assets with finite useful lives.

V. GOODWILL

Goodwill acquired in a business combination is initially measured at cost being the excess of the purchase consideration over the fair value of the net identifiable assets and contingent liabilities acquired and is subsequently presented net of any impairment charges. Goodwill arising on acquisitions prior to 1 July 2004 has been carried forward on the basis of its deemed cost being the net carrying amount as at that date.

Goodwill is allocated to cash generating units (the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets) expected to benefit from the synergies of a business combination for the purpose of impairment testing. Cash generating units are determined based principally on how goodwill is monitored by management. The recoverability of the carrying value of the goodwill allocated to each cash generating unit is tested for impairment at each reporting date, or more frequently if events or changes in circumstances indicate that it might be impaired, by determining the present value (using a pre tax discount rate that reflects the current market assessments of the risks specific to the cash generating unit) of projected net cash flows based on the five year business plans approved by management. Net cash flows beyond the five year period are extrapolated based on growth rates relevant to the asset/business which are consistent with long term industry averages. Where the carrying value exceeds the recoverable amount, an impairment charge is recognised in profit or loss and cannot subsequently be reversed.

Goodwill balances are denominated in the currency of the acquired entity and are translated to Australian dollars on a consistent basis with the other assets and liabilities held by the acquired entity.

At the date of disposal of a business, attributed goodwill is included in the share of net assets used in the calculation of the gain or loss on disposal.

W. TRADE AND OTHER PAYABLES

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

X. 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, including termination benefits, decommissioning of information technology systems and exiting surplus premises, and does not include costs associated with ongoing activities. The adequacy of the provision is reviewed regularly and adjusted if required. Revisions in the estimated amount of a restructuring provision are reported in the period in which the revision in the estimate occurs. The provision is discounted using a pre tax discount rate where the effect of the time value of money is material. Where discounting is applied, the increase in the provision due to the passage of time is recognised as a finance cost.

Y. LEASE PROVISION

Certain operating leases for property require that the land and/or building be returned to the lessor in its original condition, however, the related operating lease payments do not include an element for the cost this will involve. The present value of the estimated future cost for the plant and equipment to be removed and the premises to be returned to the lessor in its original condition are recognised as a lease provision when the relevant alterations are made to the premises. The costs are capitalised as part of the cost of plant and equipment and then depreciated over the useful lives of the assets (refer to section S of the summary of significant accounting policies note).

Z. ONEROUS CONTRACTS PROVISION

A provision is recognised for onerous contracts when the expected benefits to be derived from a contract are lower than the unavoidable cost of meeting the obligations under the contract.

AA. EMPLOYEE BENEFITS

I. Wages and salaries, annual leave and sick leave

Liabilities for wages and salaries (including bonuses), annual leave and sick leave are recognised at the nominal amounts unpaid at the reporting date using remuneration rates that are expected to be paid when these liabilities are settled, including on-costs. A liability for sick leave is considered to exist only when it is probable that sick leave taken in the future will be greater than entitlements that will accrue in the future.

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 interest rates on national government guaranteed securities 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. Share based incentive arrangements

Share based remuneration is provided in different forms to eligible employees and IAG directors. All of the arrangements are equity settled share based payments. The fair value at grant date (the date at which the employer and the employee have a shared understanding of the terms and conditions of the arrangement) is determined for each equity settled share based payment using a valuation model which excludes the impact of any non market vesting conditions. This fair value does not change over the life of the instrument. At each reporting date during the vesting period (the period during which related employment services are provided), and upon the final vesting or expiry of the equity instruments, the total accumulated expense is revised based on the fair value at grant date and the latest estimate of the number of equity instruments that are expected to vest based on non market vesting conditions only, and taking into account the expired portion of the vesting period. Changes in the total accumulated expense from the previous reporting date are recognised in profit or loss with a corresponding movement in an equity reserve. Upon exercise of the relevant instruments, the balance of the share based remuneration reserve relating to those instruments is transferred within equity.

The different treatment of market and non market vesting conditions means that if an equity instrument does not vest because a participant ceases relevant employment then the accumulated expense charged in relation to that participant is reversed, but if an equity instrument does not vest only because a market condition is not met, the expense is not reversed.

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 held in trust. Shares held in trust that are controlled for accounting purposes are treated as treasury shares held in trust (refer to section AG of the summary of significant accounting policies note).

IV. Superannuation

Contributions are made to various superannuation plans, both defined contribution and defined benefit superannuation plans, in accordance with their governing rules and, for defined benefit superannuation plans, recommendations from their respective actuaries, which are designed to ensure that each plan's funding provides sufficient assets to meet its liabilities over the longer term.

For defined contribution superannuation plans, obligations for contributions are recognised in profit or loss as they become payable. 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 actuarial gains and losses (experience adjustments and changes in actuarial assumptions), which are recognised directly in retained earnings.

AB. INTEREST BEARING LIABILITIES AND FINANCE COSTS

Interest bearing liabilities are initially recognised at fair value less transaction costs that are directly attributable to the transaction. After initial recognition the liabilities are carried at amortised cost using the effective interest method.

Finance costs include interest, which is accrued at the contracted rate and included in payables, amortisation of transaction costs which are capitalised, presented together with the borrowings, and amortised over the life of the borrowings or a shorter period if appropriate, and amortisation of discounts or premiums (the difference between the original proceeds, net of transaction costs, and the settlement or redemption value of borrowings) over the term of the liabilities. Where interest payments are subject to hedge accounting, they are recognised as finance costs net of any effect of the hedge.

AC. FOREIGN CURRENCY

I. Functional and presentation currency

Items included in the financial records are measured using the currency of the primary economic environment in which the entity operates (functional currency). The financial statements are presented in Australian dollars, which is the functional and presentation currency of the Company.

II. Translation of foreign currency transactions

Foreign currency transactions are translated into the functional currency 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 the functional currency using reporting date exchange rates. Resulting exchange differences are recognised in profit or loss.

III. Translation of the financial results of foreign operations

The financial position and performance of foreign operations with a functional currency other than Australian dollars are translated into the presentation currency for inclusion in the consolidated financial statements. The assets and liabilities are translated using reporting date exchange rates while equity items are translated using historical rates. Items from the statement of comprehensive income are translated using weighted average rates for the reporting period. Exchange differences arising from the translations are recorded directly in equity in the foreign currency translation reserve. Goodwill and fair value adjustments arising on the acquisition of a foreign operation are treated as assets and liabilities of the foreign operation and translated using reporting date exchange rates.

On the disposal of a foreign operation, the cumulative amount of the exchange differences deferred in the foreign currency translation reserve relating to that foreign operation is recognised in profit or loss.

IV. Hedge transactions

Derivatives are used to hedge the foreign exchange risk relating to certain transactions. Refer to section Q.III of the summary of significant accounting policies note for details of the relevant accounting policies.

V. Principal exchange rates used

The reporting date exchange rates for balance sheet translation and the annual average daily exchange rates for statement of comprehensive income and cash flow statement translation are provided here for selected currencies to Australian dollars as an indication of the rates used for the current period.

	BALANCE SHEET		STATEMENT OF COMPREHENSIVE INCOME AND CASH FLOW STATEMENT	
	2010	2009	2010	2009
New Zealand dollar	0.81361	0.80406	0.79651	0.81335
British pound	1.76643	2.05679	1.79332	2.16128
Thai baht	0.03624	0.03614	0.03419	0.03856
United States dollar	1.17488	1.22926	1.13327	1.33816

AD. PROVISION FOR DIVIDENDS

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.

AE. EARNINGS PER SHARE

I. Basic earnings per share

Basic earnings per share is determined by dividing the profit or loss attributable to equity holders of the Parent by the weighted average number of shares of the Parent on issue during the reporting period, net of treasury shares held in trust.

II. Diluted earnings per share

Diluted earnings per share is determined by dividing the profit or loss attributable to equity holders of the Parent used in the calculation of basic earnings per share, adjusted for relevant costs associated with dilutive potential ordinary shares, by the weighted average number of ordinary shares and dilutive potential ordinary shares.

AF. SHARE CAPITAL

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.

AG. TREASURY SHARES HELD IN TRUST

Ordinary shares of IAG that are controlled for accounting purposes by share based remuneration trusts that are subsidiaries of the Consolidated entity, are presented on the balance sheet as treasury shares held in trust. The shares are measured at cost (total amount paid to acquire the shares including directly attributable costs), and are presented as a deduction from equity until they are otherwise dealt with. 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.

AH. LOANS TO/FROM RELATED PARTIES

Loans to/from related parties are initially recognised at fair value less transaction costs that are directly attributable to the transaction. After initial recognition the liabilities are carried at amortised cost using the effective interest method.

NOTE 2. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

In the process of applying the significant accounting policies, certain critical accounting estimates and assumptions are used, and certain judgements are made.

The estimates and related assumptions are based on experience and other factors that are considered to be reasonable, the results of which form the basis for judgements about the carrying values of assets and liabilities. Actual results may differ from these estimates. The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised, and future periods if relevant.

The areas where the estimates and assumptions involve a high degree of judgement or complexity and are considered significant to the financial statements, listed together with reference to the notes to the financial statements where more information is provided, are:

- insurance contracts related:
 - claims, refer to note 12;
 - reinsurance and other recoveries on outstanding claims, refer to note 13; and
 - liability adequacy test, refer to note 15.B.

There are other amounts relating to insurance contracts that are based on allocation methodologies supported by assumptions (e.g. deferred acquisition costs, which are costs related to the acquisition of general insurance contracts and so eligible for deferral). The estimates relate to past events, do not incorporate forward looking considerations, and generally do not change from year to year.

- other:
 - intangible assets and goodwill impairment testing, refer to notes 19 and 20;
 - acquired intangible assets initial measurement and determination of useful life, refer to notes 19 and 26;
 - share based remuneration, refer to note 30; and
 - defined benefit superannuation arrangements, refer to note 31.

The accounting judgements made during the reporting period that did not involve estimations, including determination of the existence of control when entities are not wholly owned, the selection of valuation models for complex financial instruments such as the recognition of the identifiable intangible assets acquired in a business combination, and the probability of recovering carry forward tax losses, are considered to have had no significant impact on the amounts recognised in the financial report (2009—none).

NOTE 3. INSURANCE RISK MANAGEMENT

A key risk from operating in the general insurance industry is the exposure to insurance risk arising from underwriting general insurance contracts. The insurance contracts transfer risk to the insurer by indemnifying the policyholders against adverse effects arising from the occurrence of specified uncertain future events. There is a risk that the actual amount of claims to be paid in relation to contracts will be different to the amount estimated at the time a product was designed and priced. The Consolidated entity is exposed to this risk because the price for a contract must be set before the losses relating to the product are known. Hence the insurance business involves inherent uncertainty. The Consolidated entity also faces other risks relating to the conduct of the general insurance business including financial risks (refer to the financial risk management note) and capital risks (refer to the capital management note).

A fundamental part of the IAG Group's overall risk management strategy is the effective governance and management of the risks that impact the amount, timing and uncertainty of cash flows arising from insurance contracts.

A. RISK MANAGEMENT FRAMEWORK

The IAG Group has in place a dedicated group risk management function responsible for the development and maintenance of the risk management framework. The risk management framework provides reasonable assurance that the IAG Group's material risks are being prudently and soundly managed. At the same time it is acknowledging that all business activity entails risk so the focus is on management of this risk rather than complete risk avoidance. The risk management framework includes a written Risk Management Strategy (RMS) which is in accordance with the prudential standards issued by Australian Prudential Regulation Authority (APRA). The RMS:

- is a high level, strategic document intended to describe key elements of the risk management framework;
- describes board and management approved parameters (i.e. risk appetite) within which key decisions must be made;
- is a key input into how regulators understand and assess the approach to risk management; and
- forms the basis of twice yearly declarations provided by executives and senior management to the board.

The framework also includes clearly defined managerial responsibilities, details of the group level risk management related policies and the key processes to identify, assess, monitor, report on and mitigate all material risks, financial and non financial, likely to be faced. The group level policies for the management of risk are required to be applied by all businesses consistently across the IAG Group with certain allowances made for local circumstances in non-Australian jurisdictions. There is a transition period for newly acquired businesses to comply with these policies.

A review process is in place to ensure that the risk management framework remains appropriate and effective. The IAG Group has an internal audit function. As part of the internal audit plan there are reviews undertaken on various aspects of the risk management framework usage in the business divisions. Standard & Poor's (S&P) has rated the IAG Group enterprise risk management program to be 'strong'.

The RMS is updated annually and approved by the board. It is resubmitted to APRA after any material changes are made. A three year rolling business plan is also submitted to APRA after each annual review or whenever material changes are made.

The framework also includes a written Reinsurance Management Strategy (REMS) which sets out key elements of the reinsurance management framework, processes for setting and monitoring the maximum event retention (MER), processes for selecting, implementing, monitoring and reviewing reinsurance arrangements and identification, roles and responsibilities of those charged with managerial responsibility for the reinsurance management framework. The REMS is in accordance with the prudential standards issued by APRA. The REMS is updated annually and approved by the board.

B. RISK MANAGEMENT OBJECTIVES AND POLICIES FOR MITIGATING INSURANCE RISK

The insurance activities primarily involve the underwriting of risks and the management of claims. A disciplined approach to risk management is adopted rather than a premium volume or market share orientated approach. IAG believes this approach provides the greatest long term likelihood of being able to meet the objectives of all stakeholders, including policyholders, lenders and equity holders.

The policies for the management of risk are applied consistently across the IAG Group with certain allowances made for local circumstances in non-Australian jurisdictions. There is a transition period for newly acquired businesses to comply with these policies.

The key policies and processes put in place to mitigate insurance risk include the following.

I. Acceptance and pricing of risk

The underwriting of large numbers of less than fully correlated individual risks, across a range of classes of insurance businesses, in different regions reduces the variability in overall claims experience over time. Business divisions set underwriting criteria covering the types of risks they are licensed to underwrite. Maximum limits are set for the acceptance of risk both on an individual contract basis and for classes of business and specific risk groupings. Having limited exposure to long-tail classes of business (where the settlement of claims typically takes longer than one year), currently approximately 20% of the business as measured by gross written premium, limits risk. Management information systems are maintained that provide up to date, reliable data on the risks to which the business is exposed at any point in time. Efforts are made, including plain language policy terms, to ensure there is no misalignment between what policyholders perceive will be paid when a policy is initially sold and what is actually paid when a claim is made.

Statistical models that combine historical and projected data are used to calculate premiums and monitor claims patterns for each class of business. The data used includes historical pricing and claims analysis for each class of business as well as current developments in the respective markets and classes of business. All data used is subject to rigorous verification and reconciliation processes. The models incorporate consideration of prevailing market conditions.

The charts in section C of this note provide a dissection of gross written premium by region and product for the current and prior financial year demonstrating the limited exposure to the additional risks associated with long-tail classes of business.

II. Reinsurance

Reinsurance is used to limit exposure to large single claims and accumulation of claims that arise from the same event or the accumulation of similar events.

Risks underwritten are reinsured in order to limit exposure to losses, stabilise earnings, protect capital resources and ensure efficient control and spread of the risks underwritten. Each subsidiary that is an insurer has its own reinsurance program and determines its own risk tolerances, subject to principles set out in the REMS. To facilitate the reinsurance process, manage counter party exposure and to create economies of scale, the IAG Group has established a captive reinsurance operation comprising companies located in Australia and Malaysia. This operation acts as the reinsurer for the IAG Group by being the main buyer of the IAG Group's outwards reinsurance program. The reinsurance operation is intended to manage reinsurance and earnings volatility and the IAG Group's exposure to catastrophe risk. The operation retains a portion of the intercompany business it assumes and retrocedes (passes on) the remainder to external reinsurers. The REMS provides that the reinsurance retention for catastrophe is not to exceed 4% of net earned premium.

While a large portion of the business ceded by the Consolidated entity's subsidiaries is reinsured with the Group's captive reinsurance operation, individual business units located do purchase additional reinsurance protection outside the IAG Group. This generally relates to facultative reinsurance covers and selected treaty reinsurance arrangements.

The use of reinsurance introduces credit risk. The management of reinsurance includes the monitoring of reinsurers' credit risk and controls the exposure to reinsurance counterparty default. Refer to the financial risk management note for further details.

a. CURRENT PROGRAM

The reinsurance operation purchases reinsurance on behalf of IAG Group entities to cover a maximum return period of at least APRA's minimum of 1:250 year event on a single site basis but is authorised to elect to purchase covers up to 1:250 year event on a whole of portfolio basis. Dynamic financial analysis modelling is used to determine the optimal level to which reinsurance should be purchased for capital efficiency, compared with the cost and benefits of covers available in the market.

The external reinsurance programs consist of a combination of the following reinsurance protection:

- a Group catastrophe cover which is placed in line with the strategy of buying to the level of a 1:250 year event on a modified whole of portfolio basis. The catastrophe program is negotiated on an annual calendar year basis. Covers purchased are dynamic; the MER changes as total requirements change and as the reinsurance purchase strategy evolves;
- an aggregate cover which protects against a frequency of attritional event losses in Australia, New Zealand, Asia and the United Kingdom and operates below the Group catastrophe cover;
- excess of loss and proportional reinsurances which provide "per risk" protection for retained exposures of the commercial property and engineering businesses in Australia, New Zealand, Thailand, Malaysia and the United Kingdom;
- excess of loss reinsurance for all casualty portfolios including CTP, public liability, workers' compensation and home owners warranty products; and
- excess of loss reinsurance for all marine portfolios.

b. CHANGES DURING THE YEAR

The limit of catastrophe cover purchased was maintained at \$4.1 billion. At 1 January 2010, the MER for a first event arising from a physical peril was increased from \$126 million to \$135 million for Australia dropping to a lower amount for a second event. In respect of New Zealand the MER increased marginally from \$105 million to \$115 million and for the United Kingdom cover the MER was maintained at \$53 million.

The Group's reinsurance program was impacted by losses from both the Melbourne storm and the Perth hailstorm in March 2010. These events triggered the Group's second and third event protections, reducing the current MER to \$50 million for Australia and \$42 million for New Zealand. In addition, the Group's aggregate cover is also in operation and this reduces the next event to a maximum loss to the Group of \$15 million. The IAG Group had purchased a multi-year retention buy down which was exhausted during the year ended 30 June 2010.

During the year ended 30 June 2010, as part of the strategy to manage the recent reserve deterioration in the United Kingdom, a reinsurance structure was purchased. This reinsurance provides the IAG Group with significant protection against any further adverse development of the United Kingdom motor portfolio for the underwriting years ended 31 December 2009 and prior. This cover is securitised.

III. Claims management and provisioning

Initial claims determination is 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. It is the IAG Group's policy to respond to and settle all genuine claims quickly whenever possible and to pay claims fairly, based on policyholders' full entitlements.

Claims provisions are established using actuarial valuation models and include a risk margin for uncertainty (refer to the claims note).

C. CONCENTRATIONS OF INSURANCE RISK

The exposure to concentrations of insurance risk is mitigated by a portfolio diversified into many classes of business across different regions and by the utilisation of reinsurance.

Concentration risk is particularly relevant in the case of catastrophes, usually natural disasters, which generally result in a concentration of affected policyholders over and above the norm and which constitutes the largest individual potential financial loss. Catastrophe losses are an inherent risk of the general insurance industry that have contributed, and will continue to contribute, to potentially material year-to-year fluctuations in the results of operations and financial position. Catastrophes are caused by various natural events including earthquakes, bushfires, hailstorms, tropical storms and high winds. The IAG Group is also exposed to certain human-made catastrophic events such as industrial accidents and building collapses. The nature and level of catastrophes in any period cannot be predicted accurately but can be estimated through the utilisation of predictive models. The IAG Group actively limits the aggregate insurance exposure to catastrophe losses in regions that are subject to high levels of natural catastrophes.

Each year, the IAG Group sets its tolerance for concentration risk and purchases reinsurance in excess of these tolerances. Various models are used to estimate the impact of different potential natural disasters and other catastrophes. The tolerance for concentration risk is used to determine the MER which is the maximum net exposure to insurance risk determined appropriate for any single event with a given probability. The MER for a second event during the period of reinsurance cover is generally lower than that for the first event. While it is desirable to limit the net exposure, it is reduced to only the MER limit because the cost of purchasing reinsurance cover to reduce the net exposure further is not considered capital efficient.

The tables below demonstrate the diversity of the IAG Group's operations by both region (noting that the insurance risks underwritten in Australia are written in all states and territories) and product indicating that the concentration of insurance risk is not significant. The tables show risk concentrations before reinsurance.

The table below provides an analysis of gross written premium by region.

	CONSOLIDATED	
	2010	2009
	%	%
Australia	77	74
New Zealand	12	12
United Kingdom	9	12
Asia	2	2
	100	100

The consolidated gross written premium decreased by 0.8% to \$7,782 million.

The table below provides an analysis of gross written premium by product.

Motor	37	38
Home	23	22
Short-tail commercial	17	16
CTP (Motor liability)	12	11
Liability	5	5
Other short-tail	4	5
Workers' compensation	2	3
	100	100

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	Insured property concentrations	Accumulation risk modelling, reinsurance protection
A large property loss	Fire or collapse affecting one building or a group of adjacent buildings	Maximum acceptance limits, property risk grading, 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

D. OPERATIONAL RISK

Operational risk is the risk of financial loss (including lost opportunities) resulting from external events and/or inadequate or failed internal processes wherein, people and systems fail to perform as required. Operational risk can have overlaps with all of the other risk categories. When controls fail, operational risk events can cause injury, damage to reputation, have legal or regulatory implications or can lead to financial loss. The IAG Group cannot expect to eliminate all operational risks, but manages these by initiating an appropriate control framework and by monitoring and responding to potential risks, the IAG Group is able to manage risks and therefore minimise its exposure to such risks.

The RMS includes consideration of operational risk. Operational risk is identified and assessed on an ongoing basis and the capital management strategy includes consideration of operational risk. Management and staff are responsible for identifying, assessing and managing operational risks in accordance with their roles and responsibilities. The IAG Group has an internal audit function which monitors processes and procedures surrounding operational risk.

I. Regulatory and compliance risk

The general insurance operations of the IAG Group are subject to regulatory supervision in the jurisdictions in which they operate. The regulatory frameworks continue to develop in a number of those jurisdictions but at a minimum include requirements in relation to reserving, capital and the payment of dividends. The IAG Group works closely with regulators and monitors regulatory developments across its international operations to assess any potential impact on the ongoing ability to meet the various regulatory requirements.

Throughout the current reporting period the IAG Group has conformed with the requirements of its debt agreements, including all financial and non financial covenants (2009—full conformance).

The IAG Group participates in three Lloyd's syndicates being Equity Red Star Motor Syndicate 218 (64% share of capacity), Alba Group Syndicate 4455 (100%—in run off), and Syndicate 1208 (100%—in run off). All members at Lloyd's have joint and several liability and, in extreme cases, Lloyd's can also require 'special contributions' from members at the discretion of the Council of Lloyd's to maintain the Central Fund. Lloyd's has an A+ 'strong' rating issued by Standard & Poor's Rating Services.

E. ACQUISITION RISK

Acquisition risks are principally managed by the Consolidated entity's controls over the due diligence and subsequent integration process of significant acquisitions. The Consolidated entity mitigates this risk as much as possible by performing due diligence appropriate to its risk appetite for each target entity and by using an assembled team of relevant subject matter experts from both corporate office and business divisions to manage the integration process.

NOTE 4. FINANCIAL RISK MANAGEMENT

THE PARENT

The Parent is a non-operating holding company and so has limited direct exposure to financial risks. The board of the Parent sets the risk management policies for the IAG Group.

The financial assets and liabilities of the Parent are primarily limited to amounts receivable from/payable to related bodies corporate, loans to/from related bodies corporate, tax assets/liabilities and interest bearing liabilities.

THE CONSOLIDATED ENTITY

IAG Group's RMS, as outlined in the insurance risk management note, includes financial risk and focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the financial performance. Key aspects of the processes established to mitigate financial risks include:

- having an Asset and Liability Committee comprised of key executives with relevant oversight responsibilities that meets on a regular basis;
- monthly stress testing undertaken to determine the impact of adverse market movements and the impact of any derivative positions;
- maintenance of an approved Group Credit Risk Policy and Group Liquidity Management Policy which are reviewed at least annually; and
- implementation of a Derivatives Risk Management Statement that addresses the controls surrounding the use of derivatives and sets out the permissible use of derivatives in relation to investment strategies.

A. MARKET RISK

Market risk is the risk of adverse financial impact due to changes in fair values or future cash flows of financial instruments from fluctuations in foreign currency exchange rates, interest rates and equity prices.

I. Currency risk

a. NATURE OF THE RISKS AND HOW MANAGED

Currency risk is the risk of loss arising from an unfavourable movement in market exchange rates. The Consolidated entity operates internationally and so is exposed to currency risk from various activities conducted in the normal course of business. Foreign currency is a centrally managed risk, with hedging coordinated at the corporate office. Refer to the derivatives note for further detail on the hedging arrangements used to manage currency risk.

The key currency risk exposures relate to the following:

i. Investment of equity holders' funds

The investment of equity holders' funds in assets denominated in currencies different to the functional currency of the investing subsidiary being primarily Australian dollars, United States dollars and British pounds. Note that assets held to back insurance liabilities are held in the same currency as the related insurance liabilities eliminating any net foreign exchange exposure.

ii. Interest bearing liabilities

Foreign currency denominated interest bearing liabilities are normally of a capital nature. Some of these have been designated as hedging instruments to manage the foreign currency risk associated with investments in foreign operations as noted below.

iii. Investment in foreign operations

Net investment in foreign operations through the translation of the financial position and performance of foreign operations that have a functional currency other than the Australian dollar with the key currencies being New Zealand dollars, British pounds, Indian rupees, Malaysian ringgit and Thai baht.

b. CURRENCY RISK EXPOSURE

The financial impact from exposure to currency risk is reflected in the financial report through two mechanisms:

- translation of foreign currency transactions—these financial impacts relating primarily to investments are directly recognised in profit; and
- translation of the financial results of foreign operations—these financial impacts are recognised directly in equity in the foreign currency translation reserve and so have no impact on profit.

c. SENSITIVITY

The following tables provide information regarding the exposure of the Consolidated entity to foreign currency risk. The sensitivity analysis provided in the following tables demonstrate the effect of a change in a key assumption while other assumptions remain unchanged. In reality, there is a correlation between the assumptions and other factors. The sensitivities do not include interdependencies among the currencies, but rather show isolated exchange rate movements. The sensitivity analysis does not take into consideration that the assets and liabilities are actively managed and so assume no action by management in response to movements in the factor. Additionally, the financial position may vary at the time that any actual market movement occurs.

The impact on the measurement of various financial instruments held at reporting date of an instantaneous 10% depreciation of the Australian dollar at reporting date compared with selected currencies, on profit before tax and equity, net of related derivatives, is provided in the table below. An appreciation of the Australian dollar would have predominantly the opposite impact.

	CONSOLIDATED	
	2010	2009
	\$m	\$m
	Impact to profit	Impact to profit
Equity holders' funds including related derivatives		
United States dollar	24	4
British pound	2	3
Other currencies where considered significant	8	5
	34	12

	CONSOLIDATED	
	2010	2009
	\$m	\$m
	Impact directly to equity	Impact directly to equity
Net investments in foreign operations and related hedge arrangements		
New Zealand dollar	8	2
British pound	46	28
Other currencies where considered significant	12	4
	66	34

The sensitivity to currency fluctuations is mitigated by the extensive currency hedging measures. Refer to the derivatives note for further details.

II. Interest rate risk

a. NATURE OF THE RISK AND HOW MANAGED

Interest rate risk is the risk of loss arising from an unfavourable movement in market interest rates. Fixed interest rate assets and liabilities create exposure to fair value interest rate risk which is a market risk. Financial assets and liabilities with floating interest rates create exposure to cash flow interest rate risk.

Interest rate risk arises primarily from investments in interest bearing securities. Interest bearing liabilities are exposed to interest rate risk but as they are measured at amortised cost and are not traded they therefore do not expose the IAG Group to fair value interest rate risk. In addition, interest bearing liabilities bearing fixed interest rates (subject to some reset conditions) reduce the IAG Group's exposure to cash flow interest rate risk. Movements in market interest rates therefore impact the price of the securities (and hence their fair value measurement) however have a limited effect on the contractual cash flows of the securities.

Exposure to interest rate risk is monitored through several measures that include Value At Risk analysis, position limits, scenario testing, stress testing, and asset and liability matching using measures such as duration. Derivatives are used to manage interest rate risk. The interest rate risk arising from money market securities is managed using interest rate swaps and futures. For information regarding the notional contract amounts associated with these derivative financial instruments together with a maturity profile and reporting date fair values refer to the derivatives note.

The underwriting of general insurance contracts creates exposure to the risk that interest rate movements may materially impact the value of the insurance liabilities. Movements in interest rates should have minimal impact on the insurance profit due to the IAG Group's policy of investing in assets backing insurance liabilities principally in fixed interest securities matched to the expected payment pattern of the insurance liabilities. Movements in investment income on assets backing insurance liabilities offset the impact of movements in discount rates on the insurance liabilities, other than the changes in credit spreads on the fixed interest securities which are expected to reverse on maturity.

b. SENSITIVITY

The sensitivity analysis provided in the following table demonstrates the effect of a change in a key assumption while other assumptions remain unchanged. In reality, there is a correlation between the assumptions and other factors. The sensitivities do not include interdependencies among variables, but rather show isolated interest rate movements.

The investments in interest bearing securities are recognised on the balance sheet at fair value. Movements in market interest rates impact the price of the securities (and hence their fair value measurement) and so would impact profit. The impact from the measurement of the interest bearing securities held at reporting date of a change in interest rates at reporting date by +1% or -1% (e.g. a move from 4% to 5% or to 3%) on profit before tax, net of related derivatives, is shown in the table below.

		CONSOLIDATED	
		2010	2009
		\$m	\$m
		Impact to profit	Impact to profit
Investments—interest bearing securities and related interest rate derivatives	+1%	(252)	(194)
	-1%	276	205

The majority of the interest bearing securities are expected to be held to maturity and so movements in the fair value are expected to reverse upon maturity of the instruments.

III. Price risk

a. NATURE OF THE RISK AND HOW MANAGED

Price risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market prices (other than those arising from interest rate or currency risk), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting all similar financial instruments traded on the market. The IAG Group has significant exposure to equity price risk.

The IAG Group is exposed to equity price risk through its investment in equities (both directly and through certain trusts) and the use of equity related derivative contracts.

Exposure to equity price risk is monitored through several measures that include Value At Risk analysis, position limits, scenario testing, and stress testing. The exposure is actively managed against a broad equity market index utilising the experience of a small number of external fund managers. For information regarding the notional contract amounts associated with these derivative financial instruments together with a maturity profile and reporting date fair values refer to the derivatives note.

b. SENSITIVITY

The impact from the measurement of the investments held at reporting date of a change in equity values at reporting date by +10% or -10% on profit before tax, net of related derivatives, is shown in the table below.

		CONSOLIDATED	
		2010	2009
		\$m	\$m
Investments—equity and trust securities, and related equity derivatives	+10%	109	58
	-10%	(109)	(58)

All equity investments are measured at fair value through profit and so there would be no direct impact to equity from those movements.

B. CREDIT RISK

I. Nature of the risk and how managed

Credit risk is the risk of loss from a counterparty failing to meet their financial obligations. The IAG Group credit risk arises predominantly from investment activities, reinsurance activities and dealings with intermediaries. The IAG Group credit quality management roles, principles and processes are detailed in the IAG Group Credit Risk Management Policy document which is approved by the IAG Board and complies with APRA's guidance of credit risk management by licensed general insurers and insurance groups. 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 IAG Group.

The IAG Group Treasury function is responsible for ensuring that the policies governing the management of credit quality risk are properly implemented. The IAG Group's credit risk appetite relies heavily on credit rating agency research and is predominantly weighted towards counterparties of high quality investment grade. All new, changed and continuing credit risk exposures must be approved in accordance with the IAG Group's approval authority framework.

Concentrations of credit risk exist if a number of counterparties have similar economic characteristics. At the reporting date, there are no material concentrations of credit risk as the Consolidated entity transacts with a large number of counterparties in various regions without any individual counterparty having a material outstanding balance, except for possible exposure to four major banks in Australia. The level of reinsurance cover entered into with individual reinsurers is sufficiently diversified so as to avoid a concentration charge in the regulatory capital calculation (refer to the capital management note).

II. Credit risk exposure

a. PREMIUM AND REINSURANCE RECOVERIES ON PAID CLAIMS RECEIVABLE

The maximum exposure to credit risk as at reporting date is the carrying amounts of the receivables on balance sheet.

An ageing analysis for certain receivables balances is provided here. The other trade debtors provision of \$5 million (2009—\$9 million) represents specific provisions in an Australian subsidiary that relate to balances overdue more than one year. The other receivables balances not included below have either no overdue amounts or an immaterial portion of overdue amounts. The amounts are aged according to their original due date. Receivables for which repayment terms have been renegotiated represent an immaterial portion of the balances.

	NOT OVERDUE	<30 DAYS	30-120 DAYS	OVERDUE >120 DAYS	TOTAL
	\$m	\$m	\$m	\$m	\$m
Premium receivable	1,615	246	205	18	2,084
Provision for impairment—specific	(14)	(14)	(2)	(5)	(35)
Provision for impairment—collective	—	—	—	(3)	(3)
Net balance	1,601	232	203	10	2,046
Reinsurance recoveries on paid claims	121	36	39	9	205
Net balance	121	36	39	9	205

The majority of the premium receivable balance relates to policies which are paid on a monthly instalment basis. It is important to note that 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 is reversed.

The total provision for impairment at reporting date for receivables balances totalled \$41 million (2009—\$32 million). The net movement in the aggregated provision for the current period was \$9 million (2009—\$5 million).

b. REINSURANCE RECOVERIES RECEIVABLE ON OUTSTANDING CLAIMS

Reinsurance arrangements mitigate insurance risk but expose the IAG Group to credit risk. Reinsurance is placed with companies based on an evaluation of the financial strength of the reinsurers, terms of coverage, and price. The IAG Group has clearly defined credit 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 to the Consolidated entity under respective existing and future reinsurance contracts. Some of the reinsurers are domiciled outside of the jurisdictions in which the Company operates and so there is the potential for additional risk such as country risk and transfer risk.

The level and quality of reinsurance protection is an important element in understanding the financial strength of an insurer. The financial condition of a reinsurer is a critical deciding factor when entering into a reinsurance agreement. There is limited value in purchasing reinsurance protection from a reinsurer when that reinsurer may be unable to meet its payment obligations upon submission of a claim. The longer the tail of the direct insurance, the more important is the credit rating of the reinsurer.

It is IAG Group policy to only deal with reinsurers with credit ratings of at least Standard & Poor's BBB+ (or other rating agency equivalent) without collateralisation. Exposure to BBB+ rated reinsurers is limited to 1.5% of the capital base. Where IAG acquires a business a transition period is used for implementation of this policy. 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 have deposited funds equivalent to their participation in a trust fund. The counterparty credit profile of the catastrophe reinsurance program currently stands with more than 85% of the limit for the 2010 program with parties rated by Standard & Poor's as A+ or better. For long-tail reinsurance arrangements 100% of the program is placed with parties rated by Standard & Poor's as A+ or better.

Having reinsurance protection with strong reinsurers also benefits the Consolidated entity in its regulatory capital calculations. The risk charges vary with the grade of the reinsurers such that higher credit quality reinsurance counterparties incur lower APRA regulatory capital charges.

The following table provides information regarding the credit risk relating to the reinsurance and recoveries receivable on outstanding claims balance based on Standard & Poor's counterparty credit ratings. These rating allocations relate to balances accumulated from reinsurance programs in place over a number of years and so will not necessarily align with the rating allocations noted above for the current program.

CREDIT RATING	CONSOLIDATED	
	2010	2009
	%	%
AAA	1	5
AA	43	38
A	51	44
BBB and below	5	13
	100	100

No separate provision for impairment has been recognised for the reinsurance recoveries on outstanding claims balances. The actuarial estimates include a credit risk component in the underlying balance and therefore no separate provision is required.

Of these, approximately \$88 million is secured directly by deposits held in trust which reduces the credit risk.

c. INVESTMENTS

The IAG Group is exposed to credit risk from investments in third parties where the IAG Group holds debt and similar securities issued by those companies.

The credit risk relating to investments is monitored and assessed, and maximum exposures are limited. The maximum exposure to credit risk as at reporting date is the carrying amounts of the investments on the balance sheet as they are measured at fair value. The investments comprising assets backing insurance liabilities are restricted to investment grade securities.

The following table provides information regarding the credit risk relating to the interest bearing investments based on Standard & Poor's counterparty credit ratings.

AAA	50	48
AA	45	46
A	2	5
BBB and below	3	1
Total	100	100

C. LIQUIDITY RISK

I. Nature of the risk and how managed

Liquidity risk is concerned with the risk of there being insufficient cash resources to meet payment obligations without affecting the daily operations or the financial condition of the Consolidated entity. Liquidity facilitates the ability to meet expected and unexpected requirements for cash. The liquidity position is derived from operating cash flows, investment portfolios and access to outside sources of liquidity such as bank lines of credit, established debt funding programs, reinsurance arrangements and other sources. The liquidity management roles, principles and processes are detailed in the IAG Group Liquidity Risk Management Policy document which is approved by the IAG Board. The policy outlines the framework and procedures in place to ensure an adequate and appropriate level of monitoring and management of liquidity.

Underwriting insurance contracts expose the IAG Group to liquidity risk through the obligation to make payments of unknown amount on unknown dates. The assets backing insurance liabilities consist predominantly of government securities (the most liquid of securities) and other very high quality securities which can generally be readily sold or exchanged for cash. The assets are managed so as to effectively match the maturity profile of the assets with the expected pattern of claims payments. The debt securities are restricted to investment grade securities with concentrations of investments managed by various criteria including issuer, industry, geography and credit rating. The proportion, by market value, of the portfolio of assets backing insurance liabilities invested in high quality liquid assets for each general insurer must exceed 35% of the portfolio balance. There is a transition period for newly acquired businesses to comply with these policies.

A significant source of liquidity risk for the IAG Group relates to interest bearing liabilities. The management of this risk includes the issuance of a range of interest bearing liabilities denominated in different currencies with different maturities.

II. Liquidity risk exposure

a. OUTSTANDING CLAIMS LIABILITY AND INVESTMENTS

The breakdowns of the fixed term investments are provided by contractual maturity. Actual maturities may differ from contractual maturities because certain counterparties have the right to call or prepay certain obligations with or without call or prepayment penalties.

A maturity analysis of the estimated net discounted outstanding claims liability based on the remaining term to payment at the reporting date and the investments that have fixed term is provided in the table below.

This maturity profile is a key tool used in the investment of assets backing insurance liabilities in accordance with the policy of matching the maturity profile of the assets with the estimated pattern of claims payments.

MATURITY ANALYSIS	NET DISCOUNTED OUTSTANDING CLAIMS LIABILITY		INVESTMENTS	
	2010	2009	2010	2009
	\$m	\$m	\$m	\$m
Floating interest rate (at call)	–	–	605	944
Within 1 year or less	2,497	2,409	2,094	1,835
Within 1 to 2 years	1,161	1,067	1,537	2,577
Within 2 to 3 years	881	817	2,887	1,923
Within 3 to 4 years	634	568	773	1,515
Within 4 to 5 years	414	390	1,375	371
Over 5 years	1,178	1,154	1,302	800
Total	6,765	6,405	10,573	9,965

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 undiscounted cash flows. All of the liabilities have call or reset dates which occur prior to any contractual maturity.

	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
2010							
Tier 1 regulatory capital ^(a)	900	–	–	–	–	900	900
Tier 2 regulatory capital ^(a)	541	–	–	–	541	–	541
Contractual undiscounted interest payments ^(b)		81	81	243	–	–	405
Total contractual undiscounted payments		81	81	243	541	900	1,846
2009							
Tier 1 regulatory capital ^{(a), (c)}	350	–	–	–	–	350	350
Tier 2 regulatory capital ^(a)	707	111	–	–	596	–	707
Contractual undiscounted interest payments ^(b)		66	53	128	–	–	247
Total contractual undiscounted payments		177	53	128	596	350	1,304

(a) These liabilities have call or reset dates upon which certain terms, including the interest or distribution rate, can be changed. The detailed descriptions of the instruments are provided in section C of the interest bearing liabilities note.

(b) Contractual undiscounted interest payments are 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. Reporting date exchange rates have been used for interest projections for liabilities in foreign currencies.

(c) These liabilities are liabilities of the Parent.

c. FINANCING FACILITIES

There are financing facilities set up to manage the liquidity of the IAG Group. Information regarding access to unutilised credit facilities is provided below.

	TABLE NOTE	CONSOLIDATED			
		Facilities drawn at reporting date		Facilities available	
		2010	2009	2010	2009
		\$m	\$m	\$m	\$m
Standby letter of credit facilities	A	59	61	60	66
Debt issuance program		-	-	750	750

Various entities within the Consolidated entity have other financing facilities outstanding with external service providers, mostly banks, providing short term financing arrangements for specific situations not significant to the Consolidated entity including standby letters of credit, and guarantees for lease guarantees and performance bonds.

Table notes

A The standby letter of credit facilities are denominated in US dollars and are translated into equivalent Australian dollars using the reporting date exchange rate. The majority of the amount shown relates to a standby letter of credit issued in support of the Consolidated entity's participation in Lloyd's of London.

NOTE 5. ANALYSIS OF INCOME

	PARENT		CONSOLIDATED	
	2010	2009	2010	2009
	\$m	\$m	\$m	\$m
A. GENERAL INSURANCE REVENUE				
Gross written premium	-	-	7,782	7,842
Movement in unearned premium liability	-	-	(161)	(124)
Premium revenue	-	-	7,621	7,718
Direct premium revenue	-	-	7,610	7,695
Inwards reinsurance premium revenue	-	-	11	23
Premium revenue	-	-	7,621	7,718
Reinsurance and other recoveries revenue	-	-	826	696
Total general insurance revenue	-	-	8,447	8,414
B. INVESTMENT INCOME				
Dividend revenue	327	218	24	28
Interest revenue	32	37	538	470
Trust revenue	-	-	8	78
Total investment revenue	359	255	570	576
Net changes in fair values of investments				
Realised net gains and (losses)	(1)	(1)	227	100
Unrealised net gains and (losses)	-	1	(23)	63
Total investment income	358	255	774	739
Represented by				
Investment income on assets backing insurance liabilities	-	-	574	795
Investment income on equity holders' funds	358	255	200	(56)
	358	255	774	739
C. FEE AND OTHER INCOME				
Fee based revenue	-	-	147	170
Brokerage and commission	-	-	33	75
Other income	-	70	76	158
Unrealised gains/(losses) on embedded derivatives	(96)	27	(96)	27
Total fee and other income	(96)	97	160	430
D. SHARE OF NET PROFIT/(LOSS) OF ASSOCIATES				
	-	-	3	8
Total income	262	352	9,384	9,591

NOTE 6. ANALYSIS OF EXPENSES

	2010	PARENT 2009	CONSOLIDATED 2010	2009
	\$m	\$m	\$m	\$m
A. EXPENSES AS PRESENTED IN THE STATEMENT OF COMPREHENSIVE INCOME				
Outwards reinsurance premium expense	–	–	556	485
Claims expense	–	–	5,898	6,066
Acquisition costs	–	–	1,054	1,213
Other underwriting expenses	–	–	761	680
Fire services levies	–	–	239	235
Investment expenses on assets backing insurance liabilities	–	–	20	15
Finance costs	37	50	88	87
Net income attributable to non-controlling interests in unitholders' funds	–	–	7	2
Fee based, corporate and other expenses	–	–	359	496
Total expenses	37	50	8,982	9,279
B. ANALYSIS OF EXPENSES BY FUNCTION				
General insurance business expenses	–	–	8,528	8,694
Fee based business expenses	–	–	172	166
Investment and other expenses	–	–	19	21
Corporate and administration expenses	37	50	263	398
Total expenses	37	50	8,982	9,279
C. OTHER ITEMS				
Disclosure of the following items is considered relevant in explaining the results for the financial year:				
I. Depreciation and amortisation				
Acquired intangible assets	–	–	26	47
Capitalised software development expenditure	–	–	24	29
Property and equipment	–	–	51	61
	–	–	101	137
II. Impairment charges				
Goodwill	–	–	50	–
Acquired intangible assets	–	–	37	18
Trade and other receivables	–	–	–	5
	–	–	87	23
III. Employee benefits				
Defined contribution superannuation plans	–	–	79	84
Defined benefit superannuation plans	–	–	14	6
Share based remuneration	–	–	25	17
Salaries and other employee benefits expense	–	–	945	1,115
	–	–	1,063	1,222
IV. Transfers to provisions charged to profit or loss				
Restructuring provision	–	–	16	43
	–	–	16	43
V. Finance costs				
Reset preference shares distributions paid/payable	20	20	20	20
Subordinated term notes interest paid/payable	14	26	43	50
Reset exchangeable securities	–	–	17	–
Other debts of operational nature, interest paid/payable*	2	2	2	16
Ineffective portion of hedges	–	–	–	(2)
Amortisation of capitalised transaction costs	1	2	6	3
	37	50	88	87

* The balance for prior year included an amount of \$13 million representing the movement of the fair value of derivatives related to USD subordinated term notes. The fair value movement was recognised as finance costs in the statement of comprehensive income. No such movement was recognised for the current year as the derivatives matured when the USD subordinated term notes were redeemed on 28 April 2010.

	2010	PARENT 2009	CONSOLIDATED 2010	2009
	\$m	\$m	\$m	\$m
VI. Other				
Operating lease payments	-	-	154	172
Software research and development costs	-	-	59	62
Net foreign exchange (gains)/losses	-	-	(20)	(22)
Liability adequacy test deficiency	-	-	16	50
Insurance protection tax levied by the NSW State Government	-	-	20	20
Net loss on disposal of property and equipment	-	-	-	1

NOTE 7. REMUNERATION OF AUDITORS

	2010	CONSOLIDATED 2009
	\$000	\$000
A. KPMG AUSTRALIA		
I. Assurance services		
Audit of the financial statements prepared for the Parent and subsidiaries	4,903	4,753
Audit of statutory returns in accordance with regulatory requirements	811	831
Other assurance services	595	69
	6,309	5,653
II. Advisory services		
Taxation services	839	626
Due diligence	200	58
Other attestation and advisory	-	68
	1,039	752
B. OVERSEAS RELATED PRACTICES OF KPMG AUSTRALIA		
I. Assurance services		
Audit of the financial statements prepared for subsidiaries	2,936	2,643
Audit of statutory returns in accordance with regulatory requirements	145	186
Other assurance services	57	43
	3,138	2,872
II. Advisory services		
	122	212
C. OTHER AUDITORS		
I. Assurance services		
Audit of the financial statements prepared for subsidiaries	3	70
II. Advisory services		
	10	34
Total remuneration of auditors	10,621	9,593

It is the IAG Group's policy that KPMG may provide assurance and other audit related services that, while outside the scope of the statutory audit, are consistent with the role of auditor. These include regulatory and prudential reviews requested by a regulator such as APRA. KPMG may not provide services that are perceived to be materially in conflict with the role of auditor. It is IAG Group policy to contract KPMG on assignments additional to their statutory audit and assurance duties where KPMG's expertise and experience with the IAG Group are important. The total fees for such services cannot exceed the audit fees without the approval of the IAG Audit, Risk Management & Compliance Committee and KPMG can be contracted only in relation to reviewing financial information and not in its preparation. The IAG Board is of the opinion that audit independence was not impaired during the current financial year as a result of the provision of these services.

NOTE 8. INCOME TAX

	2010	PARENT 2009	CONSOLIDATED 2010	2009
	\$m	\$m	\$m	\$m
A. INCOME TAX EXPENSE				
Current tax	2	27	149	44
Deferred tax	2	(25)	68	23
(Over)/under provided in prior year	–	(2)	(5)	(2)
Income tax expense/(credit)	4	–	212	65
Deferred income tax expense/(credit) included in income tax comprises				
(Increase)/decrease in deferred tax assets	2	(25)	70	(14)
Increase/(decrease) in deferred tax liabilities	–	–	(2)	37
	2	(25)	68	23
B. INCOME TAX RECONCILIATION				
The income tax for the financial year differs from the amount calculated on the profit/(loss) before income tax. The differences are reconciled as follows:				
Profit/(loss) for the year before income tax	225	302	402	312
Income tax calculated at 30% (2009—30%)	68	91	121	94
Amounts which are not deductible/(taxable) in calculating taxable income				
Rebateable dividends	(99)	(66)	(4)	(2)
Capital profits/(losses) not subject to income tax	–	(21)	(5)	(17)
Deferred tax asset on tax loss (UK) not recognised in current year	–	–	109	–
Deferred tax asset written off in current year	–	–	54	–
Foreign exchange gains not subject to income tax	–	–	(119)	–
Amortisation and impairment charge on acquired intangible assets and goodwill	–	–	34	19
Interest on reset preference shares	6	6	6	6
Realised (gains) and losses on embedded derivatives	29	(8)	29	(8)
Other	–	–	(8)	(25)
Income tax expense/(credit) applicable to current year	4	2	217	67
Adjustment relating to prior year	–	(2)	(5)	(2)
Income tax expense/(credit) attributable to profit/(loss) for the year before impact of tax consolidation	4	–	212	65
Income tax expense/(credit) attributable to profit/(loss) for the year after impact of tax consolidation	4	–	212	65
C. TAX CONSOLIDATION				
The Company, being the head entity, formed a tax-consolidated group comprising the Company and all of its Australian wholly owned subsidiaries and the accounting treatment is applied in accordance with the relevant accounting standards.				

	2010	PARENT 2009	CONSOLIDATED 2010	2009
	\$m	\$m	\$m	\$m
D. DEFERRED TAX ASSETS				
I. Composition				
a. AMOUNTS RECOGNISED IN PROFIT				
Property and equipment	–	–	43	70
Employee benefits	–	–	65	71
Insurance provisions	–	–	122	145
Investments	–	–	12	32
Provisions	–	–	10	5
Tax losses	71	27	71	81
Other	–	–	10	–
	71	27	333	404
b. AMOUNTS RECOGNISED DIRECTLY IN OTHER COMPREHENSIVE INCOME				
Defined benefit superannuation plans	–	–	14	18
Other	–	3	–	4
	71	30	347	426
c. AMOUNTS SET-OFF AGAINST DEFERRED TAX LIABILITIES				
	–	–	(45)	(44)
	71	30	302	382
II. Reconciliation of movements				
Balance at the beginning of the financial year	30	7	426	380
Credited/(charged) to profit or loss	(2)	25	(70)	14
Credited/(charged) to equity	(3)	(3)	(8)	24
Transfers	46	–	–	6
Adjustments relating to prior year	–	1	9	(1)
Foreign exchange differences	–	–	(10)	3
Balance at the end of the financial year prior to set-off	71	30	347	426
III. Tax losses				
The Consolidated entity has not recognised \$201 million of UK tax losses (2009—\$25 million).				
E. DEFERRED TAX LIABILITIES				
I. Composition				
a. AMOUNTS RECOGNISED IN PROFIT				
Investments	–	–	45	34
Other	–	–	24	32
	–	–	69	66
b. AMOUNTS RECOGNISED DIRECTLY IN OTHER COMPREHENSIVE INCOME				
Hedges	–	–	11	17
	–	–	80	83
c. AMOUNTS SET-OFF AGAINST DEFERRED TAX ASSETS				
	–	–	(45)	(44)
	–	–	35	39
II. Reconciliation of movements				
Balance at the beginning of the financial year	–	–	83	109
Charged/(credited) to profit or loss	–	–	(2)	37
Charged/(credited) to equity	–	–	(6)	(90)
Foreign exchange differences	–	–	(3)	–
Transfers	–	–	–	6
Adjustments relating to prior year	–	–	8	21
Balance at the end of the financial year prior to set-off	–	–	80	83

NOTE 9. SEGMENT REPORTING

The Consolidated entity operates in the Australia, New Zealand, United Kingdom and Asia (principally Thailand) general insurance industries. In Australia, the financial results are generated from three different divisions being Australia direct insurance, Australia intermediated insurance and Corporate and other.

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

The operating segments are identified by the management based on the manner in which the insurance products are underwritten and the related services provided to customers through the various distribution channels in various countries. Discrete financial information about each of these operating segments is reported to the Chief Executive Officer on a monthly basis.

The reportable segments are based on aggregated operating segments as these are the sources of the Consolidated entity's major risks and have the most effect on the rates of return.

The reportable segments comprise the following business divisions.

A. AUSTRALIA DIRECT INSURANCE

This segment comprises insurance products distributed through a network of branches, franchises and country service centres throughout Australia as well as call centres and online facilities using predominantly the NRMA Insurance, SGIO and SGIC brands as well as via a distribution relationship and underwriting joint venture with RACV Ltd. The recently launched internet brand, The Buzz, is included in this segment.

B. AUSTRALIA INTERMEDIATED INSURANCE

This segment comprises insurance products primarily sold under the CGU and Swann insurance brands through insurance brokers, authorised representatives and distribution partners.

C. NEW ZEALAND INSURANCE

This segment comprises the general insurance business underwritten through subsidiaries in New Zealand. The insurance products are predominantly sold directly to customers using the State brand, and through intermediaries such as brokers and agents using the NZI brand. Personal and commercial products are also distributed by corporate partners, such as large financial institutions, using third party brands.

D. UNITED KINGDOM INSURANCE

This segment comprises the general insurance underwriting and broker distribution services operating through subsidiaries in the United Kingdom. The underwriting business, Equity Red Star operates through a Lloyd's syndicate. The United Kingdom non-core mass market distribution businesses that were sold during the second half of the prior financial year formed part of this segment until divestment.

E. ASIA INSURANCE

This segment comprises primarily the direct insurance business underwritten through subsidiaries in Thailand and the share of the operating result from the investment in associates in Malaysia and India (a newly acquired associate company which commenced underwriting insurance contracts in March 2010). The businesses offer personal and commercial insurance products through local brands.

F. CORPORATE AND OTHER

This segment comprises other activities, including corporate services, funding costs on the IAG Group's interest bearing liabilities, inwards reinsurance from associates, investment management and investment of the equity holders' funds. The results of the run off of the Alba Group are also included in this segment.

The net outstanding claims liability for each segment includes an allocation of the diversification benefit incorporated into the risk margin relating to the combination of the segments at the Consolidated entity level.

There are no differences between the recognition and measurement criteria used in the segment disclosures and those used in the financial statements.

CONSOLIDATED	AUSTRALIA DIRECT INSURANCE	AUSTRALIA INTER- MEDIATED INSURANCE	NEW ZEALAND INSURANCE	UNITED KINGDOM INSURANCE	ASIA INSURANCE	CORPORATE AND OTHER	TOTAL
	\$m	\$m	\$m	\$m	\$m	\$m	\$m
2010							
External revenue	4,458	2,814	998	795	199	120	9,384
Total revenue	4,458	2,814	998	795	199	120	9,384
Underwriting profit/(loss)	259	(78)	115	(361)	(3)	7	(61)
Investment income net of investment fees—technical reserves	310	217	16	6	5	–	554
Insurance profit/(loss)	569	139	131	(355)	2	7	493
Investment income net of investment fees—equity holders' funds	–	–	–	–	–	96	96
Share of net profit/(loss) of associates	–	–	–	–	3	–	3
Finance costs	–	–	–	–	–	(88)	(88)
Other net operating result	–	9	1	(3)	–	(109)	(102)
Profit/(loss) before income tax	569	148	132	(358)	5	(94)	402
Income tax expense							(212)
Profit/(loss) for the year							190
Segment assets	5,466	3,987	701	1,122	234	8,936	20,446
Total assets							20,446
Segment liabilities	5,466	3,987	701	1,122	234	4,280	15,790
Total liabilities							15,790
Acquisitions of property and equipment, intangibles and other non-current segment assets	–	–	–	–	–	116	116
Depreciation expense	30	4	6	3	2	6	51
Amortisation and impairment charges on acquired intangibles and goodwill	7	6	9	115	–	–	137
Total depreciation and amortisation expense	37	10	15	118	2	6	188
Other non cash expenses	38	14	7	5	–	10	74
2009							
External revenue	4,086	3,020	990	1,231	228	36	9,591
Total revenue	4,086	3,020	990	1,231	228	36	9,591
Underwriting profit/(loss)	(21)	(252)	(24)	32	4	(4)	(265)
Investment income net of investment fees—technical reserves	394	300	24	57	5	–	780
Insurance profit/(loss)	373	48	–	89	9	(4)	515
Investment income net of investment fees—equity holders' funds	–	–	–	–	–	(39)	(39)
Share of net profit/(loss) of associates	–	–	–	(2)	10	–	8
Finance costs	–	–	–	–	–	(87)	(87)
Other net operating result	–	18	1	(13)	(4)	(87)	(85)
Profit/(loss) before income tax	373	66	1	74	15	(217)	312
Income tax expense							(65)
Profit/(loss) for the year							247
Segment assets	5,816	4,310	727	1,000	159	7,348	19,360
Total assets							19,360
Segment liabilities	5,816	4,310	727	1,000	159	2,512	14,524
Total liabilities							14,524
Acquisitions of property and equipment, intangibles and other non-current segment assets	–	–	–	–	–	161	161
Depreciation expense	34	5	5	8	2	7	61
Amortisation and impairment charges on acquired intangibles and goodwill	9	5	11	63	–	6	94
Total depreciation and amortisation expense	43	10	16	71	2	13	155
Other non cash expenses	59	25	8	19	–	12	123

NOTE 10. EARNINGS PER SHARE

	CONSOLIDATED	
	2010	2009
	cents	cents
A. REPORTING PERIOD VALUES		
Basic earnings per ordinary share*	4.39	9.32
Diluted earnings per ordinary share	4.36	9.26

* The basic earnings per ordinary share excludes the treasury shares held in trust from the denominator of the calculation, but includes earnings attributable to those shares in the numerator, to comply with AASB 133 Earnings per Share. If the amounts relating to those shares are excluded from both the numerator and denominator, the basic earnings per ordinary share for the current reporting period would be reduced to 4.36 cents (2009—9.26 cents).

	CONSOLIDATED	
	2010	2009
	\$m	\$m
B. RECONCILIATION OF EARNINGS USED IN CALCULATING EARNINGS PER SHARE		
Profit/(loss) for the year	190	247
Profit attributable to non-controlling interests	(99)	(66)
Profit/(loss) attributable to equity holders of the Parent which is used in calculating basic and diluted earnings per share	91	181

	CONSOLIDATED	
	2010	2009
	Number of shares in millions	Number of shares in millions
C. RECONCILIATION OF WEIGHTED AVERAGE NUMBER OF ORDINARY SHARES USED IN CALCULATING EARNINGS PER SHARE		
Ordinary shares on issue*	2,077	1,961
Treasury shares held in trust	(12)	(13)
Weighted average number of ordinary shares used in the calculation of basic earnings per share	2,065	1,948
Weighted average number of dilutive potential ordinary shares relating to		
Unvested share based remuneration rights supported by treasury shares held in trust	12	13
Weighted average number of ordinary shares used in the calculation of diluted earnings per share	2,077	1,961

* The weighted average number of ordinary shares used to calculate the basic earnings per share in 2009 includes an additional 23 million shares that are deemed to be bonus shares. These deemed bonus shares were issued in response to the share purchase plan and institutional placement. These deemed bonus shares are considered to have been issued on 1 July 2007 (being at the beginning of the corresponding prior period presented in these financial statements) and thus have a retrospective dilutive effect on the basic earnings per share.

The following matter is relevant to the determination of the weighted average number of ordinary shares:

- the reset preference shares, the reset exchangeable securities and the GBP subordinated exchangeable term notes are not included as dilutive potential ordinary shares even though they may convert into ordinary shares because the contingent conversion conditions were not met at the reporting date.

NOTE 11. DIVIDENDS

	CENTS PER SHARE	TOTAL AMOUNT	PAYMENT DATE	TAX RATE FOR FRANKING CREDIT	PERCENTAGE FRANKED
		\$m			
A. ORDINARY SHARES					
2010					
2010 interim dividend	8.5	177	12 April 2010	30%	100%
2009 final dividend	6.0	124	2 October 2009	30%	100%
		301			
2009					
2009 interim dividend	4.0	76	8 April 2009	30%	100%
2008 final dividend	9.0	169	3 October 2008	30%	100%
		245			

It is standard practice that the IAG Board determine to pay the dividend for a period after the relevant reporting date. In accordance with the relevant accounting policy (refer to section AD of the summary of significant accounting policies note) a dividend is not accrued for until it is determined to pay and so the dividends for a period are generally recognised and measured in the financial reporting period following the period to which the dividend relates.

The dividends recognised in the current reporting period include \$Nil (2009—\$1 million) paid in relation to treasury shares held in trusts controlled by the Consolidated entity.

B. DIVIDEND REINVESTMENT

A Dividend Reinvestment Plan (DRP) operates which allows equity holders to elect to receive their dividend entitlement in the form of IAG shares. The price of DRP shares is the average share market price, less a discount if any (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.

The DRP for the 2010 interim dividend payable on 12 April 2010 was settled with the on market purchase of 9.3 million shares priced at \$3.9601 per share (based on a daily volume weighted average price for 10 trading days from 15 March 2010 to 26 March 2010 inclusive, with no discount applied).

The DRP for the 2009 final dividend payable on 2 October 2009 was settled with the issuance of 7.6 million fully paid ordinary shares priced at \$3.6199 per share (based on the average market price for the five trading days from 7 September 2009 to 11 September 2009 inclusive, with no discount applied) to existing shareholders with dividend entitlements.

A copy of the terms and conditions for the IAG Group DRP is available at www.iag.com.au/shareholder.

C. DIVIDEND NOT RECOGNISED AT REPORTING DATE

In addition to the above dividends, the IAG Board determined to pay the following dividend after the reporting date but before finalisation of this financial report and it has not been recognised in this financial report.

	CENTS PER SHARE	TOTAL AMOUNT	EXPECTED PAYMENT DATE	TAX RATE FOR FRANKING CREDIT	PERCENTAGE FRANKED
		\$m			
2010 final dividend	4.5	94	6 October 2010	30%	100%

On 26 August 2010 the IAG Board determined the final dividend will be payable to shareholders as at 5pm on 8 September 2010.

The Company's DRP will operate by issuing ordinary shares to participants by acquiring shares on market with an issue price per share of the average market price as defined in DRP terms with no discount applied. The last election notice for participation in the DRP in relation to this final dividend is 8 September 2010.

D. HISTORICAL SUMMARY

The table below provides a historical summary of dividend payments (cents per share) since the IAG Group listed in 2000, aggregating dividends based on the financial period for which they were declared and not the financial period in which they were recognised and paid.

	YEAR ENDED 30 JUNE 2001	YEAR ENDED 30 JUNE 2002	YEAR ENDED 30 JUNE 2003	YEAR ENDED 30 JUNE 2004	YEAR ENDED 30 JUNE 2005	YEAR ENDED 30 JUNE 2006	YEAR ENDED 30 JUNE 2007	YEAR ENDED 30 JUNE 2008	YEAR ENDED 30 JUNE 2009	YEAR ENDED 30 JUNE 2010
Interim dividend	4.0	4.5	4.5	8.0	12.0	13.5	13.5	13.5	4.0	8.5
Final dividend	6.0	6.0	7.0	14.0	14.5	16.0	16.0	9.0	6.0	4.5
Special dividend	–	–	–	–	–	12.5	–	–	–	–

E. DIVIDEND POLICY

The IAG Group's dividend policy is intended to pay dividends equivalent to 50%–70% of reported cash earnings. Cash earnings are defined as:

- net profit after tax attributable to IAG shareholders;
- plus amortisation of acquired identifiable intangible assets; and
- excluding any unusual items.

F. 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 generally being limited to profits subject to ongoing solvency obligations noting that under the Australian Prudential Regulation Authority (APRA) Level 2 insurance group supervision requirements, IAG is required to obtain approval from APRA before payment of dividends on ordinary shares that exceeds the IAG 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 reset preference shares or reset exchangeable securities or GBP subordinated exchangeable term notes, unless certain actions are taken by IAG. For further details refer to the interest bearing liabilities note.

There are currently no restrictions on the payment of dividends from subsidiaries to the Parent other than:

- the payment of dividends generally being limited to profits subject to ongoing solvency obligations of the subsidiary;
- for certain subsidiaries which are required to meet the statutory reserve and regulatory minimum capital requirements. In particular, APRA has advised Australian general insurers that a general insurer under its supervision must obtain approval from it before declaring a dividend if the general insurer has incurred a loss, or proposes to pay dividends which exceed the level of profits earned in the current period; and
- the Lloyd's syndicate operations being subject to specific solvency calculation restrictions regarding the payment of distributions from Funds at Lloyd's.

	2010	PARENT 2009	CONSOLIDATED 2010	2009
	\$m	\$m	\$m	\$m
G. DIVIDEND FRANKING AMOUNT				
Amount of franking credits available for subsequent reporting periods				
Franking account balance at reporting date at 30%	385	491	415	540
Franking credits to arise from payment of income tax payable	–	1	43	16
Franking debits to arise from receipt of income tax refundable	–	(49)	–	(49)
Franking credits to arise from receipt of dividends receivable	1	–	1	1
Franking credits available for future reporting periods	386	443	459	508
Franking account impact of dividends determined before issuance of financial report but not recognised at reporting date	(40)	(53)	(40)	(53)
Franking credits available for subsequent financial periods based on a tax rate of 30%	346	390	419	455

After payment of the final dividend the franking balance of the Company is capable of fully franking a further \$807 million distributions.

The balance of the franking account arises from:

- franked income received or recognised as a receivable at the reporting date;
- income tax paid, after adjusting for any franking credits which will arise from the payment of income tax provided for in the financial statements; and
- franking debits from the payment of dividends recognised as a liability at the reporting date.

In accordance with the tax consolidation legislation, the Parent, as the head entity in the tax-consolidated group, has also assumed the benefit of the franking credits available. The consolidated amounts include franking credits that would be available to the Parent if distributable profits of non-wholly owned subsidiaries were paid as dividends.

All of the distributions paid in relation to the reset preference shares and the interest payments in relation to the reset exchangeable securities for the financial year were fully franked at 30% (2009—fully franked at 30%).

NOTE 12. CLAIMS

	CONSOLIDATED	
	2010	2009
	\$m	\$m
A. NET CLAIMS EXPENSE		
Direct business	5,088	5,366
Inwards reinsurance business	(16)	4
Net claims expense	5,072	5,370

B. CLAIMS DEVELOPMENT**I. Net claims expense recognised in the statement of comprehensive income**

Given the uncertainty in establishing the outstanding claims liability, it is likely that the final outcome will be different from the original liability established. Claims development refers to the financial adjustment in the current period relating to claims incurred in previous periods because of new and more up to date information that has become available and to reflect changes in inflation and discount assumptions. The information is presented on an accident year basis (claims are related to the period in which the insured event occurred and not the period in which the policy was underwritten).

	CONSOLIDATED					
	2010			2009		
	Current year	Prior years	Total	Current year	Prior years	Total
	\$m	\$m	\$m	\$m	\$m	\$m
Gross claims—undiscounted	6,380	(424)	5,956	6,565	(364)	6,201
Discount	(209)	151	(58)	(281)	146	(135)
Gross claims—discounted	6,171	(273)	5,898	6,284	(218)	6,066
Reinsurance and other recoveries—undiscounted	(954)	155	(799)	(867)	195	(672)
Discount	19	(46)	(27)	25	(49)	(24)
Reinsurance and other recoveries—discounted	(935)	109	(826)	(842)	146	(696)
Net claims expense	5,236	(164)	5,072	5,442	(72)	5,370

Current year claims relate to claim events that occurred in the current financial year. Prior year claims relate to a reassessment of the claim events that occurred in all previous financial periods. Historically, there have been significant prior year reserve releases.

II. Net outstanding claims liability recognised on the balance sheet

The following table shows the development of the estimated net undiscounted outstanding claims payments relative to the current estimate of ultimate claims payments as estimated at each reporting date. The table also shows a reconciliation of the net discounted outstanding claims liability to the gross outstanding claims liability on the balance sheet.

	CONSOLIDATED										
	Accident year										
	2001 and prior	2002	2003	2004	2005	2006	2007	2008	2009	2010	Total
	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
NET ULTIMATE CLAIMS PAYMENTS											
Development											
At end of accident year		3,217	3,355	3,496	3,608	4,000	4,695	4,596	4,617	4,603	
One year later		3,145	3,178	3,331	3,561	3,927	4,660	4,554	4,656		
Two years later		3,084	3,103	3,358	3,529	3,858	4,619	4,549			
Three years later		3,050	3,073	3,342	3,485	3,860	4,632				
Four years later		3,028	3,018	3,326	3,450	3,847					
Five years later		3,000	3,026	3,315	3,399						
Six years later		3,000	3,020	3,286							
Seven years later		2,980	3,008								
Eight years later		2,981									
Current estimate of net ultimate claims payments		2,981	3,008	3,286	3,399	3,847	4,632	4,549	4,656	4,603	
Cumulative payments made to date		(2,901)	(2,929)	(3,153)	(3,213)	(3,494)	(4,046)	(3,845)	(3,558)	(2,387)	
Net undiscounted outstanding claims payments	690	80	79	133	186	353	586	704	1,098	2,216	6,125
Discount to present value	(207)	(15)	(14)	(22)	(28)	(47)	(62)	(79)	(126)	(184)	(784)
Net discounted outstanding claims payments	483	65	65	111	158	306	524	625	972	2,032	5,341
Reconciliation											
Claims handling costs											325
Risk margin											1,099
											6,765
Gross outstanding claims liability on the balance sheet											8,253
Outstanding reinsurance and other recoveries											(1,071)
GST recoverable on net outstanding claims liability											(417)
Net outstanding claims liability											6,765

Favourable claims experience has given rise to the release of central estimates as the ultimate claims costs have been settled or become more certain.

Conditions and trends that have affected the development of the liabilities in the past may, or may not, occur in the future, and accordingly, conclusion about future results may not necessarily be derived from the information presented in the tables above.

Short-tail claims are normally reported soon after the incident and are generally settled within months following the reported incident. Hence any development on short-tail claims is normally limited to the year the incident occurred and the following year. For long-tail classes of business it can be several years before a claim is reported and settled, hence the original estimation involves greater uncertainty and so inherently there is more likely to be greater disparity between the original and current estimates. It is for these long-tail classes of business that the development of the outstanding claims liability generally occurs over a number of years.

Where an entity or business that includes outstanding claims liabilities has been acquired the claims costs for the acquired businesses are included in the claims development table from and including the year of acquisition.

The Consolidated entity conducts general insurance business in local currencies in foreign countries. The gross outstanding claims liability for international operations outside Australia includes contracts written in New Zealand dollars, British pounds, US dollars and Thai baht. The translation of the outstanding claims liabilities denominated in foreign currencies into Australian dollars over a number of reporting dates, includes exchange rate movements that have no bearing on the development of the measurement of the underlying claims. All payments not denominated in Australian dollars have been converted to Australian dollars using constant exchange rates being the rates as at the current reporting date to eliminate this factor and aid comparability.

The claims development table disclosed each period will not be directly reconcilable to the tables presented in previous periods with the key difference being the application of current reporting date exchange rates to the claims liability relating to all accident years.

	CONSOLIDATED	
	2010	2009
	\$m	\$m
C. COMPOSITION OF OUTSTANDING CLAIMS LIABILITY—GROSS, DISCOUNTED		
Expected future payment for claims incurred		
Central estimate	6,595	6,055
Claims handling costs	325	347
Risk margin	1,333	1,414
Outstanding claims liability	8,253	7,816

The outstanding claims liability includes \$5,073 million (2009—\$4,802 million) which is expected to be settled after more than 12 months from reporting date. The gross and net outstanding claims liability at the financial reporting date relating to the inwards reinsurance business was \$55 million (2009—\$74 million) and \$15 million (2009—\$29 million) respectively.

D. RECONCILIATION OF MOVEMENTS IN OUTSTANDING CLAIMS LIABILITY		
Outstanding claims liability at the beginning of the financial year—gross, discounted	7,816	7,827
Outstanding reinsurance and other recoveries at the beginning of the financial year (refer to note 13.A)	(1,047)	(1,104)
GST recoverable on net outstanding claims liability at the beginning of the financial year	(364)	(368)
Net outstanding claims liability at the beginning of the year	6,405	6,355
Risk margin at the beginning of the year	(1,026)	(1,011)
Net central estimate at the beginning of the year	5,379	5,344
Claims incurred in the current year	5,709	5,678
Reinsurance and other recoveries in the current year	(813)	(690)
Claims cost paid	(5,362)	(5,833)
Reinsurance and other recoveries received	684	774
Unwind of the discount	195	249
Development on prior year net central estimate	(106)	(197)
Movement in discounting	29	205
Movement in foreign currency exchange rates	(49)	13
Movement of net claims disposed through sale of businesses	–	(164)
Net central estimate at the end of the year	5,666	5,379
Risk margin at the end of the year	1,099	1,026
Net outstanding claims liability at the end of the year	6,765	6,405
Outstanding reinsurance and other recoveries at the end of the financial year (refer to note 13.A)	1,071	1,047
GST recoverable on net outstanding claims liability at the end of the financial year	417	364
Outstanding claims liability at the end of the financial year—gross, discounted	8,253	7,816
E. DISCOUNTING OF NET OUTSTANDING CLAIMS LIABILITY		
Net outstanding claims liability—undiscounted	8,055	7,704
Discount to present value	(1,290)	(1,299)
Net outstanding claims liability—discounted	6,765	6,405

F. MATURITY ANALYSIS

A maturity analysis of the estimated net discounted outstanding claims liability based on the remaining term to payment at the reporting date is provided in the table below. This maturity profile is a key tool used in the investment of assets backing insurance liabilities in accordance with the policy of matching the maturity profile of the assets with the estimated pattern of claims payments.

Within 1 year or less	2,497	2,409
Within 1 to 2 years	1,161	1,067
Within 2 to 3 years	881	817
Within 3 to 4 years	634	568
Within 4 to 5 years	414	390
Over 5 years	1,178	1,154
Total	6,765	6,405

G. CENTRAL ESTIMATE AND RISK MARGIN

I. Reporting date values

The percentage risk margin applied to the present value of expected future payments for claims incurred net of outstanding recoveries and expected GST recovery

	19.4	19.1
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The probability of adequacy of the risk margin

	90	90
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II. Process

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

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

a. FUTURE CASH FLOWS

The estimation of the outstanding claims liability is based on a variety of actuarial techniques that analyse experience, trends and other relevant factors. The claims estimation process commences with the actuarial projection of the future payments relating to claims incurred at the reporting date. The expected future payments include those in relation to claims reported but not yet paid or not yet paid in full, claims incurred but not enough reported (IBNER), claims incurred but not reported (IBNR) and the anticipated direct and indirect claims handling costs.

The estimation 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, legal, social and economic factors that may impact upon each class of business as well as the key actuarial assumptions set out in section H, and the impact of reinsurance and other recoveries (refer to the reinsurance and other recoveries on outstanding claims note).

Different actuarial valuation models are used for different claims types with the results then being aggregated. This aggregation of results enhances the valuation process by allowing the use of the model best suited to particular claims types. The selection of the appropriate model takes into account the characteristics of a class of business and the extent of development of each past accident period.

The different components of the outstanding claims liability are subject to different levels of uncertainty. The estimation of the cost of claims reported but not yet paid or not yet paid in full is made on a case by case basis by claims personnel having regard to the facts and circumstances of the claims as reported, any information available from assessors and information on the cost of settling claims with similar characteristics in previous periods. A further amount, which may be a reduction, is included for IBNER on the basis of past experience with the accuracy of initial claims estimates. With IBNR, the estimation is generally subject to a greater degree of uncertainty than the estimation of the cost of settling claims already notified, as no information is currently available about the claim. IBNR claims may often not be apparent to the insured until many years after the events giving rise to the claim have occurred. In calculating the estimated cost of unpaid claims a variety of estimating techniques are used, generally based on statistical analysis of historical experience, which assumes that the development pattern of the current claims will be consistent with past experience. Allowance is made, however, for changes or uncertainties which may create distortions in the underlying statistics or which might cause the cost of unsettled claims to increase or reduce when compared with the cost of previously settled claims.

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

Reserves are not established for catastrophes in advance of such events and so these events may cause volatility in the results for a period and in the level of the outstanding claims liability, subject to the effects of reinsurance recoveries.

The valuation of the outstanding claims liability for the major portfolios is primarily performed by actuaries who do not have any direct role in the pricing function so as to ensure that an objective and independent assessment of the outstanding claims liability is maintained on a regular basis.

b. DISCOUNTING

A projection of future claims payments, both gross and net of reinsurance and other recoveries, is undertaken. Projected future claims payments and associated claims handling costs are discounted to a present value as required using appropriate risk free discount rates.

c. RISK MARGIN

The central estimate of the outstanding claims liability is an estimate which is intended to contain no deliberate or conscious over or under estimation and is commonly described as providing the mean of the distribution. It is considered appropriate for the measurement of the claims liability to represent a higher degree of certainty regarding the sufficiency of the liability over time, and so a risk margin is added to the central estimate. The risk margin refers to the amount by which the liability recognised in the financial statements is greater than the actuarial central estimate of the liability. The risk margin added to the central estimate increases the probability that the net outstanding claims liability will ultimately prove to be adequate.

Risk margins are held to allow for uncertainty surrounding the outstanding claims liability estimation process. Potential uncertainties include those relating to the actuarial models and assumptions, the quality of the underlying data used in the models, general statistical uncertainty, the general insurance environment, scope for and experience of political intervention (particularly for long-tail classes) and the impact of legislative reform. Uncertainty from the above sources is examined for each class of business and expressed as a volatility relative to the net central estimate. The volatility for each class is derived after consideration of stochastic modelling and benchmarking to industry analysis. Certain product classes may be subject to the emergence of new types of latent claims and such uncertainties are considered when setting the risk margin appropriate for those classes.

The long-tail classes of business generally have the highest volatilities of the insurance classes 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.

The risk margin is expressed using a probability of adequacy approach. The risk margin that equates to a given probability of adequacy for two or more classes of business or for two or more geographic locations combined is likely to be less than the sum of the risk margins for the individual classes. This reflects the benefit of diversification in general insurance. Two key components of the valuation methodology are the selection of coefficients of variation (CoV) for each class of business and the correlation factors between each pair of classes of business. The CoV is a measure of the volatility of a class of business and is generally greater for long-tail classes when compared to short-tail classes because of the increased uncertainty relating to the longer time until settlement of claims. The correlation factors are a measure of the correlation between pairs of business classes and measure the strength of the relationship of movements in that pair of class liabilities. The higher the correlation between two classes of business, the more likely it is that a negative outcome in one class will correspond to a negative outcome in the other class. The correlations adopted are normally derived from industry analysis, historical experience and the judgement of experienced and qualified actuaries.

The risk margin is set taking into account the correlations assessed between the outstanding claims liabilities arising from the various forms of business underwritten by the different entities within the Consolidated entity. The overall risk margin is estimated on a diversified basis, taking into account the diversification benefit arising from combining all classes of business within the Consolidated entity. Allowance is made for diversification between portfolios, between entities and between geographies. The assumptions regarding uncertainty for each class are applied to the net central estimates, and the results are aggregated. The aggregated central estimate plus the risk margin calculated on a diversified basis forms the outstanding claims liability. The current risk margins, which have been determined having regard to the inherent uncertainty in the central estimate and the prevailing market environment, result in an overall probability of adequacy for the outstanding claims liability of 90%.

H. ACTUARIAL ASSUMPTIONS

The key actuarial assumptions used in the measurement of outstanding claims and recoveries, where appropriate, at reporting date.

	CONSOLIDATED				
	Australia direct insurance	Australia intermediated insurance	New Zealand insurance	United Kingdom insurance	Asia insurance
2010					
Discounted average term to settlement	2.6 years	4.2 years	0.6 years	1.7 years	0.5 years
Inflation rate	2.8%–4.0%	2.8%–4.5%	2.8%	3.5%	0.0%–3.5%
Superimposed inflation rate	0.0%–4.0%	0.0%–8.0%	0.0%	0.0%–6.5%	0.0%
Discount rate	4.3%–6.1%	4.4%–5.9%	2.7%–4.8%	0.0%–4.2%	0.0%
Claims handling costs ratio	4.2%	5.5%	4.0%	2.8%	2.9%
2009					
Discounted average term to settlement	2.7 years	3.9 years	0.5 years	1.6 years	0.5 years
Inflation rate	3.6%–4.0%	3.0%–4.3%	2.3%–3.5%	3.0%–3.5%	0.0%–3.5%
Superimposed inflation rate	0.0%–4.4%	0.0%–5.0%	0.0%	0.0%–4.0%	0.0%
Discount rate	4.5%–5.4%	3.0%–6.5%	3.2%	0.2%–4.7%	0.0%
Claims handling costs ratio	5.2%	6.3%	4.5%	4.0%	2.9%

I. PROCESS USED TO DETERMINE ASSUMPTIONS

The process for establishing the outstanding claims liability involves extensive consultation with internal and external actuaries, claims managers, underwriters and other senior management. One of the key elements of the valuation process is rigorous data verification and reconciliation.

A description of the key assumptions and the processes used to determine those assumptions is provided below.

I. Discounted average term to settlement

The discounted average term to settlement relates to the expected payment pattern for claims (inflated and discounted). The payment pattern is important in considering the timing of future cash outflows and hence discounting and in managing the assets backing insurance liabilities to support the outflows. The future cash flow pattern is estimated separately for each class of business based on historic settlement patterns and estimated future settlement patterns. The discounted average term to settlement, while not itself an assumption, provides a summary indication of the future cash flow pattern.

II. Inflation rate

Insurance costs are subject to inflationary pressures. Economic inflation assumptions are set by reference to current economic indicators. For example, for the motor and property classes, claims costs are related to the inflationary pressures of the materials and goods insured as well as labour costs to effect repairs.

III. Superimposed inflation rate

Superimposed inflation occurs due to non-economic effects such as court settlements increasing at a faster rate than wages or CPI inflation and from social and environmental pressures. Where appropriate, the effect of superimposed inflation is made either in the underlying model for the class of business, for example where the past pattern of development in claims cost is used to estimate future claims cost development factors, or by including a specific superimposed inflation rate assumption designed to allow for all other claims inflation not modelled. The level of superimposed inflation is estimated after considering both the superimposed inflation present in the portfolio and industry superimposed inflation trends.

IV. Discount rate

Because the outstanding claims liability represents payments that will be made in the future, they are discounted to reflect the time value of money effectively recognising that the assets held to back insurance liabilities will earn a return during that period. Discount rates represent a risk free rate derived from market yields on government securities.

V. Claims handling costs ratio

In respect of claims incurred up to the reporting date, it is known that costs will be incurred in the management of claims to finalisation. An estimate of these costs is incorporated into the outstanding claims liability using the claims handling costs ratio. The ratio incorporates assumptions about the future costs to be incurred based on past experience of such costs for each class of business.

J. THE EFFECT OF CHANGES IN ASSUMPTIONS

I. General impact of changes

Sensitivity analysis is conducted to quantify the exposure to changes in the key underlying variables. The valuations included in the reported results are calculated using certain assumptions about these variables as disclosed above. The movement in any key variable will impact the financial position and performance for a period. The information below describes how a change in each assumption will affect claims liabilities and provides an analysis of the sensitivity of the net outstanding claims liability to changes in these assumptions.

a. DISCOUNTED AVERAGE TERM TO SETTLEMENT

A decrease in the average term to settlement would reflect claims being paid sooner than anticipated and so increase the claims expense. Note this sensitivity only extends or shortens the term of the payments assumed in the valuation, without changing the total amount of the payments.

b. INFLATION AND SUPERIMPOSED INFLATION RATES

Expected future payments are inflated to take account of inflationary increases. An increase or decrease in the assumed levels of inflation would have a corresponding impact on claims expense, with particular reference to long-tail business. The inflation rate sensitivity is provided as an indicator of the impact of inflation on the portfolio, whether it be from economic inflation, inflation implied from the use of the past pattern of development in claims cost in the valuation method or inflation related to a superimposed inflation rate specified.

c. DISCOUNT RATE

The outstanding claims liability is calculated by reference to expected future payments. These payments are discounted to adjust for the time value of money. An increase or decrease in the assumed discount rate will have an opposing impact on total claims expense.

d. CLAIMS HANDLING COSTS RATIO

An increase in the ratio reflects an increase in the estimate for the internal costs of administering claims which will increase the outstanding claims liability.

II. Sensitivity analysis of changes

The impact of changes in key outstanding claims variables is summarised below. Each change has been calculated in isolation of the other changes.

It is not possible to quantify the sensitivity of certain assumptions such as legislative changes or uncertainty in the estimation process.

The impact on the net outstanding claims liability is disclosed for each of the key assumptions. The movements are stated in absolute terms where the base assumption is a percentage, for example, if the base inflation rate assumption was 3.5%, a 1% increase would mean assuming a 4.5% inflation rate. All movements are recognised directly through profit.

VARIABLE	CONSOLIDATED					
	Movement in variable	Australia direct insurance \$m	Australia intermediated insurance \$m	New Zealand insurance \$m	United Kingdom insurance \$m	Asia insurance \$m
2010						
Discounted average term to settlement	+10%	(42)	(52)	–	(1)	–
	–10%	43	55	–	1	–
Inflation rate	+1%	90	109	1	8	–
	–1%	(87)	(98)	(1)	(8)	–
Discount rate	+1%	(84)	(96)	(1)	(8)	–
	–1%	90	108	1	8	–
Claims handling costs ratio	+1%	44	32	2	7	1
	–1%	(44)	(32)	(2)	(7)	(1)
2009						
Discounted average term to settlement	+10%	(48)	(59)	–	(3)	–
	–10%	48	62	–	3	–
Inflation rate	+1%	84	99	1	7	–
	–1%	(86)	(90)	(1)	(7)	–
Discount rate	+1%	(84)	(88)	(1)	(7)	–
	–1%	84	99	1	7	–
Claims handling costs ratio	+1%	35	26	3	7	1
	–1%	(35)	(26)	(3)	(7)	(1)

The movements in the net outstanding claims liability would have an opposing net impact on the profit or loss before tax for a year.

NOTE 13. REINSURANCE AND OTHER RECOVERIES ON OUTSTANDING CLAIMS

	CONSOLIDATED	
	2010 \$m	2009 \$m
A. REINSURANCE AND OTHER RECOVERIES RECEIVABLE ON OUTSTANDING CLAIMS		
Reinsurance recoveries receivable on outstanding claims	663	654
Other recoveries receivable	408	393
Reinsurance recoveries on outstanding claims and other recoveries receivable	1,071	1,047

The carrying value of reinsurance recoveries and other recoveries receivable includes \$658 million (2009—\$643 million) which is expected to be settled more than 12 months from reporting date. Reinsurance recoveries on paid claims are included in trade and other receivables.

B. ACTUARIAL ASSUMPTIONS

The measurement of reinsurance and other recoveries on outstanding claims is an inherently uncertain process involving estimates. The amounts are computed using actuarial assumptions and methods similar to those used for outstanding claims (refer to section G of the claims note). The outstanding claims liability is calculated gross of any reinsurance recoveries and a separate estimate is then made of the amounts that are expected to be recoverable from reinsurers based upon the gross provisions, including incurred but not reported unpaid claims. Estimates of potential reinsurance recoveries are made on an individual claim basis for reported claims. Consideration is given to limitations and coverage exclusions under the reinsurance agreements. Accordingly, the estimate of reinsurance recoverables is subject to similar risks and uncertainties as the estimate of the outstanding claims liability. The recoverables are considered to have been appropriately established. However, as the underlying reserves continue to develop, the amount ultimately recoverable may vary from amounts currently recorded. The recoverability of these assets is assessed on a periodic basis to ensure that the balance is reflective of the amounts that will ultimately be received.

C. THE EFFECT OF CHANGES IN ASSUMPTIONS

The effect of changes in assumptions on the net outstanding claims liability, which incorporates the reinsurance recoveries on outstanding claims and other recoveries receivable, is disclosed in the claims note.

NOTE 14. DEFERRED ACQUISITION COSTS

	CONSOLIDATED	
	2010	2009
	\$m	\$m
RECONCILIATION OF MOVEMENTS		
Deferred acquisition costs at the beginning of the financial year	733	758
Acquisition costs deferred	1,022	1,203
Amortisation charged to profit	(1,038)	(1,163)
Write down for liability adequacy test	(16)	(50)
Disposed through sale of businesses	–	(16)
Net foreign exchange movements	(13)	1
Deferred acquisition costs at the end of the financial year	688	733

The carrying value of deferred acquisition costs includes \$57 million (2009—\$39 million) which is expected to be amortised more than 12 months from reporting date.

NOTE 15. UNEARNED PREMIUM LIABILITY

A. RECONCILIATION OF MOVEMENTS

Unearned premium liability at the beginning of the financial year	4,072	4,097
Unearned premium disposed through sale of businesses	–	(136)
Deferral of premiums on contracts written	4,103	4,078
Earning of premiums written in previous financial years	(3,942)	(3,954)
Net foreign exchange movements	(26)	(13)
Unearned premium liability at the end of the financial year	4,207	4,072

The carrying value of unearned premium liability includes \$122 million (2009—\$130 million) which is expected to be earned more than 12 months from reporting date.

B. LIABILITY ADEQUACY TEST

The liability adequacy test has been conducted using the central estimate of the premium liabilities calculated for reporting to APRA (refer to the capital management note), adjusted as appropriate, together with an appropriate margin for uncertainty for each portfolio of contracts, being Australia direct insurance, Australia intermediated insurance, New Zealand insurance, United Kingdom insurance and Asia insurance. The test is based on prospective information and so is heavily dependent on assumptions and judgements.

The liability adequacy test at reporting date resulted in a surplus for each portfolio of contracts except for the United Kingdom insurance portfolio, for which additional information is provided in the table below (2009—surplus for each portfolio of contracts except for Australia intermediated insurance portfolio).

	2010		2009	
	United Kingdom insurance	Consolidated	Australia intermediated insurance	Consolidated
	\$m	\$m	\$m	\$m
Unearned premium liability	367		1,546	
Deferred acquisition costs	(97)		(289)	
Related reinsurance asset	(9)		(291)	
	261		966	
Central estimate of present value of expected future cash flows from future claims	279	3,154	1,109	3,094
Present value of expected future cash inflows arising from reinsurance recoveries on future claims	(11)	(341)	(201)	(342)
Risk margin	9	116	40	118
	277	2,929	948	2,870
Net surplus/(deficiency)	(16)		18	
Risk margin percentage	3.3%	4.1%	4.5%	4.3%
Probability of adequacy	64.1%	65.0%	67.7%	65.9%
Net deficiency recognised in the statement of comprehensive income				
Write down of deferred acquisition costs*	(16)		(50)	
	(16)		(50)	

* The write down of deferred acquisition costs of \$50 million represented a shortfall for the Australia intermediated business in the liability adequacy test as at 31 December 2008. At 30 June 2009, the liability adequacy test of the Australia intermediated business resulted in a surplus. However, the write down of deferred acquisition costs recognised in the first half of the current annual reporting period could not be reversed.

Reasonably foreseeable changes in the key assumptions used in the liability adequacy test would not result in a deficiency for any of the portfolios for which a surplus was identified.

The risk margin used in testing individual portfolios is determined based on an assessment of the recent historical experience in relation to the volatility of the insurance margin for each portfolio of contracts together with an allocation of group diversification.

The test has not been applied using the statistical concept of probability of adequacy. Hence the risk margin applied for the purposes of the liability adequacy test has been determined using a different methodology to that used for the determination of the risk margin for the outstanding claims liability. The probability of adequacy represented by the liability adequacy test also differs from the probability of adequacy represented by the outstanding claims liability. The reason for these differences is that the former is in effect an impairment test used only to test the sufficiency of net premium liabilities whereas the latter is a measurement accounting policy used in determining the carrying value of the outstanding claims liability carried on the balance sheet. It is also important to understand that the IAG Group is predominantly a short-tail insurer, with over 80% of gross written premium relating to short-tail products, and so the net premium liability consists mostly of short-tail products and so appropriately bears a lower probability of adequacy reflecting the lower risk compared to the outstanding claims liability which comprises mostly long-tail insurance claims aggregated over many years.

NOTE 16. INVESTMENTS

	CONSOLIDATED	
	2010	2009
	\$m	\$m
A. COMPOSITION		
I. Interest bearing investments		
Cash and short term money held for investment	637	938
Government and semi-government bonds	4,503	3,914
Corporate bonds and notes	4,004	4,134
Subordinated debt	890	799
Fixed interest trusts	52	43
Other	487	137
	10,573	9,965
II. Equity investments		
a. DIRECT EQUITIES		
Listed	626	479
Unlisted	138	2
b. EQUITY TRUSTS (INCLUDING PROPERTY TRUSTS)		
Listed	36	17
Unlisted	339	84
	1,139	582
III. Other investments		
Other trusts	7	8
	7	8
IV. Derivatives		
Interest rate risk derivatives	9	4
Equity risk derivatives	4	2
Foreign exchange risk derivatives	2	2
	15	8
	11,734	10,563

The investments balance includes Funds at Lloyd's of \$389 million at the current reporting date (2009—\$182 million) which are subject to certain restrictions.

The Parent held no investment as at 30 June 2010 (2009—\$1 million being an investment in a former subsidiary which was put into liquidation).

Since 30 June 2009, the IAG Group's strategy has been to gradually increase the growth assets weighting in the equity holders' funds. The change in strategy reflected both a recovery in underlying equity markets and recognition that market conditions are sufficiently improved to justify an increased exposure to growth assets.

The IAG Group intends to move towards a 50% target for growth assets within the equity holders' funds. As at 30 June 2010, the growth assets held are 37% of total equity holders' funds.

B. DETERMINATION OF FAIR VALUE

All investments are initially recorded at fair value and are then subsequently remeasured to fair value at each reporting date. For those investments traded in an active market this involves applying the published bid price quotations. For trust securities this generally means using the redemption price provided by the trustee.

There has been no change during the current reporting period in the processes used for the determination of the fair value for investments. The fair value of investments has continued to be principally determined based on independently sourced prices that do not involve the exercise of judgement by management.

There is an insignificant portion of investments (1%) for which a valuation methodology is used to determine the fair value. The assets are effectively marked to model rather than marked to market. Reasonable changes in the judgement applied in conducting these valuations would not have a significant impact on the balance sheet.

The table below separates the total investments balance based on a hierarchy that reflects the significance of the inputs used in the determination of fair value. The fair value hierarchy has the following levels:

I. Level 1 quoted prices

Quoted prices (unadjusted) in active markets for identical assets and liabilities are used.

II. Level 2 other observable inputs

Inputs that are observable (other than Level 1 quoted prices) for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices) are used.

III. Level 3 unobservable inputs

Inputs for the asset or liability that are not based on observable market data (unobservable inputs) are used.

Where the determination of fair value for an instrument involves inputs from more than one category, the level within which the instrument is categorised in its entirety is determined on the basis of the lowest level input that is significant to the fair value measurement in its entirety.

	LEVEL 1 \$m	LEVEL 2 \$m	LEVEL 3 \$m	TOTAL \$m
2010				
Interest bearing investments	5,987	4,585	1	10,573
Equity investments	662	335	142	1,139
Other investments	5	-	2	7
Derivatives	14	1	-	15
	6,668	4,921	145	11,734
2009				
Interest bearing investments	5,515	4,432	18	9,965
Equity investments	495	2	85	582
Other investments	8	-	-	8
Derivatives	8	-	-	8
	6,026	4,434	103	10,563

NOTE 17. RECEIVABLES

	CONSOLIDATED	
	2010	2009
	\$m	\$m
A. COMPOSITION		
I. Premium receivable		
Premium receivable	2,084	2,131
Provision for impairment	(38)	(23)
Premium receivable	2,046	2,108
II. Trade and other receivables		
Reinsurance recoveries on paid claims	205	131
Other trade debtors	208	28
Provision for impairment	(5)	(9)
	203	19
GST recoverable on gross outstanding claims liability	421	369
Investment income receivable	118	103
Investment transactions not yet settled at reporting date	50	3
Corporate treasury derivatives receivable	-	138
Other debtors	87	124
Trade and other receivables	1,084	887
	3,130	2,995

The Parent had \$1 million of other trade receivables at 30 June 2010. At 30 June 2009, the Parent had a receivable of \$96 million related to the RES embedded derivative, which for the Consolidated entity was included in the trade and other receivables line of the balance sheet.

The Consolidated entity had a receivable at reporting date of \$180 million (2009—\$Nil) included in other trade debtors. The receivable is part of the adverse development cover (ADC) purchased following the United Kingdom claim reserve strengthening. This reinsurance provides the IAG Group with significant protection against any further adverse development of the United Kingdom motor portfolio for the underwriting years ended 31 December 2009 and prior. The balance is predominantly secured by a letter of credit. It is anticipated the deposit will be recovered through settlement of the ADC.

The receivables are non interest bearing and are normally settled between 30 days and 12 months. The balance has not been discounted, except the ADC receivable, because 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 because of the short term nature of the assets.

NOTE 18. PROPERTY AND EQUIPMENT

	CONSOLIDATED			
	Land and buildings \$m	Motor vehicles \$m	Other equipment \$m	Total \$m
2010				
A. COMPOSITION				
At cost	198	66	361	625
Accumulated depreciation	(37)	(29)	(258)	(324)
Net foreign exchange movements	–	–	1	1
Balance at the end of the financial year	161	37	104	302
2010				
B. RECONCILIATION OF MOVEMENTS				
Balance at the beginning of the financial year	149	40	119	308
Additions	31	20	20	71
Disposals	(2)	(12)	(12)	(26)
Additions through business combination	–	–	1	1
Depreciation	(16)	(11)	(24)	(51)
Net foreign exchange movements	(1)	–	–	(1)
Balance at the end of the financial year	161	37	104	302
2009				
C. COMPOSITION OF COMPARATIVES				
Cost	169	65	359	593
Accumulated depreciation	(21)	(25)	(241)	(287)
Net foreign exchange movements	1	–	1	2
Balance at the end of the financial year	149	40	119	308
D. DEPRECIATION RATES				
	2%–5%	12.5%–33%	6.67%–40%	

The net carrying amount of all classes of property and equipment is considered a reasonable approximation of the fair value of the assets in the context of the financial statements. There are no items of property and equipment pledged as security for liabilities. The depreciation expense amounts are allocated across various lines in the statement of comprehensive income.

NOTE 19. INTANGIBLE ASSETS

	CONSOLIDATED						
	Software development expenditure	Lloyd's syndicate capacity	Distribution channels	Customer relationships	Brands	Other contractual arrangements	Total
	\$m	\$m	\$m	\$m	\$m	\$m	\$m
2010							
A. COMPOSITION							
Cost	259	138	269	104	92	5	867
Accumulated amortisation	(199)	–	(70)	(29)	(16)	(3)	(317)
Accumulated impairment	(7)	(11)	(24)	(25)	(9)	(1)	(77)
Net foreign exchange movements	(14)	(40)	(63)	(21)	(33)	(1)	(172)
Balance at the end of the financial year	39	87	112	29	34	–	301
2010							
B. RECONCILIATION OF MOVEMENTS							
Balance at the beginning of the financial year	51	114	170	11	52	–	398
Additions acquired and developed	13	–	–	–	–	–	13
Additions through acquisition of business	2	–	–	25	–	–	27
Amortisation	(24)	–	(16)	(6)	(4)	–	(50)
Impairment charge	–	(11)	(19)	–	(7)	–	(37)
Net foreign exchange movements	(3)	(16)	(23)	(1)	(7)	–	(50)
Balance at the end of the financial year	39	87	112	29	34	–	301
2009							
C. COMPOSITION OF COMPARATIVES							
Cost	245	138	269	79	92	5	828
Accumulated amortisation	(176)	–	(54)	(23)	(12)	(3)	(268)
Accumulated impairment	(7)	–	(5)	(25)	(2)	(1)	(40)
Net foreign exchange movements	(11)	(24)	(40)	(20)	(26)	(1)	(122)
Balance at the end of the financial year	51	114	170	11	52	–	398
D. AMORTISATION RATES	33.33%	n/a	8%–14%	10%–17%	5%–20%	20%–33%	

E. EXPLANATORY NOTES FOR INTANGIBLE ASSETS

I. Software development expenditure

The software development expenditure asset comprises both internally generated assets and acquired assets. The capitalisation of the software development expenditure involves the exercise of judgement in determining whether the costs incurred will be recovered through the probable generation of future economic benefits from the internal use of the asset. This process is supported by the preparation of detailed business cases and subsequent review processes that are required to approve a greater than \$2 million project including a detailed business case. The asset represents both projects that have been completed and the developed software implemented as well as projects that continue in development. The future economic benefits expected to be realised from the capitalised software development expenditure will benefit various operating functions and so the amortisation of the assets is included in various lines in the statement of comprehensive income.

II. Acquired intangible assets

All of the intangible assets other than the capitalised software development expenditure intangible asset have been acquired. With the exception of the Lloyd's syndicate capacity, each of the acquired intangible assets has a finite useful life. The amortisation of the acquired intangible assets forms part of fee based, corporate and other expenses in the statement of comprehensive income. A broad description of the nature of each of the significant intangible assets is provided here.

a. LLOYD'S SYNDICATE CAPACITY

The Lloyd's syndicate capacity is allocated to the United Kingdom cash generating unit. The syndicate capacity was acquired as part of the acquisition of Equity Insurance Group in 2007 which at acquisition date held 64.02% of the capacity of Syndicate 218. The syndicate capacity was categorised as an indefinite life asset on the basis that there is no foreseeable limit to the period over which the asset is expected to generate net cash flows for the United Kingdom cash generating unit. The basis of the determination of recoverable amount is a return (profit) to be generated on the expected premiums to be written by the syndicate. The growth and profitability assumptions are based on the management forecast for the next five years with long term growth and insurance margin assumptions of 3.5% and 9.6% respectively. A 1% reduction in the terminal growth rate would reduce the value by approximately \$50 million and a 1% reduction in the terminal insurance margin would reduce the value by approximately \$52 million.

b. BRANDS

This represents the revenue generating value of acquired brands.

c. CUSTOMER RELATIONSHIPS

This is in effect the capitalisation of future profits relating to the insurance contracts in place at acquisition and the expected renewals of those contracts. It represents the amount paid to the vendor for the value of the customer relationships developed prior to acquisition. A fall in renewal rates may lead to a reduction in the useful life of the asset and a commensurate acceleration of the amortisation.

d. DISTRIBUTION CHANNELS

The value of the distribution channels is in the future revenue expected to be generated as a result of the existing relationships with the broker networks and affinity accounts.

III. Other intangible assets

There are a number of other intangible assets that are controlled but which are not presented on the balance sheet because they do not meet the recognition criteria. These are both acquired and internally generated intangible assets. These include brands, information technology systems, and distribution channels.

F. IMPAIRMENT TESTING

For each category an impairment trigger review was conducted and where necessary the recoverable amount of particular assets determined.

I. Impairment testing results for current period

Adverse development in the UK motor bodily injury experience has led to a range of proposed actions to strengthen the business performance of the UK cash generating unit which are being undertaken. These include rate increases of 10%–20% across all classes of business, exiting certain unprofitable broker relationships, ceasing to write external aggregator-sourced business of a non-bike nature, strengthening underwriting and actuarial resources and revising and enhancing underwriting and claim practices. Industry developments coupled with the anticipated impact of proposed business actions have led to reductions in the short to medium term business volume and profitability assumptions. As a result of these actions, the following acquired intangible assets were impaired during this financial period.

a. LLOYD'S SYNDICATE CAPACITY

Impairment charge of \$11 million due to the anticipated adverse impact of anticipated price increases on gross written premium (GWP) volume and poor short to medium term profitability.

b. EQUITY INSURANCE BRAND

Impairment charge of \$7 million due to the adverse impact of the anticipated price increases on GWP volume.

c. EQUITY INSURANCE DISTRIBUTION CHANNEL—AFFINITY RELATIONSHIPS

Impairment charge of \$19 million due to the anticipated adverse impact of the exiting of certain broker relationships on GWP volume and poor short to medium term profitability.

II. Impairment testing results for prior period

During the prior period, the following acquired intangible assets were impaired.

a. EQUITY INSURANCE DIRECT CHANNEL—CUSTOMER RELATIONSHIPS

The Equity Insurance customer relationships intangible asset reflects the anticipated profits from a mix of over-the-phone and internet insurance broking. In respect of customers acquired, the impairment was triggered because it was found that customer profitability had fallen due to increasing volumes of business being placed by aggregators (lower margins) and the general level of competition in the market place. The recalculation of the value of this intangible asset at 30 June 2009 led to a write down of \$12 million.

b. EQUITY INSURANCE DISTRIBUTION CHANNEL—AFFINITY RELATIONSHIPS

The Equity Insurance distribution channel intangible asset reflects the anticipated profits from customers acquired through Equity affinity relationships. The impairment was triggered because it was found that customer profitability and attrition had both breached the relevant trigger levels. While turnover of affinity relationships has remained low, the attribution rates of end customers had been significantly higher than expected and customer profitability had been significantly lower than expected due to the highly competitive nature of the UK market. The recalculation of the value of this intangible asset at 30 June 2009 led to a full write down of \$5 million.

NOTE 20. GOODWILL

	CONSOLIDATED	
	2010	2009
	\$m	\$m
A. COMPOSITION		
Goodwill	2,154	2,149
Accumulated impairment charges	(168)	(118)
Net foreign exchange movements	(204)	(151)
	1,782	1,880
B. RECONCILIATION OF MOVEMENTS		
Balance at the beginning of the financial year	1,880	1,875
Additional amounts arising from business combinations	5	7
Disposed through sale of businesses	–	(12)
Impairment charge	(50)	–
Net foreign exchange movements	(53)	10
Balance at the end of the financial year	1,782	1,880
C. ALLOCATION TO CASH GENERATING UNITS		
Australia direct insurance operations	582	582
Australia intermediated insurance operations	574	574
New Zealand insurance operations	288	286
Asia insurance operations	54	54
United Kingdom insurance operations	284	384
	1,782	1,880

As the IAG Group incorporates businesses into the IAG Group and/or reorganises the way businesses are managed, reporting structures may change requiring a reconsideration of the identification of the cash generating units.

The goodwill relating to certain acquisitions outside Australia is denominated in currencies other than Australian dollars and so is subject to foreign exchange rate movements.

D. IMPAIRMENT ASSESSMENT

The impairment testing of goodwill involves the use of accounting estimates and assumptions. The recoverable amount of each cash generating unit is determined on the basis of value in use calculations. The value in use is calculated using a discounted cash flow methodology covering a five or 10 year period with an appropriate terminal value at the end of year five or 10, less net assets required, for each of the key business units within a cash generating unit. 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.

I. Assumptions used

The following describes the key assumptions on which management has based its cash flow projections to undertake impairment testing of goodwill.

a. CASH FLOW FORECASTS

Cash flow forecasts are based on five year business plans. 10 year periods are only used in emerging markets, to enable appropriate phasing to terminal values.

b. TERMINAL VALUE

Terminal value is calculated using a perpetuity growth formula based on the cash flow forecast for year five or 10, 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 IAG Group's impairment assessment as at 30 June 2010 range from 3% to 5%.

c. DISCOUNT RATE

Discount rates reflect a beta and equity risk premium appropriate to the Group, with risk adjustments for individual segments and countries where applicable. Discount rates used are pre tax and range from 11.7% to 14.5% (equivalent to 10.2% and 11.6% on a post tax basis).

The gross discount rate used to value the UK cash generating unit as at 30 June 2010 was 11.7% (10.2% net of tax). This compares with 13.2% (10.3% net of tax) used for the previous assessment as at 31 December 2009. The change in discount rate resulted from a change in the Group's estimate of its weighted average cost of capital.

II. Sensitivity—UK

There are a number of key sensitivities within the valuation and these are noted below. They are stated in isolation although they are not wholly independent—for example, changes in interest rates leading to a change in discount rate could also lead to a change in profitability as investment income would change:

- an increase/decrease of 1% in the discount rate used would have increased/decreased the impairment charge by approximately \$112 million/\$50 million;
- an increase/decrease of 3% in the year-on-year premium growth over the valuation period would have reduced/increased the impairment charge by approximately \$88 million/\$50 million;
- an increase/decrease of 1% in the terminal growth rate used would have decreased/increased the impairment charge by approximately \$50 million/\$75 million; and
- an increase/decrease of 1% in the terminal insurance margin used would have decreased/increased the impairment charge by approximately \$50 million/\$61 million.

III. Impairment testing results for current period

Adverse development in UK motor bodily injury experience has led to an impairment of \$50 million in the UK cash generating unit during the current financial year (2009—\$Nil). A range of actions to strengthen the business performance of the UK cash generating unit are being undertaken. The anticipated impact of these proposed business actions coupled with industry developments have led to reductions in the short to medium term business volume and profitability assumptions.

NOTE 21. TRADE AND OTHER PAYABLES

	CONSOLIDATED	
	2010	2009
	\$m	\$m
A. COMPOSITION		
I. Trade creditors		
Commissions payable	107	129
Stamp duty payable	74	69
GST payable on premium receivable	81	80
Other	391	267
	653	545
Deferred payable under acquisition agreement*	–	25
II. Other payables		
Other creditors and accruals	326	279
Investment creditors	51	2
Interest payable on interest bearing liabilities	11	12
	1,041	863

* Relates to the Alba Group acquisition effected 3 July 2006. Cash flow hedge accounting is applied in relation to this payable.

The Parent had interest payable on interest bearing liabilities of \$7 million at reporting date (2009—\$8 million).

Trade and other payables are unsecured, non interest bearing and are normally settled within 30 days. 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.

NOTE 22. RESTRUCTURING PROVISION

A. COMPOSITION		
Restructuring provision	22	34
	22	34
B. RECONCILIATION OF MOVEMENTS		
Balance at the beginning of the financial year	34	61
Additions	16	43
Settled	(27)	(70)
Remeasurement of provisions	(1)	–
Balance at the end of the financial year	22	34

All of the provision outstanding at the reporting date is expected to be settled within 12 months (2009—all). The balance has not been discounted.

NOTE 23. INTEREST BEARING LIABILITIES

	SECTION	2010 \$m	PARENT 2009 \$m	CONSOLIDATED 2010 \$m	2009 \$m
A. COMPOSITION					
I. Capital nature					
a. TIER 1 REGULATORY CAPITAL ^(a)					
Reset preference shares	C.I	350	350	350	350
Reset exchangeable securities	C.II	–	–	550	–
b. TIER 2 REGULATORY CAPITAL					
USD subordinated term notes	C.III	–	–	–	295
Derivatives related to USD subordinated term notes ^(b)	C.III	–	–	–	111
GBP subordinated term notes	C.IV	252	293	183	220
NZD subordinated term notes	C.V	–	–	81	81
GBP subordinated exchangeable term notes	C.VI	–	–	277	–
II. Operational nature					
Other interest bearing liabilities		–	–	14	–
Less: capitalised transaction costs		(2)	(3)	(5)	(4)
		600	640	1,450	1,053

(a) These instruments are eligible for recognition as Tier 1 capital. A portion will be reclassified as Tier 2 capital to the extent the amount on issue is in excess of APRA's Innovative Tier 1 limit.

(b) The derivatives related to the USD subordinated term notes are disclosed together with the notes but do not form part of Tier 2 regulatory capital.

B. RECONCILIATION OF MOVEMENTS

Balance at the beginning of the financial year		640	860	1,053	1,401
I. New issues/recognition					
Reset exchangeable securities brought onto the balance sheet		–	–	550	–
Issue of GBP subordinated exchangeable term notes		–	–	260	–
Issue of other interest bearing liabilities		–	–	14	–
II. Repayments					
Repayment of USD subordinated term notes		–	–	(260)	–
Repayment of derivative relating to USD subordinated term notes		–	–	(141)	–
Buyback of GBP subordinated term notes		–	(236)	(6)	(310)
Repayment of Euro floating rate notes		–	–	–	(21)
Repayment of GBP unsecured notes		–	–	–	(4)
Repayment of NZD subordinated term notes		–	–	–	(41)
III. Other movements					
Foreign exchange movement on notes		(41)	10	(49)	60
Foreign exchange movement on cash flow hedge		–	–	35	(45)
Other fair value movement on cash flow hedge		–	–	(5)	5
Amortisation of capitalised transaction costs		1	6	(1)	8
		600	640	1,450	1,053

C. SIGNIFICANT TERMS AND CONDITIONS

I. Reset preference shares

The reset preference shares (RPS) are a hybrid security with characteristics of both debt and equity. The securities have a face value of \$350 million and were issued in June 2002 (with terms reset in June 2007).

The RPS entitle the holder to a preferred, but not cumulative, distribution of 5.63% per annum. The distributions are payable semi annually in arrears on 15 December and 15 June and are able to be franked. The distributions are expected to be fully franked and if a distribution is unfranked or partially franked, the distribution will be increased to compensate for the unfranked component. Because of the hybrid nature of the securities, distributions on the RPS are not the same as interest payments and may not always be paid, as there are a number of conditions that must be met before a distribution can be paid. If distributions are not paid on the RPS, no dividends can be paid and no returns of capital can be made on ordinary shares unless IAG takes certain actions.

The RPS may be exchanged by IAG or the holder on a reset date, by the holder upon a specified trigger event (such as change in control of IAG by a takeover bid), or by IAG on a tax event (such as a more than insignificant increase in taxation costs), regulatory event (such as not all of the RPS being entitled to be treated as Tier 1 capital for regulatory reporting purposes) or following certain takeovers or schemes of arrangements. While the holder may initiate an exchange, IAG is able to select the method of exchange being either conversion into ordinary shares, arranging for a third party to acquire the RPS for their face value, or to redeem, buy back or cancel the RPS (subject to APRA approval). The RPS convert into ordinary shares that would rank equally in all respects with all other ordinary shares. All conversions into ordinary shares, other than a holder requesting conversion on a reset date, will receive a discount of 2.5% of the ordinary share price used in calculating the number of ordinary shares to be issued on conversion. The next reset date for RPS is 15 June 2012.

The RPS rank in priority to ordinary shares for the payment of dividends and in the event of a winding up. In a winding up, all RPS will rank equally for return of capital behind all other creditors of IAG, and ahead of ordinary shares. Except in limited circumstances, the RPS do not carry voting rights at general meetings. The RPS qualify as Innovative Tier 1 capital for the purposes of determining the IAG Group's APRA regulatory capital position.

II. Reset exchangeable securities

The reset exchangeable securities (RES) have a face value of \$550 million and were issued at par by IAG Finance (New Zealand) Limited, a wholly owned subsidiary of the Company. At 30 June 2009, the RES were presented net of the portfolio of assets (invested in high quality, short dated, fixed interest securities) backing the RES because of the legal right of set-off.

On 9 December 2009, the RES holders approved amendments to the RES terms and conditions. In accordance with the terms and conditions, the RES were brought onto the IAG Group's balance sheet with the corresponding assets of \$550 million included in investments.

The RES entitle the holder to a non-cumulative floating rate distribution payable quarterly. The distribution rate is based on the sum of three month Bank Bill Rate plus RES margin multiplied by (1 – tax rate). The RES margin is 4.00% per annum. Because of the hybrid nature of the securities, distributions on the RES are not the same as interest payments and may not always be paid, as there are a number of conditions that must be met before a distribution can be paid. If distributions are not paid on the RES, no dividends can be paid and no return of capital be made on ordinary shares unless IAG takes certain actions.

The RES may be exchanged into preference shares issued by IAG at the option of IAG (which have substantially similar terms to the RES) at any time and mandatorily in certain circumstances. The RES may be converted by either the issuer or the holder on a reset date, or upon acquisition event (such as change in control of IAG by a takeover bid) into ordinary shares. The RES can be redeemed, converted or resold by the issuer on a tax event (such as a more than insignificant increase in taxation costs), regulatory event (such as not all of the RES being entitled to be treated as Tier 1 capital for regulatory reporting purposes) or there are less than one million RES on issue. The RES may only be redeemed with the approval of APRA.

While the holder may request conversion, the issuer is able to select the method of response to the request being either conversion into ordinary shares, arranging for a third party to acquire the RES for their face value, or to redeem, buy back or cancel the RES (subject to APRA approval).

The RES convert into ordinary shares that would rank equally in all respects with all other ordinary shares. All conversions into ordinary shares will receive a discount of 2.5% of the ordinary share price used in calculating the number of ordinary shares to be issued on conversion. The next reset date for RES is 16 December 2019.

The RES rank in priority to ordinary shares for the payment of dividends and in the event of a winding up. In a winding up, all RES will rank equally for return of capital behind all other creditors of the IAG Group and ahead of ordinary shares. Except in limited circumstances, the RES do not carry voting rights at general meetings. The RES qualify as Innovative Tier 1 capital for the purposes of determining the IAG Group's APRA regulatory capital position.

III. USD subordinated term notes

The USD subordinated term notes had a face value of US\$240 million and were issued at par by NRMA Insurance Funding 2003 Limited (a wholly owned subsidiary of Insurance Australia Limited). They were fixed rate notes (5.19% payable semi annually), with the principal and interest flows denominated in US dollars and hedged with cross currency swaps and interest rate swaps. Cash flow hedge accounting was applied for this hedge arrangement (refer to the financial risk management note for further information). The notes qualified as Lower Tier 2 for the purposes of IAG Group's and Insurance Australia Limited's APRA regulatory capital position.

The issuer exercised its option to redeem the notes at face value on 28 April 2010 in accordance with their terms.

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 and were issued at a discount. They are fixed rate notes (5.625% payable annually) listed on the London Stock Exchange with the principal and interest flows denominated in British pounds. Amounts are translated into the equivalent Australian dollars using the reporting date exchange rate. The primary difference between the Australian dollar equivalent of the face value of the notes at inception and the carrying value is due to foreign exchange rate movements. The notes mature on 21 December 2026 (non-callable for the first 10 years). If the notes are not redeemed by 21 December 2016, all notes become floating rate notes with an interest rate of the three month GBP Libor plus 1.62%. The notes qualify as Lower Tier 2 capital for the purposes of the IAG Group's APRA regulatory capital position. The notes are used as an economic hedge to manage the foreign currency risk associated with investments in foreign operations.

The GBP subordinated term notes with face value of £144 million were bought back at 30% discount to face value during 2009 financial year. During the year ended 30 June 2010, £3 million of notes were bought back. The current outstanding face value of the notes as at reporting date is £103 million excluding £39 million of notes held by IAG. The notes are used as an economic hedge to manage the foreign currency risk associated with investments in foreign operations.

V. NZD subordinated term notes

The NZD subordinated term notes have a face value of NZ\$100 million, and were issued at par by Insurance Australia Funding 2007 Limited (a wholly owned subsidiary of Insurance Australia Limited). They are fixed rate notes with an interest rate of 9.105% per annum, payable semi annually. The notes mature in November 2017, however, they may be redeemed at par at the issuer's option from November 2012 onwards, subject to the approval of APRA. If the notes are not redeemed in November 2012, all notes become floating notes with an interest rate of the three months New Zealand Bank Bill Swap Rate plus a margin of 1.5% per annum. The notes qualify for Lower Tier 2 capital for the purposes of the IAG Group's and Insurance Australia Limited's APRA regulatory capital position. The notes are used as an economic hedge to manage the foreign currency risk associated with investments in foreign operations.

VI. GBP subordinated exchangeable term notes

The GBP subordinated exchangeable term notes were issued at par by Insurance Australia Limited with a face value of £157 million (equivalent to \$260 million at date of issue). The notes carry a deferrable, cumulative semi-annual interest payment with floating interest rate of six month GBP Libor plus 2.5% per annum.

The principal and interest flows are denominated in British pounds and are translated into the equivalent Australian dollars using the reporting date exchange rate. The primary difference between the Australian dollar equivalent of the face value of the notes at inception and the carrying value at reporting date is due to foreign exchange rate movements.

The notes mature on 20 April 2035, however, the notes may be exchanged at the option of the holder in October 2011, each subsequent interest payment date and in certain other circumstances, into ordinary shares of IAG, subject to the right of the issuer to redeem or require the transfer of the notes to IAG or a third party for cash (in either case with APRA's approval). The notes may also be redeemed by the issuer upon certain events, subject to APRA's approval (ie acquisition event, regulatory or tax event).

If an exchange occurs, the number of ordinary shares in IAG which will be issued in exchange for the notes will be calculated with reference to a 35 day volume weighted average price (other than in limited circumstances) adjusted for the exchange discount of 1.0% and an Australian dollar/British pound exchange rate.

The notes rank in priority to ordinary shares for the payment of dividend and in the event of a winding up. In a winding up, all notes will rank equally for return of capital behind all senior creditors of the issuer or IAG, and ahead of all shareholders of the issuer or IAG. Except in limited circumstances, the notes do not carry voting rights at general meetings. The notes qualify as Lower Tier 2 capital for the purposes of determining the IAG Group's APRA regulatory capital position. The notes are used as an economic hedge to manage the foreign currency risk associated with investments in foreign operations.

D. USE OF DERIVATIVES

The IAG Group uses derivatives to manage the exposure to risks relating to the interest bearing liabilities. Hedge accounting is applied to only a limited number of these arrangements. In each case where hedge accounting is applied the arrangements are designated as cash flow hedges. Additional information is provided below for those related derivative positions. For information regarding the notional contract amounts associated with these derivative financial instruments together with a maturity profile and reporting date fair values refer to the financial risk management note.

It is important to note that some of the interest bearing liabilities themselves are used to hedge currency risk relating to the net investment in foreign operations by forming part of arrangements for which hedge accounting is applied, refer to the financial risk management note.

I. Cross currency swaps on USD subordinated term notes

Insurance Australia Limited (IAL) had entered into cross currency swaps to fully hedge the Australian dollar value of principal and interest flows on the Consolidated entity's USD subordinated term notes. Over the term of the swaps, the Consolidated entity received US dollar payments equal to the interest payable on the notes and paid interest at either a fixed rate or variable rate of the three month bank bill swap rate plus a margin on a principal amount of A\$401 million. These swaps matured on 28 April 2010 and the principal amount of A\$401 million was paid and US\$240 million was received based on the original spot exchange rate at inception.

II. Interest rate swap agreements on USD subordinated term notes

IAL entered into interest rate swap agreements to manage the interest rate exposure on the Consolidated entity's USD subordinated term notes. IAL paid a fixed rate of interest under the swap agreements and received a variable rate of interest equal to the amount payable on the underlying hedged borrowings. These swaps matured on 28 April 2010.

E. FAIR VALUE INFORMATION

The interest bearing liabilities are initially measured at fair value (net of transaction costs) but are 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. A comparison of the carrying amount and fair value for the liabilities is provided in the table below.

	2010		2009	
	Carrying value \$m	Fair value \$m	Carrying value \$m	Fair value \$m
I. Capital nature				
a. TIER 1 REGULATORY CAPITAL				
Reset preference shares*	350	345	350	350
Reset exchangeable securities	550	550	–	–
b. TIER 2 REGULATORY CAPITAL				
USD subordinated term notes	–	–	295	298
Derivatives for USD subordinated term notes	–	–	111	111
GBP subordinated term notes*	183	154	220	168
NZD subordinated term notes	81	83	81	75
GBP subordinated exchangeable term notes	277	277	–	–
II. Operational nature				
Various instruments	14	14	–	–
Total	1,455		1,057	
Less: capitalised transaction costs	(5)		(4)	
	1,450		1,053	

* These instruments are liabilities of the Parent. The GBP subordinated term notes of the Parent are \$252 million (2009—\$293 million).

The differences between the carrying value of the liabilities and the fair value have been driven predominantly by widening credit spreads in the current period. Under the IAG Group's current accounting policy of measuring the interest bearing liabilities at amortised cost in line with the purpose and nature of the instruments, the differences in value will not be realised by the IAG Group as the liabilities are not transferable.

III. Methodology

The fair value of the individual interest bearing liabilities cannot be determined by simple reference to traded market prices with the exception of the reset preference shares and reset exchangeable securities for which the fair value is determined using the reporting date offer price per the Australian Securities Exchange. Hence the fair values have been determined by mark to model applying valuation techniques using objective market inputs sourced from third parties wherever possible. The inputs are based on financial instruments in the market around reporting date noting that some of the liabilities are not as directly comparable to other market instruments as some liabilities in which case a greater level of judgement has been applied in determining the inputs.

NOTE 24. NOTES TO THE STATEMENTS OF CHANGES IN EQUITY

	2010		2009	
	Number of shares in millions	Number of shares in millions	PARENT/CONSOLIDATED 2010 \$m	2009 \$m
A. SHARE CAPITAL				
Ordinary shares				
Balance at the beginning of the financial year	2,071	1,878	5,326	4,740
TRANSACTIONS WITH OWNERS IN THEIR CAPACITY AS OWNERS				
Shares issued under institutional placement, net of transaction costs	–	150	–	444
Share issued under Share Purchase Plan, net of transaction costs	–	28	–	83
Shares issued under Dividend Reinvestment Plan	8	15	27	59
Balance at the end of the year	2,079	2,071	5,353	5,326

All ordinary shares on issue are fully paid. 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 the Company in proportion to the number of, and amounts paid on, the shares held. Dividends, if declared, are subject to there being distributable profits available and not breaching APRA capital adequacy requirements.

I. 2010

The Company issued \$27 million ordinary shares to the Dividend Reinvestment Plan participants to fund the 2009 final dividend payment.

II. 2009

The Company made the following two issues of ordinary shares:

- \$450 million issued through a fully underwritten institutional placement at \$3 per ordinary share; and
- \$84.4 million issued through a share purchase plan at \$3 per ordinary share.

The Company made the following two issues of ordinary shares to fund dividend payments:

- 2009 interim dividend—\$17 million issued to the Dividend Reinvestment Plan participants; and
- 2008 final dividend—\$42 million issued to the Dividend Reinvestment Plan participants.

B. TREASURY SHARES HELD IN TRUST

Share based remuneration is provided in different forms to eligible employees. 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 held in trust. Upon consolidation of the trusts, the shares held that are controlled for accounting purposes are recognised as treasury shares held in trust, as described in note 1.AG. The balance of treasury shares held in trust at a reporting date represents the cumulative cost of acquiring IAG shares that have not yet been distributed to employees as share based remuneration.

C. NATURE AND PURPOSE OF RESERVES

I. 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 that have a functional currency other than Australian dollars.

II. Share based remuneration reserve

The share based remuneration reserve is used to recognise the fair value at grant date of equity settled share based remuneration provided to employees and non-executive directors over the vesting period, as described in section AA of the summary of significant accounting policies note.

III. Hedging reserve

The hedging reserve is used to record gains or losses on derivatives that form part of hedging relationships which have been designated as cash flows hedges or net investment hedges, as described in section Q of the summary of significant accounting policies note.

D. NON-CONTROLLING INTERESTS

Non-controlling interests in the following subsidiaries in the IAG Group are:

- Insurance Manufacturers of Australia Pty Limited (Australia)—30%;
- World Class Accident Repairs (Cheltenham North) Pty Limited (Australia)—30%;
- Mutual Community General Insurance Proprietary Limited (Australia)—49%;
- NHCT Limited (Thailand)—51%; and
- Safety Insurance Public Company Limited (Thailand)—1.5%.

NOTE 25. NOTES TO THE CASH FLOW STATEMENTS

	PARENT		CONSOLIDATED	
	2010	2009	2010	2009
	\$m	\$m	\$m	\$m
A. COMPOSITION				
Cash held for operational purposes	–	–	416	344
Cash and short term money held for investment	–	–	637	938
Cash and cash equivalents	–	–	1,053	1,282

Cash and cash equivalents represent cash on hand and held with banks, deposits at call and short term money held for investment readily convertible to cash within two working days, net of any bank overdraft. There are no cash balances held that are not available for use in normal operations. The carrying amount of the cash and cash equivalents presented on the balance sheets is the same as that used for the purposes of the cash flow statements as there are no bank overdrafts used which are repayable upon demand.

B. SIGNIFICANT RISKS

The net carrying amount of cash and cash equivalents represents the maximum exposure to credit risk relevant to cash and cash equivalents at reporting date and is equivalent to the fair value of the assets because of the negligible credit risk and frequent repricing.

A portion of the cash balances is held in currencies other than the Australian dollar. For information regarding the management of currency risk by the IAG Group refer to the financial risk management note.

The majority of the amounts bear variable rates of interest. Those balances bearing a fixed rate of interest mature in less than one year. A small portion of the amounts bear no interest.

	2010	PARENT 2009	CONSOLIDATED 2010	2009
	\$m	\$m	\$m	\$m
C. RECONCILIATION OF PROFIT/(LOSS) FOR THE YEAR TO NET CASH FLOWS FROM OPERATING ACTIVITIES				
Profit/(loss) for the year	221	302	190	247
I. Non cash items				
Depreciation and impairment of property and equipment	–	–	51	61
Amortisation and impairment of intangible assets and goodwill	–	–	137	94
Net realised (gains) and losses on disposal of investments	–	2	(227)	(100)
Net unrealised (gains) and losses on revaluation of investments	–	(1)	23	(63)
Net (gains) and losses on disposal of property and equipment	–	–	–	2
Provision for doubtful debts and impairment	–	–	5	11
Retained earnings adjustment for actuarial gains and (losses) on defined benefit superannuation plans	–	–	(2)	(65)
Retained earnings adjustment for share based remuneration	–	–	25	(17)
Unrealised (gains) and losses on embedded derivatives	96	(27)	96	(27)
Other	1	1	(11)	19
Net (gains) and losses on disposal of businesses	–	–	–	114
Realised gain on buyback of GBP subordinated term notes	–	(70)	(1)	(92)
II. Movement in operating assets and liabilities				
DECREASE/(INCREASE) IN OPERATING ASSETS				
Premium and other receivables	(31)	69	(202)	(199)
Prepayments and deferred levies and charges	–	–	116	52
Deferred tax assets	(41)	(23)	80	(102)
Current tax assets	49	(49)	80	(67)
Defined benefit superannuation asset	–	–	–	3
INCREASE/(DECREASE) IN OPERATING LIABILITIES				
Trade and other payables	(30)	35	166	115
Provisions	–	–	(36)	61
Current tax liabilities	–	(42)	57	(42)
Deferred tax liabilities	–	–	(4)	22
Outstanding claims liability	–	–	437	288
Unearned premium liability	–	–	135	111
Unexpired risk liability	–	–	–	(12)
Net cash flows from operating activities	265	197	1,115	414

D. 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.

NOTE 26. ACQUISITIONS AND DISPOSALS OF BUSINESSES

There were no acquisitions or disposals of businesses by the Parent during the current reporting period (2009—none). The following acquisitions and disposals of businesses relate to the Consolidated entity.

A. ACQUISITION OF SUBSIDIARIES

I. During the financial year ended 30 June 2010

a. ACQUISITION OF REGIONAL BROKING BUSINESS IN THE UNITED KINGDOM

During the current financial year, the United Kingdom business acquired an additional stake in a regional broking business to increase its share from 25% to 52.6% for \$1 million. This company is controlled by the United Kingdom segment and formed part of its segment results.

II. For the financial year ended 30 June 2009

a. ACQUISITION OF REGIONAL BROKING BUSINESSES IN THE UNITED KINGDOM

The IAG Group acquired a number of small regional brokers during the period with total consideration of \$1 million. The acquired businesses form part of the United Kingdom segment.

B. OTHER ACQUISITIONS

I. During the financial year ended 30 June 2010

a. INDIAN GENERAL INSURANCE VENTURE

On 19 November 2009, the Consolidated entity paid 5.4 billion Indian rupees (equivalent to \$126 million) to acquire a 26% strategic stake in SBI General Insurance Company Limited (SBI General), an Indian based general insurance company. The venture is a newly established business and commenced underwriting in March 2010. The net assets of SBI General as at 30 June 2010 were approximately 6.5 billion Indian rupees (equivalent to \$165 million).

b. NTI BUSINESS

In August 2009, CGU Insurance Limited reached an agreement with Suncorp's intermediated business, Vero, regarding the ongoing structure of the 50:50 NTI joint venture (NTI JV). The agreement allows the joint venture to continue, with the parties agreeing to the transfer of Suncorp's heavy motor vehicle book to the NTI JV from an agreed date at an agreed price which is confidential and which IAG has assessed as immaterial to the IAG Group. A customer relationship identifiable intangible asset was recognised during the current financial year.

II. For the financial year ended 30 June 2009

a. ACQUISITION OF A 25% STAKE IN REGIONAL INSURANCE BROKER IN AUSTRALIA

On 19 August 2008, the IAG Group acquired a 25% stake in NAS Insurance Broker, a general insurance brokerage based in Western Australia. This business forms part of the Australia intermediated insurance segment.

b. INCREASED INVESTMENT IN EXISTING GENERAL INSURANCE ASSOCIATE IN MALAYSIA

In December 2008, the IAG Group acquired an additional stake in the general insurance business of the existing associate AmAssurance (renamed to AmG), lifting the stake from 30% to 49% (the maximum allowable ownership under Malaysia's current foreign investment rules), funded through the sale of the interest in the life insurance component of the business from which a profit on disposal of \$38 million (net of \$2 million loss transferred from foreign currency translation reserve) is presented in the fee based, corporate and other expenses line in the statement of comprehensive income. At the same time an additional amount of risk based capital was injected into the business bringing the total costs of investment to \$132 million. For more detailed information refer to the market announcement (unaudited) on 1 December 2008 available at www.iag.com.au.

c. INCREASED INVESTMENT IN EXISTING GENERAL INSURANCE SUBSIDIARY IN THAILAND

In October 2008, the IAG Group increased its stake in Safety Insurance Public Company Limited from 96.09% to 98.47%.

C. DISPOSAL OF SUBSIDIARIES

I. During the financial year ended 30 June 2010

There was no disposal of subsidiaries by the Consolidated entity.

II. For the financial year ended 30 June 2009

a. UNITED KINGDOM MASS MARKET DISTRIBUTION BUSINESS

The IAG Group completed the sale of its mass market distribution businesses in the United Kingdom. The sale was effected through two separate transactions as set out below and resulted in the recognition of a total loss of \$119 million (including transaction costs and other costs incremental to the transactions) presented in the fee based, corporate and other expense lines in the statement of comprehensive income. The two transactions were:

- the Equity and Open & Direct branch networks (Branch networks) sold for £50 million (\$105 million). In addition to the loss on disposal, the IAG Group incurred other costs incremental to the transaction resulting in a total loss of \$25 million in relation to the sale of Branch networks. The sale of the business was completed on 8 January 2009; and
- the Hastings and Advantage businesses (Hastings and Advantage) sold via a management buy-out for £17 million (\$37 million). In addition to the loss on disposal, the IAG Group incurred other costs incremental to the transaction resulting in a total loss of \$94 million in relation to the sale of Hastings and Advantage. The sale of the business was completed on 3 February 2009.

	CONSOLIDATED	
	Hastings and Advantage \$m	Branch networks \$m
2009		
Sales proceeds		
Cash consideration	37	105
Transaction costs	(2)	(6)
Net cash consideration received	35	99
Fair value of net assets of businesses disposed		
Cash and cash equivalents	153	15
Investments	153	–
Receivables	322	10
Intangible assets	1	–
Trade and other payables	(149)	(31)
Unearned premium liability	(136)	–
Outstanding claims liability	(299)	–
Other assets	64	6
Acquired intangible assets disposed	18	89
Acquired goodwill disposed	–	12
Net identifiable assets disposed during the financial year	127	101
Net loss on disposals	(92)	(2)
Other costs necessarily incurred as part of the sale process and included in total costs on businesses held for sale	2	23

NOTE 27. DETAILS OF SUBSIDIARIES

The following entities constitute the Consolidated entity.

	TABLE NOTE	COUNTRY OF INCORPORATION/FORMATION	EXTENT OF BENEFICIAL INTEREST IF NOT 100%	
			2010 %	2009 %
A. ULTIMATE PARENT				
Insurance Australia Group Limited		Australia		
B. SUBSIDIARIES				
I. Australian general insurance operations				
Insurance Australia Limited		Australia		
NRMA Personal Lines Holdings Pty Limited		Australia		
Insurance Manufacturers of Australia Pty Limited		Australia	70.00	70.00
World Class Accident Repairs (Cheltenham North) Pty Limited		Australia	70.00	70.00
CGU Insurance Australia Limited		Australia		
CGU Insurance Limited		Australia		
Swann Insurance (Aust) Pty Ltd		Australia		
Mutual Community General Insurance Proprietary Limited		Australia	51.00	51.00
IAG Re Australia Limited		Australia		
Sitrof Australia Limited		Australia		
CGU-VACC Insurance Limited		Australia		
CGU Workers Compensation (NSW) Limited		Australia		
CGU Workers Compensation (VIC) Limited		Australia		
CGU Workers Compensation (SA) Limited		Australia		
Strata Unit Underwriting Agency Pty Limited		Australia		
ACN 007 078 140 Pty Limited (formerly Pacific Indemnity Underwriting Agency Pty Ltd)	A	Australia		
The Buzz Insurance Pty Limited	A	Australia		
The Buzz Australia Pty Limited	A	Australia		
II. New Zealand operations				
IAG (NZ) Holdings Limited	C	New Zealand		
IAG New Zealand Limited	C,D	New Zealand		
New Zealand Insurance Limited	C	New Zealand		
State Insurance Limited	C	New Zealand		
Direct Insurance Services Limited	C	New Zealand		
Belves Investments Limited	C	New Zealand		
Anthony Runacres and Associates Limited	C	New Zealand		
DriveRight Limited	C	New Zealand		
IAG (NZ) Share Plan Nominee Limited	C	New Zealand		
The IAG New Zealand Limited Employee Share Plan	C	New Zealand		
The IAG Performance Awards Rights Plan for Executives in New Zealand	C	New Zealand		
NZI Staff Superannuation Fund Nominees Limited	C	New Zealand		
III. United Kingdom operations				
IAG UK Holdings Limited	C	United Kingdom		
EIG (Investments) Limited	C	United Kingdom		
Equity Insurance Group Limited	C	United Kingdom		
Equity Insurance Holdings Ltd	C	United Kingdom		
Equity Red Star Limited	C	United Kingdom		
Equity Syndicate Management Limited	C	United Kingdom		
Equity Red Star Services Limited	C	United Kingdom		
Equity Insurance Management Limited	C	United Kingdom		
Equity Red Star Holdings Limited	C	United Kingdom		
Equity Insurance Properties Limited	C	United Kingdom		
CDCM (No2) Limited	C	United Kingdom		

	TABLE NOTE	COUNTRY OF INCORPORATION/ FORMATION	EXTENT OF BENEFICIAL INTEREST IF NOT 100%	
			2010	2009
			%	%
CDCM Limited	C	United Kingdom		
Equity Red Star (accident & health) Limited	C	United Kingdom		
HML Marketing Limited	C	United Kingdom		
Equity Claims Limited	C	United Kingdom		
Direct Insurance Services Limited	C	United Kingdom		
Equity Direct Broking Limited	C	United Kingdom		
Barnett & Barnett Holdings Limited	C	United Kingdom		
Barnett & Barnett Ltd	C	United Kingdom		
Barnett & Barnett Financial Services Ltd	C	United Kingdom		
EIG (Finance) Limited	C	United Kingdom		
Alba Group Pte Ltd	C	Singapore		
Alba Pte Ltd	C	Singapore		
Alba Underwriting Ltd	C	United Kingdom		
Diagonal Underwriting Agency Limited	C	United Kingdom		
AU No2 Limited (formerly Whittington Underwriting Limited)	C	United Kingdom		
EIG (Acquisitions) Ltd	C	United Kingdom		
Insurance Dialogue Ltd	C	United Kingdom	51.10	25.00
E Red Limited	C	United Kingdom		
Insurancwide Services Limited	C	United Kingdom		
IAG Finance (UK) LLP	C	Gibraltar		
IV. Other international operations				
IAG Re Labuan (L) Berhad	C	Malaysia		
IAG (Asia) General Insurance Pte Ltd	C	Singapore		
IAG Re Singapore Pte Ltd	C	Singapore		
NHCT Limited	C,E	Thailand	49.10	49.10
IAG Insurance (Thailand) Ltd	E	Thailand		
Safety Insurance Public Company Limited	E	Thailand	98.47	98.47
Beijing Continental Automobile Association Limited	C	China		
V. Investment operations				
IAG Asset Management Limited		Australia		
ACN 064 960 514 Pty Limited (formerly IAG Nominees Pty Limited)	A	Australia		
IAG Asset Management Cash Management Trust		Australia	87.43	95.99
IAG Asset Management Private Equity Trust		Australia	83.20	83.20
IAGAM Sustainable Investment Trust		Australia	50.00	50.00
Fixed Interest Technical Provisions Fund		Australia		
Fixed Interest Shareholders Fund		Australia		
VI. Corporate operations				
IAG International Pty Limited		Australia		
NRMA Information Services Pty Limited		Australia		
IAG Finance (New Zealand) Limited		Australia		
Insurance Australia Group Services Pty Limited		Australia		
IAG & NRMA Superannuation Pty Limited	A	Australia		
IAG Share Plan Nominee Pty Limited	A	Australia		
The IAG Share and Performance Award Rights Plan Trust		Australia		
The IAG Deferred Award Rights Plan		Australia		
The IAG Executive Performance Rights Plan		Australia		
Insurance Australia Funding 2007 Limited		Australia		
Empire Equity Australia Pty Limited (formerly Empire Equity Limited domiciled in Gibraltar until 16 December 2009)		Australia		
IAG Funding Partnership		Australia		

	TABLE NOTE	COUNTRY OF INCORPORATION/ FORMATION	EXTENT OF BENEFICIAL INTEREST IF NOT 100%	
			2010	2009
			%	%
C. SUBSIDIARIES THAT COMMENCED DEREGISTRATION DURING THE YEAR ENDED 30 JUNE 2010				
ACN 111 769 843 Pty Limited (formerly IAG Portfolio Limited)	A	Australia		
NRMA Insurance Funding 2003 Limited	A	Australia		
CGU Premium Funding Pty Limited	A	Australia		
D. SUBSIDIARIES THAT DEREGISTERED DURING THE YEAR ENDED 30 JUNE 2010				
Mike Henry Travel Insurance Limited	C	New Zealand	—	
National Auto Club Underwriters Agency (NZ) Limited	C	New Zealand	—	
Clipper Club Underwriters Limited	C	New Zealand	—	
Micro Wind Turbines Australia Pty Limited	A	Australia	—	50.00
E. ENTITIES PUT INTO LIQUIDATION DURING THE YEAR ENDED 30 JUNE 2010				
Equity Group 2005 Limited		United Kingdom	—	
Can Do Finance Limited		United Kingdom	—	
Equity Nominee Services Limited		United Kingdom	—	
ERSH Limited		United Kingdom	—	
Cox Managing Agency Limited		United Kingdom	—	
Equity Share Services Limited		United Kingdom	—	
Cox Commercial Limited		United Kingdom	—	
Brokersure.co.uk Limited		United Kingdom	—	
Anthony Kidd Agencies Limited		United Kingdom	—	
Logan Consultants Limited		Gibraltar	—	
Wedring Limited		United Kingdom	—	
IAG India (Mauritius)		Mauritius	—	
IAG Investments Management Services (Shanghai) Company Limited		China	—	

Table notes

- A Small proprietary companies that are not required to prepare, and have not prepared, audited financial statements.
- B Audited by accounting firms not affiliated with KPMG.
- C Audited by overseas KPMG firms.
- D All subsidiaries have only ordinary shares on issue except this entity also has perpetual preference shares on issue.
- E The following special conditions exist with respect to the IAG Group's Thailand subsidiaries:
- IAG International Pty Limited owns 49% of the share capital of NHCT Limited and has a majority voting right and the right to appoint the board of directors of NHCT Limited. Therefore, NHCT Limited is considered a subsidiary of IAG International Pty Limited. The remaining 51% is held by Alessi Capital Co., Ltd, a company registered in Thailand; and
 - IAG International Pty Limited owns 25% directly in IAG Insurance (Thailand) Ltd and is able to govern the financial and operating policies of the company through a further 75% interest held indirectly through its holding in NHCT Limited.

NOTE 28. INVESTMENT IN JOINT VENTURES AND ASSOCIATES

A. INTERESTS IN JOINT VENTURES AND ASSOCIATES

	TABLE NOTE	REPORTING DATE	COUNTRY OF INCORPORATION/FORMATION	PRINCIPAL ACTIVITY	CARRYING VALUE	CONTRIBUTION TO PROFIT	OWNERSHIP INTEREST	
					2010 \$m	2010 \$m	2010 %	2009 %
I. Joint ventures								
NTI Limited	A,C,D	30 June	Australia	Managing co-insurance arrangement	6	-	50.00	50.00
Assetinsure Financial Risk Products Pty Limited	A	30 June	Australia	Risk insurance products	-	-	-	50.00
II. Associates								
AmG Insurance Berhad*	C	31 March	Malaysia	Insurance underwriting	131	3	49.00	49.00
SBI General Insurance Company Limited	C	31 March	India	Insurance underwriting	137	-	26.00	-
First Rescue and Emergency (NZ) Limited	A,C	31 March	New Zealand	Roadside assistance	-	-	50.00	50.00
Loyalty New Zealand Limited	A,C	31 March	New Zealand	Loyalty program	-	-	25.00	25.00
Sureplan New Zealand Limited	A,C	31 March	New Zealand	Fleet risk management	-	-	30.00	30.00
AR Hub Pty Ltd	A,B	30 June	Australia	Software development	-	-	33.33	33.33
Arista Insurance Limited	A	31 December	United Kingdom	Wholesale broker	-	-	29.35	25.60
InsuranceWide.com Services Limited	A	31 December	United Kingdom	Online aggregator	6	-	35.00	26.70
Photosecure (NZ) Limited	A	30 June	New Zealand	Photographic security management	-	-	50.00	50.00
National Adviser Services Pty Ltd (formerly NAS Insurance Broker)	A	30 June	Australia	Insurance broker	3	-	25.00	25.00
					283	3		

* The contribution of AmG Insurance Berhad to the net profit of the IAG Group represents the share of associates' net profit of \$10 million offset by the regional support and development costs of \$7 million.

Table notes

- A Investment is measured at cost in the Consolidated entity due to materiality.
- B Small proprietary companies that are not required to prepare, and have not prepared, audited financial statements.
- C Audited by accounting firms not affiliated with KPMG.
- D The following special conditions exist with respect to the NTI Limited joint venture:
- CGU Insurance Limited, a subsidiary of the Consolidated entity, has a 50% interest in NTI Limited, the principal activity of which is to facilitate a co-insurance arrangement of commercial motor vehicle business. The Consolidated entity's portion of the results of the co-insurance arrangement is recorded directly in its accounting records.

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

	CONSOLIDATED	
	2010 \$m	2009 \$m
B. RECONCILIATION OF MOVEMENTS		
Balance at the beginning of the financial year	122	70
Investment in associate acquired	126	4
Additional investment in existing associate	10	41
Share of associates' net profit/(loss)*	10	8
Net foreign exchange movements	15	(1)
Balance at the end of the financial year	283	122

* The share of associates' net profit/(loss) for the current reporting period was \$10 million. The contribution of associates to the net profit of the IAG Group shown in section A includes regional support and development costs.

C. SUMMARISED FINANCIAL INFORMATION OF ASSOCIATE

These disclosures relate only to the investment in AmG Insurance Berhad, as all other investments in joint ventures and associates are not significant. The comparatives have been impacted by the IAG Group acquiring an additional stake in the general insurance business of the existing associate AmAssurance Berhad in December 2008, lifting the stake from 30% to 49%. The general insurance assets and liabilities and business of AmAssurance Berhad were transferred to AmG Insurance Berhad in the year ended 30 June 2009. The revenue and profit shown are for the financial year ended 31 March (for the comparatives, the financial period from date of incorporation (January 2009) to 31 March 2009). The figures provided in the table represent the financial position and performance of AmG Insurance Berhad as a whole and not just IAG's share (at 31 March).

	CONSOLIDATED	
	2010	2009
	\$m	\$m
Assets	340	315
Liabilities	237	146
Revenue	219	77
Profit	16	11

On 19 November 2009, the Consolidated entity purchased a 26% strategic stake in SBI General Insurance Company Limited. The net assets of the company as at the current financial reporting date were \$162 million. The company commenced underwriting insurance contracts in the final quarter of the year ended 30 June 2010. The revenue and profit for the current financial reporting period were not significant.

D. COMMITMENTS AND CONTINGENT LIABILITIES

There are no capital or other commitments or contingent liabilities arising from the investment in AmG Insurance Berhad and SBI General Insurance Company Limited that are significant to the Consolidated entity.

NOTE 29. EMPLOYEE BENEFITS

A. EMPLOYEE BENEFITS PROVISION

Annual leave	74	79
Long service leave	62	66
Cash based incentive arrangements	88	82
Defined benefit pension arrangements*	10	9
Defined benefit superannuation plan liabilities	64	85
	298	321

* There is one defined benefit pension arrangement in Australia with a discounted liability of \$7 million as at the current reporting date (2009—\$7 million) involving 71 participants (2009—72) and one defined benefit pension arrangement in New Zealand with a discounted liability of \$3 million as at the current reporting date (2009—\$2 million) involving 45 participants (2009—46). These liabilities are met from general assets rather than assets being set aside in trust.

The employee benefits provision includes \$113 million (2009—\$110 million) which is expected to be settled after more than 12 months from reporting date.

B. EMPLOYEE NUMBERS

The Consolidated entity had 12,481 employees on a full time equivalent basis as at 30 June 2010 (2009—12,655).

C. CASH BASED INCENTIVE ARRANGEMENTS

I. Short term incentive plan

The short term incentive plan continued in operation during the current reporting period. 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.

II. Insurance Manufacturers of Australia Pty Limited long term incentive scheme

A long term incentive is provided to senior employees of Insurance Manufacturers of Australia Pty Limited (IMA). This is a cash based incentive arrangement involving hurdles relating to compound growth in the IMA underwriting result over a three year period.

NOTE 30. SHARE BASED REMUNERATION

The provision of share based remuneration creates a link between shareholder value creation and rewarding employees. Share based remuneration encourages employee share ownership, links employee reward to the performance of the IAG Group and assists with retention of key personnel. This type of remuneration encourages employees to focus on creating shareholder value over the longer term.

The obligations under share based payment arrangements are covered by the on market purchase of IAG ordinary shares which are held in trust. The shares are purchased on or near grant date at the prevailing market price. The arrangements are managed using in-house trusts, one for Australia and one for New Zealand, which are controlled for accounting purposes and so are subsidiaries of the Consolidated entity. The trustee for each trust is a subsidiary of the Consolidated entity. The trusts are administered by an external company.

The number of shares purchased to cover each allocation of shares or rights is determined by the trustee based on independent actuarial advice. The trusts allow for excess shares purchased in relation to one plan to be used to meet obligations of the other plans at the trustee's discretion. The trusts held 13,033,476 shares as at 30 June 2010 (2009—12,643,703 shares) representing 0.63% (2009—0.61%) of the share capital. This includes shares that are not controlled for accounting purposes and so not recognised as treasury shares.

Trading in IAG ordinary shares that are awarded under the share based remuneration arrangements is covered by the same restrictions that apply to all forms of share ownership by employees. These restrictions limit an employee trading in IAG ordinary shares where they are in a position to be aware, or are aware, of price sensitive information.

Share based remuneration is provided through a range of different plans each of which has different purposes and different rules. The share based remuneration expense amounts are included in the claims expense, other underwriting expenses, and fee based, corporate and other expenses lines in the statement of comprehensive income.

A. NON-EXECUTIVE DIRECTORS' SHARE PLAN

The Non-executive Directors' Share Plan continued in operation during the current reporting period ended 30 June 2010 however no allocations were made in the year ended 30 June 2010. Until 2009, non-executive directors were required to receive at least 20%, but not in excess of 90%, of their annual IAG Board fee (at the time shares are allocated) in IAG ordinary shares, rather than in cash. Annual share allocations were generally made effective from 1 December each year. The shares vest on a pro rata daily basis with limited forfeiture conditions and the participant is entitled to dividends and other shareholder rights during the vesting period. The on market share price at grant date is used as the fair value of the equity instruments. The shares were purchased on market and held in trust subject to a restriction period, for tax purposes, of between one and 10 years.

The IAG Board has decided that there will be no further offers under the Non-executive Directors' Share Plan.

B. SENIOR MANAGEMENT AND EXECUTIVE SHARE PLANS

The senior management and executive share plan arrangements consist of two separate arrangements working together. These two arrangements are the Executive Performance Rights Plan and the Deferred Award Rights Plan which are detailed below. The IAG Nomination, Remuneration & Sustainability Committee (NRSC) approves the participation of each individual in the plans. Certain share plan arrangements remain in place but were closed to new offers in the prior reporting periods. Within each of these plans, there remain outstanding rights to be settled with the most significant being the Performance Award Rights Plan.

I. Deferred Award Rights Plan

The Deferred Award Rights Plan (DAR Plan) continued in operation during the current reporting period having been implemented in November 2006. The structure and operation of the plan are the same for employees in each region. The rights are granted for nil consideration, are non transferable, and can be settled only with existing IAG ordinary shares. Where the rights vest (the holder becomes entitled to exercise the right), the plan entitles participating employees to acquire one IAG ordinary share for each right. The exercise price for all rights is a nominal value of \$1 per tranche of rights exercised. Holders do not receive dividends and do not have voting rights until the rights are exercised. IAG ordinary shares are bought on market and held in trust to satisfy future exercise of the rights.

The rights vest after a period (current maximum is three years) as determined by the board subject to the participants continuing in relevant employment for the full period. When a participant ceases employment in special circumstances such as redundancy, rights may vest on cessation of employment. If there is a change of control of IAG, the board has discretion to determine if and when rights should vest.

If the vesting condition is not met then the rights lapse. The rights also lapse where the holder chooses to forgo the rights, and all rights expire 10 years (for rights granted prior to 1 July 2009) or seven years (for rights granted after 1 July 2009) from grant date where they have not previously lapsed or been exercised.

The following information relates to the rights issued under the DAR Plan.

GRANT DATE	FAIR VALUE AT GRANT DATE	RIGHTS ON ISSUE AT 1 JULY	RIGHTS GRANTED DURING THE YEAR	RIGHTS EXERCISED DURING THE YEAR	RIGHTS LAPSED DURING THE YEAR	NUMBER OF RIGHTS AT 30 JUNE	
						On issue	Exercisable
2010							
19/12/2006	\$5.354	1,047,042	–	(612,537)	(18,935)	415,570	415,570
13/03/2007	\$5.156	153,374	–	(99,750)	(9,000)	44,624	44,624
27/09/2007	\$4.820	1,920,100	–	(918,280)	(28,540)	973,280	502,680
11/02/2008	\$2.810	26,345	–	–	–	26,345	–
18/09/2008	\$3.668	4,546,700	–	(1,869,850)	(100,100)	2,576,750	692,900
27/02/2009*	\$3.263	48,908	–	(24,454)	–	24,454	–
27/02/2009*	\$3.155	40,000	–	–	–	40,000	–
27/02/2009*	\$3.397	10,000	–	–	–	10,000	10,000
27/02/2009*	\$3.311	15,000	–	–	–	15,000	7,500
25/09/2009	\$3.600	–	3,270,400	(221,800)	(59,500)	2,989,100	–
24/11/2009	\$3.770	–	158,200	–	–	158,200	–
25/03/2010	\$3.780	–	22,000	–	–	22,000	–
		7,807,469	3,450,600	(3,746,671)	(216,075)	7,295,323	1,673,274
2009							
19/12/2006	\$5.354	2,024,009	–	(722,910)	(254,057)	1,047,042	–
13/03/2007	\$5.156	209,062	–	(49,313)	(6,375)	153,374	–
27/09/2007	\$4.820	4,574,450	–	(2,474,890)	(179,460)	1,920,100	468,850
11/02/2008	\$2.810	26,345	–	–	–	26,345	–
14/04/2008	\$3.330	55,370	–	(55,370)	–	–	–
18/09/2008	\$3.668	–	5,059,050	(421,950)	(90,400)	4,546,700	–
27/02/2009*	\$3.263	–	48,908	–	–	48,908	–
27/02/2009*	\$3.155	–	40,000	–	–	40,000	–
27/02/2009*	\$3.397	–	10,000	–	–	10,000	–
27/02/2009*	\$3.311	–	15,000	–	–	15,000	–
		6,889,236	5,172,958	(3,724,433)	(530,292)	7,807,469	468,850

* Rights issued on the same grant date may have different fair values to reflect different vesting periods.

In addition to the grant of rights shown above, an additional 2,141,470 rights were issued from 8 January 2007 as part of the consideration for the acquisition of Equity Insurance Group. These rights were vested and exercisable in January 2010. The weighted average share price for rights exercised for the year ended 30 June 2010 was \$3.76.

The fair value of the rights is calculated as at the grant date using a Black Scholes valuation.

SIGNIFICANT FACTORS AND ASSUMPTIONS			
2010			
Grant date	25/09/2009	24/11/2009	25/03/2010
Share price on grant date (\$)	\$3.74	\$3.90	\$3.91
Exercise price (\$)	\$1 per tranche exercised	\$1 per tranche exercised	\$1 per tranche exercised
Risk free interest rate (%)	5.08%	5.20%	5.42%
Expected dividend yield (%)	2.64%	2.53%	3.64%
Expected life of rights (years)	2 years	2 years	2 years
2009			
Grant date		18/09/2008	27/02/2009
Share price on grant date (\$)		\$4.02	\$3.44
Exercise price (\$)		\$1 per tranche exercised	\$1 per tranche exercised
Risk free interest rate (%)		6.37%	3.66%
Expected dividend yield (%)		5.45%	3.71%
Expected life of rights (years)		2 years	1 or 2 years

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.

II. Executive Performance Rights Plan

The Executive Performance Rights Plan (EPR Plan) continued in operation during the current reporting period having been implemented in October 2007. The structure and operation of the plan are the same for employees in each region. The rights are granted for nil consideration, are non transferable, and can be settled only with IAG ordinary shares. Where the rights vest (the holder becomes entitled to exercise the right), the EPR Plan entitles participating employees to acquire one IAG ordinary share for each right. There is no exercise price. Holders do not receive dividends and do not have voting rights until the rights are exercised. IAG ordinary shares are bought on market and held in trust to satisfy future exercise of the rights.

Rights allocations are divided equally into two portions (TSR allocation and ROE allocation) and each portion has two vesting conditions. The first vesting condition for both portions is not market related and requires the participant to continue in relevant employment. Rights may be retained when a participant ceases employment in special circumstances such as redundancy.

Under the TSR allocation, the second vesting condition is a market related performance hurdle based on a comparison of IAG's total shareholder return (TSR, the measure of return on an investment in IAG ordinary shares) with the TSR of a peer group of entities. For allocations made prior to 30 June 2009, the peer group consists of entities in the S&P/ASX 100 Index and for allocations made after 30 June 2009, the peer group consists of entities in the top 50 industrials within the S&P/ASX 100 Index.

For the performance hurdle, a tiered vesting scale is applied, such that all rights in the TSR allocation vest if IAG's relative TSR is at the 75th percentile of the peer group, scaling down so that 50% of rights in the TSR allocation vest if IAG's TSR performance is at the 50th percentile of the peer group. No rights vest if IAG's TSR performance is below the 50th percentile of the peer group. Testing for the satisfaction of the performance hurdle occurs on the third, fourth and fifth anniversary of the base date. If this vesting condition is not met, the TSR allocation will lapse. The rights also lapse where the holder chooses to forgo the rights and all rights expire 10 years from grant date (for rights granted prior to 1 July 2009) or seven years from the grant date (for rights granted after 1 July 2009) where they have not previously lapsed or been exercised.

Under the ROE allocation, the second vesting condition is based on IAG's ROE which is a performance hurdle that is not market related. The ROE hurdle compares IAG's return on equity (ROE) performance with IAG's weighted average cost of capital (WACC) (WACC of IAG is determined by the IAG Board).

ROE is measured for each half year and compared to WACC for that half year period. The average of the six half year measurements over three financial years indicates whether any rights vest. For any of the ROE portion of the rights to vest and be exercisable for shares:

- normalised ROE for series 1 rights must reach at least 1.3 times WACC; and
- cash ROE for series 2 and 3 rights must reach at least 1.5 times WACC.

LEVEL OF NORMALISED ROE PERFORMANCE	LEVEL OF CASH ROE PERFORMANCE	VESTING SCALE
Rights granted before 30 June 2008	Rights granted after 30 June 2008	
>1.6 x WACC	>1.8 x WACC	100% vests
=1.5 x WACC	=1.7 x WACC	80% vests
=1.4 x WACC	=1.6 x WACC	50% vests
=1.3 x WACC	=1.5 x WACC	20% vests
<1.3 x WACC	<1.5 x WACC	0% vests

A sliding scale operates between the points represented in the table above. If ROE is less than 1.3 times WACC for rights granted before 30 June 2008 or less than 1.5 times WACC for rights granted after 30 June 2008, no rights in the ROE allocation will vest. If this vesting condition is not met, the ROE allocation will lapse. The rights also lapse where the holder chooses to forgo the rights and all rights expire 10 years (for rights granted prior to 1 July 2009) or seven years (for rights granted after 1 July 2009) from grant date where they have not previously lapsed or been exercised.

If there is a change of control of IAG, the board has discretion to determine if and when rights should vest.

The following information relates to the rights issued under the EPR Plan.

GRANT DATE	FAIR VALUE AT GRANT DATE (TSR)	FAIR VALUE AT GRANT DATE (ROE)	RIGHTS ON ISSUE AT 1 JULY	RIGHTS GRANTED DURING THE YEAR	RIGHTS EXERCISED DURING THE YEAR	RIGHTS LAPSED DURING THE YEAR	NUMBER OF RIGHTS AT 30 JUNE	
							On issue	Exercisable
2010								
GRANT DATE								
29/10/2007	\$2.870	\$4.310	1,968,800	–	–	(75,750)	1,893,050	–
29/11/2007	\$2.350	\$3.680	250,000	–	–	–	250,000	–
13/03/2008	\$1.630	\$2.710	152,400	–	–	–	152,400	–
27/05/2008	\$2.120	\$3.220	65,370	–	–	–	65,370	–
18/09/2008	\$2.530	\$3.410	4,842,900	–	–	(51,500)	4,791,400	–
27/02/2009	\$2.570	\$3.150	250,000	–	–	–	250,000	–
25/09/2009	\$2.480	\$3.480	–	3,968,500	–	(33,800)	3,934,700	–
24/11/2009	\$2.590	\$3.650	–	790,600	–	–	790,600	–
25/03/2010	\$2.050	\$2.460	–	171,400	–	–	171,400	–
			7,529,470	4,930,500	–	(161,050)	12,298,920	–
2009								
GRANT DATE								
29/10/2007	\$2.870	\$4.310	2,340,800	–	–	(372,000)	1,968,800	–
29/11/2007	\$2.350	\$3.680	250,000	–	–	–	250,000	–
13/03/2008	\$1.630	\$2.710	152,400	–	–	–	152,400	–
27/05/2008	\$2.120	\$3.220	65,370	–	–	–	65,370	–
18/09/2008	\$2.530	\$3.410	–	4,871,900	–	(29,000)	4,842,900	–
27/02/2009	\$2.570	\$3.150	–	250,000	–	–	250,000	–
			2,808,570	5,121,900	–	(401,000)	7,529,470	–

The fair value of the rights is calculated as at the grant date using the Monte Carlo simulation methodology. The valuations take into account the probability of achieving the market related performance hurdle.

Some of the assumptions, including expected share price volatility, 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.

SIGNIFICANT FACTORS AND ASSUMPTIONS

2010			
Grant date	25/09/2009	24/11/2009	25/03/2010
Share price on grant date (\$)	\$3.74	\$3.90	\$3.91
Risk free interest rate (%)	5.08%	5.20%	5.42%
Expected dividend yield (%)	2.64%	2.53%	3.64%
Expected life of rights (years)*	3 or 4 years	3 or 4 years	3 or 4 years
2009			
Grant date		18/09/2008	27/02/2009
Share price on grant date (\$)		\$4.02	\$3.44
Risk free interest rate (%)		6.37%	3.66%
Expected dividend yield (%)		5.45%	3.71%
Expected life of rights (years)*		3 or 4 years	3 or 4 years

* The expected life for the ROE rights is three years and four years for TSR rights.

III. Performance Award Rights Plan

The Performance Award Rights Plan (PAR Plan) closed to new offers during the year ended 30 June 2007. The last performance hurdle testing date for the rights is expected to be 29 August 2011. The structure and operation of the plan are the same for employees in each region. The rights were granted for nil consideration, are non transferable, and can be settled only with existing IAG ordinary shares. Where the rights vest (the holder becomes entitled to exercise the right), the plan entitles participating employees to acquire one IAG ordinary share for each right. The exercise price for all rights is a nominal value of \$1 per tranche of rights exercised. Holders do not receive dividends and do not have voting rights until the rights are exercised. IAG ordinary shares are bought on market and held in trust to satisfy future exercise of the rights.

The rights may vest between three and five years (the performance period) from a base date (calculation date for each tranche) subject to the satisfaction of two vesting conditions. The first vesting condition is not market related and requires the participant to continue in relevant employment. The second vesting condition is a market related performance hurdle based on a comparison of IAG's total shareholder return (TSR, the measure of return on an investment in IAG ordinary shares) with the TSR of a peer group of companies in the S&P/ASX 100 Index. The peer group includes insurers and non insurers because the IAG Group competes for capital with a range of large listed companies across many industries. For the performance hurdle, a tiered vesting scale is applied, such that all rights vest if IAG's relative TSR is at the 75th percentile of the peer group, scaling down so that 50% of rights vest if IAG's TSR performance is at the 50th percentile of the peer group. No rights vest if IAG's TSR performance is below the 50th percentile of the peer group. Testing for the satisfaction of the performance hurdle occurs quarterly during the performance period. If either of the vesting conditions is not met then the rights lapse. The rights also lapse where the holder chooses to forgo the rights, and all rights expire 10 years from grant date where they have not previously lapsed or been exercised.

If there is a change of control of IAG, the board has discretion to determine if and when rights should vest.

The following information relates to the rights issued under the PAR Plan.

GRANT DATE	FAIR VALUE AT GRANT DATE	RIGHTS ON ISSUE AT 1 JULY	RIGHTS GRANTED DURING THE YEAR	RIGHTS EXERCISED DURING THE YEAR	RIGHTS LAPSED DURING THE YEAR	NUMBER OF RIGHTS AT 30 JUNE	
						On issue	Exercisable
2010							
24/12/2002	\$1.870	49,996	-	-	-	49,996	49,996
17/09/2004	\$2.715	2,697,000	-	-	(2,697,000)	-	-
30/11/2004	\$2.718	251,000	-	-	(251,000)	-	-
30/03/2005	\$3.269	34,000	-	-	(34,000)	-	-
19/09/2005	\$3.187	2,319,530	-	(278,170)	(1,061,600)	979,760	184,880
30/11/2005	\$2.596	40,530	-	(8,100)	(17,250)	15,180	-
22/03/2006	\$3.145	91,800	-	-	-	91,800	4,860
19/12/2006	\$4.013	2,571,821	-	-	(113,621)	2,458,200	-
13/03/2007	\$3.660	282,000	-	-	(12,000)	270,000	-
		8,337,677	-	(286,270)	(4,186,471)	3,864,936	239,736
2009							
24/12/2002	\$1.870	96,720	-	(46,724)	-	49,996	49,996
22/09/2003	\$2.840	2,327,782	-	-	(2,327,782)	-	-
10/12/2003	\$2.764	400,000	-	-	(400,000)	-	-
26/03/2004	\$3.287	599,308	-	-	(599,308)	-	-
17/09/2004	\$2.715	3,669,000	-	-	(972,000)	2,697,000	-
30/11/2004	\$2.718	877,000	-	-	(626,000)	251,000	-
30/03/2005	\$3.269	41,000	-	-	(7,000)	34,000	-
19/09/2005	\$3.187	3,968,500	-	(1,600,110)	(48,860)	2,319,530	446,040
30/11/2005	\$2.596	670,500	-	(29,970)	(600,000)	40,530	8,100
22/03/2006	\$3.145	189,000	-	(97,200)	-	91,800	4,860
19/12/2006	\$4.013	2,895,200	-	-	(323,379)	2,571,821	-
13/03/2007	\$3.660	298,500	-	-	(16,500)	282,000	-
		16,032,510	-	(1,774,004)	(5,920,829)	8,337,677	508,996

All rights granted on 17/09/2004, 30/11/2004, 30/03/2005 and 19/09/2005 lapsed due to performance hurdles not being met.

The fair value of the rights is calculated as at the grant date using the Monte Carlo simulation methodology. The valuations take into account the probability of achieving the market related performance hurdle.

Some of the assumptions, including expected share price volatility, 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.

C. EMPLOYEE SHARE PLANS

Three new employee share plans were established in the financial year ended 30 June 2010 in Australia, New Zealand and the United Kingdom which give employees the opportunity to own a stake in IAG and share in the IAG Group's future success.

Under the plans, shares are purchased under salary sacrifice arrangements, allowing employees to acquire shares in a tax effective manner, and IAG contributes towards 10% of the cost of the share purchase. IAG ordinary shares taken up through the plans do not incur any brokerage. The salary sacrifice arrangements and structure of the plans differ between jurisdictions to comply with local legislation and utilise tax concessions.

NOTE 31. SUPERANNUATION

Contributions are made to a number of superannuation plans in various countries. The majority of employees are defined contribution members with fewer than 5.3% (2009—5.6%) of employees participating on a defined benefit basis. Entry to defined benefit superannuation plans is closed and so all new employees are provided with defined contribution arrangements. The plans provide benefits for members or their dependants in the form of lump sum or pension payments generally upon retiring from relevant employment.

The superannuation expense for the year is included in the claims expense, other underwriting expenses, and fee based, corporate and other expenses lines in the statement of comprehensive income.

A. DEFINED CONTRIBUTION SUPERANNUATION ARRANGEMENTS

Contributions to the plans are made in accordance with the governing rules of each plan together with relevant legislative requirements in each geographical region. The contributions are generally based on a percentage of employees' salaries.

The Consolidated entity is not exposed to risks or rewards of the defined contribution arrangements and has no obligations beyond the payment of contributions. There were no employer contributions payable at the end of the year for defined contribution members (2009—\$Nil).

B. DEFINED BENEFIT SUPERANNUATION ARRANGEMENTS

Employees who are entitled to defined benefit superannuation arrangements are members of one of seven superannuation plans each of which are funded plans. The defined benefit sections of those plans are closed to new members and so membership is reducing over time. Contributions to the plans are made in accordance with the governing rules of each plan and the contribution recommendations of an independent actuary. In contrast to defined contribution superannuation arrangements, the future cost of the defined benefit superannuation plans is not known with certainty in advance. The benefits received by defined benefit members are generally based on length of service and/or final average salary and/or age together with the member's own contributions (if any). The net financial positions of the plans are recognised on the balance sheet.

I. Australia

All Australian employees with defined benefit superannuation arrangements are members of the IAG & NRMA Superannuation Plan (IAG Plan). There were 632 members as at reporting date (2009—687). The Consolidated entity has contributed to the IAG Plan during the year in accordance with the recommendations of the actuary and has contributed \$9 million for defined benefit members (2009—\$7 million). There were no employer contributions payable at the end of the year (2009—\$Nil). The governing rules of the IAG Plan allow any surplus to be used to meet the contributions that would otherwise have been payable for both the defined benefit and defined contribution members of the IAG Plan.

The employer contribution rate for Australia defined benefit members remained at 16% with an additional quarterly payment of \$1 million to restore the financial position of the IAG Plan.

There are two subsidiaries in the Consolidated entity, being Insurance Australia Group Services Pty Limited and Insurance Manufacturers of Australia Pty Limited, with employees that are defined benefit members of the IAG Plan. While separate records are maintained for the liabilities relating to each member, there is effectively a sharing of the risks associated with the assets of the IAG Plan. For the measurement of the net financial position of the IAG Plan for recognition on the balance sheets of the employer sponsors, the assets of the IAG Plan are allocated between the employers in proportion to the actuarial reserves for each entity.

II. United Kingdom

The United Kingdom operation contributes to five defined benefit superannuation arrangements (UK Plans) being The Christopherson's Final Salary Scheme, The Red Star Insurance Association Limited 1978 Retirement and Death Benefit Scheme, The Anthony Kidd Agencies Scheme and schemes within the Lloyd's Superannuation Fund (a multi-employer scheme) being the Cox Services Limited Staff Pension Scheme and the HML Marketing Limited Staff Pension Scheme. The UK Plans had 543 defined benefit members as at reporting date (2009—555). The Consolidated entity contributed \$7 million to the UK Plans for defined benefit members during the year (2009—\$7 million).

None of the UK Plans is individually significant to the financial report and so the information disclosed below is provided for the UK Plans in aggregate.

	IAG PLAN		UK PLANS		TOTAL	
	2010	2009	2010	2009	2010	2009
	\$m	\$m	\$m	\$m	\$m	\$m
a. REPORTING DATE BALANCES						
Fair value of plan assets	151	143	108	103	259	246
Present value of defined benefit obligation (net discount rate)	(199)	(194)	(124)	(138)	(323)	(332)
Net defined benefit asset/(liability)	(48)	(51)	(16)	(35)	(64)	(86)
Net asset/(liability) recognised on the balance sheet	(48)	(51)	(16)	(35)	(64)	(86)

Where a plan incorporates both defined benefit and defined contribution arrangements, the amounts disclosed in this note represent only the defined benefit portion of the plan. Actuarial valuations are performed at each reporting date by an independent specialist. The financial information disclosed has been prepared in accordance with AASB 119 Employee Benefits except where otherwise noted.

Those plans with a net financial position that is an asset are presented with the defined benefit superannuation asset on the balance sheet while those plans with a net financial position that is a liability are presented within the employee benefits provision.

	IAG PLAN		UK PLANS	
	2010	2009	2010	2009
	\$m	\$m	\$m	\$m
b. RECOGNITION OF MOVEMENTS IN NET ASSET/(LIABILITY)				
Contributions expensed	9	7	7	7
Reporting date valuation adjustment to profit	(2)	(2)	(5)	(7)
	7	5	2	–
Reporting date valuation adjustment to retained earnings	–	55	(9)	35
Total amount recognised for financial year in closing retained earnings	7	60	(7)	35
Reporting date valuation adjustments represent				
Current service cost	6	6	–	–
Past service cost	1	1	–	–
Interest cost (net of tax)	10	11	7	7
Expected return on plan assets	(10)	(13)	(5)	(7)
Actuarial (gains) and losses	–	55	(9)	35
Total net amount recognised from reporting date valuation	7	60	(7)	35
c. RECONCILIATION OF MOVEMENTS IN THE PRESENT VALUE OF DEFINED BENEFIT OBLIGATION				
Defined benefit obligation at the beginning of the financial year	194	176	138	124
Current service cost	6	6	–	–
Past service cost	1	1	–	–
Interest cost	10	11	7	7
Contributions by plan participants	2	3	–	–
Actuarial (gains) and losses	9	18	2	11
Benefits paid	(23)	(21)	(4)	(2)
Disposal through sale of business	–	–	–	(2)
Net exchange difference on translation of foreign operations	–	–	(19)	–
Defined benefit obligation at the end of the financial year	199	194	124	138
d. RECONCILIATION OF MOVEMENTS IN THE FAIR VALUE OF ASSETS				
Fair value of plan assets at the beginning of the financial year	143	179	103	117
Expected return on plan assets	10	12	6	7
Actuarial gains and (losses)	10	(37)	11	(24)
Contributions by employers	9	7	7	7
Contributions by plan participants	2	3	–	–
Benefits paid	(23)	(21)	(4)	(2)
Disposal through sale of business	–	–	–	(2)
Net exchange difference on translation of foreign operations	–	–	(15)	–
Fair value of plan assets at the end of the financial year	151	143	108	103

e. PLAN ASSETS

The percentage invested in each asset class at reporting date is shown in the table below.

	IAG PLAN		UK PLANS	
	2010	2009	2010	2009
	%	%	%	%
Australian shares	37.0	38.0	–	–
Overseas shares	21.0	22.0	39.0	34.0
Listed property trusts	10.0	8.0	–	–
Fixed interest	27.0	25.0	52.0	65.0
Cash	3.0	3.0	4.0	1.0
Other	2.0	4.0	5.0	–

The assets of the IAG Plan do not include any shares issued by the Consolidated entity nor do they include other assets used by the Consolidated entity. The assets of the UK Plans are managed by independent trustee boards.

To determine the expected rate of return on assets, the actuary has considered the expected future investment returns for each major asset class net of investment tax and investment fees. These estimated returns for each asset class have been used to calculate the expected rate of return on the assets supporting the defined benefits based on the plans' target asset allocation and allowing for correlations of the investment returns between asset classes. The actual return on the IAG Plan assets for the current reporting period was a gain of 11.1% (2009—loss of 10.3%). The actual return on the UK Plans assets for the current reporting period was a gain of 16.3% (2009—loss of 14.5%).

f. ACTUARIAL ASSUMPTIONS

Assumptions used in the determination of the financial position of the plans are reviewed annually and determined in conjunction with the independent actuaries to the plans. The principal actuarial assumptions used in determining the financial position of the plans include:

Discount rate (gross)*	5.1	5.5	5.7	6.1
Expected rate of return on plan assets supporting pension liabilities	8.3	7.4	5.6	5.7
Expected rate of return on other plan assets	7.0	6.9	5.6	5.7
Expected future salary increases	4.0	4.0	5.0	5.3
Future pension increases adult/child	2.5/0.0	2.5/0.0	3.5/0.0	3.8/0.0

* The discount rate for the IAG Plan has been determined by reference to the market yields on 10 year government bonds in Australia. The UK Plans discount rate has been determined by reference to the market yields on AA rated corporate bonds in the United Kingdom.

g. SENSITIVITY OF MEASUREMENT TO ACTUARIAL ASSUMPTIONS

The superannuation arrangements are by nature long term. The majority of the assumptions reflect this and are not changed to reflect short term variations in factors. The discount rate applied for the IAG Plan reflects the market yields on government bonds and so is subject to change if those yields change. A 1% reduction in the discount rate would result in a \$26 million increase in the present value of the defined benefit obligation of the IAG Plan and result in a net financial deficit of \$74 million.

	IAG PLAN					UK PLANS			
	2010	2009	2008	2007	2006	2010	2009	2008	2007
	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Present value of defined benefit obligation	(199)	(194)	(176)	(165)	(187)	(124)	(138)	(124)	(162)
Fair value of plan assets	151	143	179	215	191	108	103	117	141
Surplus/(deficit) in the plan	(48)	(51)	3	50	4	(16)	(35)	(7)	(21)
Experience adjustments arising on plan liabilities gain/(loss)	–	(7)	(4)	6	6	(1)	(11)	(9)	2
Experience adjustments arising on plan assets gain/(loss)	10	(37)	(41)	16	10	3	(19)	6	–

The experience adjustments are based on the actuarial gain or loss after removing the impact of any change in assumptions.

i. FUNDING OBLIGATIONS FOR THE IAG & NRMA SUPERANNUATION PLAN IN AUSTRALIA

The financial information disclosed below has been determined in accordance with AAS 25 Financial Reporting by Superannuation Plans, using the Attained Age Actuarial Funding method.

	CONSOLIDATED	
	2010	2009
	\$m	\$m
Net market value of plan assets	151	143
Present value of accrued benefits	(158)	(164)
Defined benefit surplus/(deficit)	(7)	(21)
Vested benefits	154	162

	CONSOLIDATED	
	2010	2009
	%	%
The principal actuarial assumptions used in determining the financial position of the IAG Plan in accordance with AAS 25 and the funding recommendation include:		
Expected investment returns—pension assets/other assets (gross)	7.5	7.5
Expected future salary increases	4.0	4.0
Future pension increases—adult/child	2.5/0.0	2.5/0.0

The accrued benefits are determined on the basis of the present value of expected future payments that arise from membership up to the measurement date. The accrued benefits are determined by reference to expected future salary levels and are discounted by using a market based, risk adjusted discount rate. Vested benefits are the benefits which would be payable to members if they all voluntarily resigned as at the reporting date.

Assumptions used in the determination of the financial position of the IAG Plan are reviewed annually and determined in conjunction with the independent actuary to the IAG Plan. Changes in financial and/or demographic assumptions, or changes in the relevant regulatory environment, could significantly impact the financial position of the IAG Plan. The financial position of the plan is calculated at a specific point in time, however the superannuation arrangements are by nature long term. Short term variations between long term actuarial assumptions and actual experience will cause the net funding status of the IAG Plan to change without impacting on the long term viability of the plan.

The contribution recommendation uses a different actuarial methodology and a different discount rate assumption to that used in determining the financial position for measurement on the balance sheet of the employer sponsor. In determining the contribution recommendation, the actuarial valuation method focuses on the funding of benefits for current members, irrespective of whether they stem from past or future membership, whereas, for financial reporting purposes, the present value of expected future benefit payments does not include benefits that have not yet accrued. The difference in methodologies used for determining the employer contributions and the measurement of the asset/liability recognised on the balance sheet means that a liability may be recognised even where the employer has met all of the superannuation contribution obligations.

NOTE 32. COMMITMENTS

	CONSOLIDATED	
	2010	2009
	\$m	\$m
A. CAPITAL COMMITMENTS		
I. Software development		
Due within 1 year	7	9
Due within 1 to 2 years	7	9
Due within 2 to 5 years	14	30
Due after 5 years	–	23
	28	71
B. OPERATING LEASE COMMITMENTS		
I. Property		
Due within 1 year	101	99
Due within 1 to 2 years	98	93
Due within 2 to 5 years	247	249
Due after 5 years	335	384
II. Plant and equipment		
Due within 1 year	18	19
Due within 1 to 2 years	15	15
Due within 2 to 5 years	5	5
	819	864

Certain property, motor vehicles and computer equipment are leased under non cancellable operating leases. Most leases are subject to annual reviews with increases subject to a set percentage or based on either movements in consumer price indices or operating criteria. Where appropriate, a right of renewal has been incorporated into the lease agreements at which time all terms and conditions may be renegotiated. There are no options to purchase the relevant assets on expiry of the lease.

	CONSOLIDATED	
	2010	2009
	\$m	\$m
C. SOFTWARE LICENCE AND RENTAL COMMITMENTS		
Due within 1 year	30	31
Due within 1 to 2 years	17	18
Due within 2 to 5 years	1	11
	48	60
D. OTHER COMMITMENTS		
Due within 1 year	11	7
	11	7

NOTE 33. CONTINGENCIES

The IAG Group is exposed to a range of contingencies. Some are specific to instruments or transactions, others relate more to risk faced in the normal course of business.

A. CONTINGENT LIABILITIES

Contingent liabilities are not recognised on the balance sheet but are disclosed here 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. The measurement involves judgement.

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;
- undertakings for maintenance of net worth and liquidity support to subsidiaries in the Consolidated entity. It is normal practice to provide wholly owned subsidiaries with support and assistance as may be appropriate with a view to enabling them to meet their obligations and to maintain their good standing. Such undertakings constitute a statement of present intent only and are not intended to give rise to any binding legal obligation; and
- guarantees for performance obligations, including a guarantee in relation to a standby letter of credit issued in support of the Consolidated entity's participation in Lloyd's of London.

It is not believed that there are any other potential material exposures to the Parent and there are no known events that would require it to satisfy the guarantees or take action under a support agreement.

B. FIDUCIARY ACTIVITIES

The Consolidated entity's fiduciary activities consist of investment management and other fiduciary activities conducted 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 current reporting date of \$461 million (2009—\$394 million). This does not include the investment by third parties in the IAG Asset Management Wholesale Trusts presented as non-controlling interests in unitholders' funds on the balance sheet. The Consolidated entity is exposed to operational risk relating to managing these funds on behalf of third parties.

NOTE 34. RELATED PARTY DISCLOSURES

A. CONTROLLING ENTITIES

The ultimate parent entity in the Consolidated entity is Insurance Australia Group Limited which is incorporated in Australia.

The Consolidated entity consists of Insurance Australia Group Limited and its subsidiaries (information in relation to ownership interests is provided in the subsidiaries note).

The IAG Group currently operates under a devolved model but there are shared services through the use of dedicated units (such as head office finance providing accounting and processing services to operational entities) and entities (such as dedicated entities that provide employee services, technology development services, and reinsurance services) which provide services across the IAG Group. All such intragroup transactions are charged to the relevant entities on normal commercial terms and conditions, a direct and actual cost recovery basis or time allocation basis. Certain entities are economically dependent on other entities in the IAG Group. There are also loans between entities in the IAG Group. Only the transactions between the Parent and the wholly owned subsidiaries are disclosed here because all other transactions that have occurred among entities within the Consolidated entity have been eliminated for consolidation purposes.

B. SUBSIDIARIES

I. Transactions during the year

Aggregate amounts included in the determination of profit before income tax for the year that resulted from transactions with related parties within the wholly owned group were as follows.

	2010	PARENT 2009
	\$m	\$m
a. INCOME		
Dividend revenue	327	218
Interest revenue	32	37
II. Balances outstanding at reporting date		
Aggregate amounts receivable from, and payable to, subsidiaries were as follows:		
a. RECEIVABLES		
Amounts receivable	81	51
Loans receivable	912	884
b. PAYABLES		
Amounts payable	62	91

These intragroup balances are considered highly liquid and of negligible credit risk and so the carrying amount is a reasonable approximation of the fair value of the balances except for the fixed rate loans for which the fair value currently exceeds the carrying value. The intragroup balances either bear a fixed or variable interest rate or bear no interest but are repayable on demand.

There are no amounts past due though some amounts outstanding represent part of the Parent's cash flow management operations which do not have fixed payment terms. The Parent has no exposure to currency risk within its receivables and payables (2009—\$74 million exposure in relation to one loan denominated in British pounds).

III. Other notes

a. DIVIDENDS AND TAX ARRANGEMENTS

While the Parent does not transact directly with all subsidiaries, the Parent does however generally receive dividends from all subsidiaries even if indirectly through other subsidiaries. Details of the tax sharing and tax funding agreements are disclosed in note 1.M.II.

b. IAG & NRMA SUPERANNUATION PLAN

Two subsidiaries in the Consolidated entity, Insurance Manufacturers of Australia Pty Limited and Insurance Australia Group Services Pty Limited, have employees that are defined benefit members of the IAG & NRMA Superannuation Plan (refer to the superannuation note). While separate records are maintained for the liabilities relating to each member, there is effectively a sharing of the risks associated with the assets of the plan.

c. TRANSACTIONS WITH IAG ASSET MANAGEMENT WHOLESALE TRUSTS

IAG Asset Management Wholesale Trusts (some of which are disclosed as non-wholly owned subsidiaries in the subsidiaries note), were established to enable higher investment yields for smaller investment portfolios. All subsidiaries within the IAG Group can invest in the trusts in accordance with their investment mandates. All investments in these trusts are on normal commercial terms and conditions.

The IAG & NRMA Superannuation Plan, the net financial position of which is recognised on the balance sheet, has a significant holding in some of the IAG Asset Management Wholesale Trusts. All transactions between the plan and the trusts are on normal commercial terms and conditions.

d. OTHER

Both the amount of the transactions and the outstanding balances at reporting date relating to transactions between the Parent and other subsidiaries are not significant and no further information is disclosed.

C. KEY MANAGEMENT PERSONNEL

I. Details of compensation

Key management personnel 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 key management personnel 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 of the key management personnel is set out below.

	CONSOLIDATED	
	2010	2009
	\$000	\$000
Short term employee benefits	12,194	14,837
Post employment benefits	388	1,316
Other long term benefits	44	148
Termination benefits	–	3,501
Share based payments	7,518	6,591
	20,144	26,393

The key management personnel receive no compensation specifically in relation to the management of the Company. The compensation disclosed in the table above represents the key management personnel's estimated compensation received from the IAG Group in relation to their involvement in the activities with the Consolidated entity.

II. Interest in securities

The tables below disclose the movements in total number of deferred award rights (DAR), executive performance rights (EPR) and performance award rights (PAR) on issue held by each of the key management personnel. The DAR, EPR and PAR were granted as share based remuneration in accordance with the share based payment remuneration policy. The non-executive directors, who are key management personnel, did not receive share based payments in the form of DAR, EPR and PAR.

	DAR ON ISSUE 1 JULY	DAR GRANTED DURING THE YEAR	DAR EXERCISED DURING THE YEAR	DAR LAPSED DURING THE YEAR	DAR ON ISSUE 30 JUNE*	DAR VESTED AND EXERCISABLE 30 JUNE
	Number	Number	Number	Number	Number	Number
a. MOVEMENTS IN TOTAL NUMBER OF DEFERRED AWARD RIGHTS ON ISSUE						
2010						
MJ Wilkins	57,000	158,200	(28,500)	–	186,700	–
JP Breheny	99,300	58,800	–	–	158,100	69,670
A Cornish	48,908	28,500	(24,454)	–	52,954	–
IR Foy	33,675	20,900	(21,835)	–	32,740	–
NB Hawkins	86,500	53,300	(63,270)	–	76,530	–
JS Johnson	104,200	58,800	(37,330)	–	125,670	35,250
LC Murphy	29,800	46,600	(14,900)	–	61,500	–
N Utley	137,125	76,100	(87,125)	–	126,100	–
DG West	27,300	65,900	–	–	93,200	13,650
Total	623,808	567,100	(277,414)	–	913,494	118,570
2009						
MJ Wilkins	–	57,000	–	–	57,000	–
JP Breheny	83,150	40,100	(23,950)	–	99,300	–
A Cornish	–	48,908	–	–	48,908	–
IR Foy	22,325	18,200	(6,850)	–	33,675	–
NB Hawkins	83,150	27,300	(23,950)	–	86,500	–
JS Johnson	92,350	40,400	(28,550)	–	104,200	–
LC Murphy	–	29,800	–	–	29,800	–
N Utley	70,875	85,000	(18,750)	–	137,125	–
DG West	–	27,300	–	–	27,300	–
Total	351,850	374,008	(102,050)	–	623,808	–
Executives who ceased as key management personnel						
AM Coleman	90,950	–	(27,850)	–	63,100	–
CF McLoughlin	73,375	–	(20,750)	–	52,625	–
J van der Schalk	63,850	–	–	–	63,850	–
G Venardos	104,275	–	(30,950)	–	73,325	–
Total	332,450	–	(79,550)	–	252,900	–

* On 1 July 2010, some DAR on issue were vested due to the employment condition met by all these KMP. Some KMP exercised the newly vested DAR and received one share for each DAR exercised. However, these IAG shares received are restricted in accordance with IAG's Security Trading Policy.

	EPR ON ISSUE 1 JULY Number	EPR GRANTED DURING THE YEAR Number	EPR EXERCISED DURING THE YEAR Number	EPR LAPSED DURING THE YEAR Number	EPR ON ISSUE 30 JUNE Number	EPR VESTED AND EXERCISABLE 30 JUNE Number
b. MOVEMENTS IN TOTAL NUMBER OF EXECUTIVE PERFORMANCE RIGHTS ON ISSUE						
2010						
MJ Wilkins	1,000,000	790,600	–	–	1,790,600	–
JP Breheny	396,000	293,900	–	–	689,900	–
A Cornish	250,000	311,700	–	–	561,700	–
IR Foy	212,500	186,300	–	–	398,800	–
NB Hawkins	402,500	302,800	–	–	705,300	–
JS Johnson	397,000	293,900	–	–	690,900	–
LC Murphy	287,500	249,300	–	–	536,800	–
N Utley	562,000	380,200	–	–	942,200	–
DG West	433,500	329,500	–	–	763,000	–
Total	3,941,000	3,138,200	–	–	7,079,200	–
2009						
MJ Wilkins	250,000	750,000	–	–	1,000,000	–
JP Breheny	98,500	297,500	–	–	396,000	–
A Cornish	–	250,000	–	–	250,000	–
IR Foy	11,500	201,000	–	–	212,500	–
NB Hawkins	96,000	306,500	–	–	402,500	–
JS Johnson	99,500	297,500	–	–	397,000	–
LC Murphy	35,000	252,500	–	–	287,500	–
N Utley	143,500	418,500	–	–	562,000	–
DG West	100,000	333,500	–	–	433,500	–
Total	834,000	3,107,000	–	–	3,941,000	–
Executives who ceased as key management personnel						
AM Coleman	103,000	–	–	–	103,000	–
CF McLoughlin	96,000	–	–	–	96,000	–
J van der Schalk	95,000	–	–	–	95,000	–
G Venardos	113,500	–	–	–	113,500	–
Total	407,500	–	–	–	407,500	–

	PAR ON ISSUE 1 JULY Number	PAR GRANTED DURING THE YEAR Number	PAR EXERCISED DURING THE YEAR Number	PAR LAPSED DURING THE YEAR Number	PAR ON ISSUE 30 JUNE Number	PAR VESTED AND EXERCISABLE 30 JUNE Number
c. MOVEMENTS IN TOTAL NUMBER OF PERFORMANCE AWARD RIGHTS ON ISSUE						
2010						
JP Breheny	93,000	-	-	-	93,000	-
IR Foy	36,930	-	-	(16,000)	20,930	-
NB Hawkins	107,930	-	-	(40,000)	67,930	-
JS Johnson	87,350	-	-	(30,000)	57,350	-
N Utley	44,500	-	-	-	44,500	-
Total	369,710	-	-	(86,000)	283,710	-
2009						
JP Breheny	147,000	-	(54,000)	-	93,000	-
IR Foy	88,000	-	(11,070)	(40,000)	36,930	-
NB Hawkins	184,525	-	(24,570)	(52,025)	107,930	-
JS Johnson	123,635	-	(12,150)	(24,135)	87,350	-
N Utley	44,500	-	-	-	44,500	-
Total	587,660	-	(101,790)	(116,160)	369,710	-
Executives who ceased as key management personnel						
AM Coleman	298,451	-	-	(80,451)	218,000	-
CF McLoughlin	122,500	-	-	-	122,500	-
J van der Schalk	178,125	-	-	(37,372)	140,753	-
G Venardos	342,359	-	-	(93,859)	248,500	-
Total	941,435	-	-	(211,682)	729,753	-

d. MOVEMENTS IN TOTAL NUMBER OF ORDINARY SHARES HELD

The relevant interest of each key management personnel and their related parties in ordinary shares of IAG are disclosed in the tables below.

	SHARES HELD AT 1 JULY	SHARES GRANTED AS REMUN- ERATION DURING THE YEAR	SHARES RECEIVED ON EXERCISE OF PAR	SHARES RECEIVED ON EXERCISE OF DAR	NET MOVEMENT OF SHARES DUE TO OTHER CHANGES ^(a)	TOTAL SHARES HELD AT 30 JUNE ^(d)	SHARES HELD NOMINALLY AT 30 JUNE ^(b)
	Number	Number	Number	Number	Number	Number	Number
2010							
JA Strong	409,250	–	–	–	305	409,555	395,009
YA Allen	29,011	–	–	–	–	29,011	27,345
PM Colebatch	46,692	–	–	–	–	46,692	46,692
HA Fletcher	70,803	–	–	–	887	71,690	36,500
A Hynes	27,242	–	–	–	13,000	40,242	40,242
BM Schwartz	41,311	–	–	–	30,684	71,995	70,042
PJ Twyman	46,446	–	–	–	11,334	57,780	57,780
MJ Wilkins	101,666	–	–	28,500	–	130,166	101,666
JP Breheny	78,200	–	–	–	–	78,200	44,250
A Cornish	–	–	–	24,454	–	24,454	–
IR Foy	18,353	–	–	21,835	55	40,243	55
NB Hawkins	87,145	–	–	63,270	21,271	171,686	21,271
JS Johnson	52,898	–	–	37,330	–	90,228	2,750
LC Murphy	–	–	–	14,900	–	14,900	–
N Utley ^(c)	120,602	–	–	1,339,799	(51,852)	1,408,549	50,000
DG West	–	–	–	–	–	–	–

(a) Net movement of shares relates to acquisition and disposal transactions by the KMP and their related parties during the year. It includes opening balances of shares, if any, held by KMP who commenced during the year.

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

(c) Of the 1,339,799 DAR exercised by N Utley, 1,252,674 DAR were issued as part of the consideration for his sale of Equity Insurance Group's shares and are not included as part of his share based remuneration.

(d) On 1 July 2010, some DAR on issue vested and became exercisable by the KMP. Some KMP exercised those newly vested DAR post 30 June 2010.

There were no shares received on exercise of PAR by the key management personnel as no PAR vested during the year.

	SHARES HELD AT 1 JULY	SHARES GRANTED AS REMUN- ERATION DURING THE YEAR	SHARES RECEIVED ON EXERCISE OF PAR	SHARES RECEIVED ON EXERCISE OF DAR	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	Number
2009							
JA Strong	345,570	58,682	–	–	4,998	409,250	395,009
YA Allen	19,521	7,824	–	–	1,666	29,011	27,345
PM Colebatch	27,132	19,560	–	–	–	46,692	46,692
HA Fletcher	51,126	15,648	–	–	4,029	70,803	69,137
A Hynes	17,752	7,824	–	–	1,666	27,242	27,242
BM Schwartz	27,909	11,736	–	–	1,666	41,311	39,399
PJ Twyman	15,000	9,780	–	–	21,666	46,446	44,780
MJ Wilkins	100,000	–	–	–	1,666	101,666	101,666
JP Breheny	250	–	54,000	23,950	–	78,200	250
A Cornish	–	–	–	–	–	–	–
IR Foy	433	–	11,070	6,850	–	18,353	–
NB Hawkins	38,625	–	24,570	23,950	–	87,145	–
JS Johnson	12,198	–	12,150	28,550	–	52,898	4,093
LC Murphy	–	–	–	–	–	–	–
N Utley	101,852	–	–	18,750	–	120,602	101,852
DG West	–	–	–	–	–	–	–
Directors and executives who ceased as key management personnel							
RA Ross	194,189	–	–	–	(4,197)	*	*
ND Hamilton	153,103	–	–	–	(7,554)	*	*
AM Coleman	22,859	–	–	27,850	–	*	*
CF McLoughlin	23,573	–	–	20,750	–	*	*
G Venardos	169,779	–	–	30,950	–	*	*

* These non-executive directors or executives ceased as KMP during the financial year. Information on shares held are disclosed up to the date of their cessation.

(a) Net movement of shares relates to acquisition and disposal transactions by the KMP and their related parties during the year. It includes opening balances of shares, if any, held by KMP who commenced during the year.

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

e. MOVEMENTS IN TOTAL NUMBER OF RESET PREFERENCE SHARES HELD

No key management personnel had any interest in reset preference shares at any time during the financial year (2009—nil).

f. MOVEMENTS IN TOTAL NUMBER OF RESET EXCHANGEABLE SECURITIES HELD

No key management personnel had any interest in reset exchangeable securities of IAG Finance (New Zealand) Limited nominally at the beginning and the end of the financial year (2009—nil).

III. Other related party transactions with key management personnel

Mr N Utley was a shareholder of Equity Insurance Group at the time it was acquired by the IAG Group. As part of the acquisitions, Mr Utley received consideration for the sale of his shares. The consideration was paid in the form of unsecured notes and 1.2 million DAR. The DAR issued as part of the consideration for the sale of shares, are not included as part of his share based remuneration. All the 1.2 million DAR vested and were exercised by Mr Utley during the year ended 30 June 2010. Payment of £1.5 million (2009—payment of £1.5 million) of the outstanding unsecured notes was made during the year ended 30 June 2010 and no unsecured notes remain outstanding as at 30 June 2010 (2009—£1.5 million outstanding unsecured notes).

Mr Utley is a non-executive director and holds 26.85% of Hastings 888 UK Ltd (and its subsidiaries) (Hastings 888) and a shareholder in Lucky 888 Global Ltd holding 31.05% (Lucky 888). Hastings 888 and Lucky 888 acquired Hastings Insurance Services Limited (HISL) and Advantage Insurance Company Limited (Advantage) in the management buy-out during the year ended 30 June 2009. Both businesses trade with IAG UK businesses. Mr Utley has received director fees totalling £59,312 from Hastings 888 and Lucky 888 in the year ended 30 June 2010 (2009—no director fees received).

Under the terms of the agreement for the sale of HISL (SPA), IAG International Pty Limited (IAGI) agreed to indemnify Hastings 888 in respect of any potential tax related claims. Hastings 888 made a number of claims under this indemnity, which were settled by IAGI following execution of a deed of settlement and variation on 28 April 2010 by payment of a full and final settlement amount of £924,200. The SPA has also been varied to provide for the sharing of any recoveries and associated costs between the parties in respect of any matters yet to be indemnified.

D. OTHER RELATED PARTIES

Contributions are made to various superannuation plans, both defined contribution and defined benefit plans. Information regarding transactions with the plans is provided in the superannuation note.

NOTE 35. DERIVATIVES

Derivatives are used across the Company to manage various risks. Derivatives are used solely to manage risk exposures and are not used for trading or speculation.

A. DERIVATIVES FOR WHICH HEDGE ACCOUNTING IS APPLIED

I. Cash flow hedges

Cash flow hedge accounting was applied to a single economic hedge relating to the currency and interest rate risk on the USD subordinated term notes (refer to the interest bearing liabilities note).

II. Net investment hedges

Residual foreign currency exposures arising at Consolidated entity level on translation of net investments in foreign operations are hedged to between 50% and 100% of the value on an after tax basis through the use of forward exchange contracts, cross currency swaps, and the designation of certain foreign currency borrowings as hedging instruments.

Each of the hedging relationships has been broadly effective throughout the current period or since inception with the small amount of ineffectiveness recognised in the statement of comprehensive income.

III. Reporting date positions

The notional contract amounts associated with derivative financial instruments which form arrangements for which hedge accounting is applied together with a maturity profile for the current reporting period and reporting date fair value are provided below.

	Maturity profile			Notional contract amount	Fair value asset	2010 Fair value liability	CONSOLIDATED			
	Within 1 year	1 to 5 years	Over 5 years				2010		2009	
	\$m	\$m	\$m				Notional contract amount	Fair value asset	Fair value liability	Fair value asset
a. CASH FLOW HEDGES										
Cross currency swaps	-	-	-	-	-	-	295	-	(104)	
Interest rate swaps	-	-	-	-	-	-	350	-	(7)	
b. NET INVESTMENT HEDGES										
Forward foreign exchange contracts	618	-	-	618	2	(14)	1,154	19	(4)	
Cross currency swaps	-	-	-	-	-	-	165	29	-	

B. DERIVATIVES FOR WHICH HEDGE ACCOUNTING IS NOT APPLIED (DERIVATIVES HELD FOR ECONOMIC HEDGING PURPOSES ONLY)

While a variety of derivatives are used to hedge specific risks on various financial instruments, the majority of these derivatives are not designated as part of a hedge for which hedge accounting is applied. These derivatives are measured at fair value with movements in fair value being recognised in the statement of comprehensive income.

In addition to the derivatives described above, certain contracts entered into include embedded derivative features. Such embedded derivatives are assessed at inception of the contract and, depending on their characteristics, are accounted for as separate derivative financial instruments.

I. Reporting date positions

The notional contract amounts associated with derivative financial instruments for which hedge accounting is not applied together with a maturity profile for the current reporting period and reporting date fair value is provided below.

	CONSOLIDATED								
	2010						2009		
	Notional contract amount	Fair value asset	Fair value liability	Notional contract amount	Fair value asset	Fair value liability	Notional contract amount	Fair value asset	Fair value liability
	Maturity profile								
	Within 1 year	1 to 5 years	Over 5 years						
	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
a. PRESENTED IN INVESTMENTS (INVESTMENT RELATED DERIVATIVES)									
Futures	399	2	–	401	11	(2)	1,163	5	–
Share price index futures	56	–	–	56	–	–	(6)	–	–
Options	–	4	–	4	4	–	3	2	–
Forward foreign exchange contracts	182	–	–	182	3	(1)	–	–	–
b. PRESENTED IN TRADE AND OTHER RECEIVABLES/PAYABLES (TREASURY RELATED DERIVATIVES)									
Forward foreign exchange contracts	48	–	–	48	–	–	205	–	(3)
Interest rate swaps	–	202	–	202	–	–	770	12	(11)
c. EMBEDDED DERIVATIVES									
RES exchange right*	–	–	–	–	–	–	–	96	–

* The RES exchange right was an asset of the Parent which was extinguished when the RES terms changed in December 2009.

C. FAIR VALUE INFORMATION

The notional contract amounts associated with derivative financial instruments are not recorded as assets or liabilities on the balance sheet as they do not represent the fair value of these transactions.

Further to the discussion of the fair value measurement of derivatives in the summary of significant accounting policies note, the following techniques are used to determine the fair value of various derivative instruments:

I. Interest rate swap contracts

The fair value of the interest rate swap contracts is the estimated amount that the IAG Group would receive or pay to terminate the swap at balance date taking into account current interest rates.

II. Forward foreign exchange contracts

The fair value of the forward foreign exchange contract is calculated by reference to current forward exchange contracts for contracts with similar maturity profile as at reporting date.

III. Determination of fair value

The table below separates the total derivatives balance based on a hierarchy that reflects the significance of the inputs used in the determination of fair value. Details on the levels of the fair value hierarchy are disclosed in the investments note.

Where the determination of fair value for an instrument involves inputs from more than one category, the level within which the instrument is categorised in its entirety is determined on the basis of the lowest level input that is significant to the fair value measurement in its entirety.

	CONSOLIDATED	
	2010	2009
	\$m	\$m
Level 1	14	8
Level 2	1	–
	15	8

NOTE 36. CAPITAL MANAGEMENT

A. CAPITAL MANAGEMENT STRATEGY

The capital management strategy plays a central role in managing risk to create shareholder value whilst meeting the crucial and equally important objective of providing an appropriate level of capital to protect policyholders' and lenders' interests and satisfy regulators. Capital expenditure and business plans also provide support in the face of adverse outcomes from insurance and other activities and investment performance.

The IAG Group actively considers its risk appetite through the holistic implementation of strategies around identified key risk levels of underwriting, reinsurance, capital, asset allocation and risk management. The target level of capitalisation for the IAG Group is assessed by consideration of factors including:

- the probability of ruin over the next one to three years;
- the probability of falling below the Australian Prudential Regulation Authority (APRA) minimum capital requirement (MCR) 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.

The amount of capital required that fulfils these risk appetite factors varies according to the business underwritten, extent of reinsurance and asset allocation and is estimated using dynamic financial analysis modelling. For ease of communication, internally and externally, the IAG Group has translated the outcome into a multiple of MCR by applying the APRA prescribed methodology for Level 2 Insurance Groups, the rules applicable to the IAG Group since August 2009. On this basis, the IAG Group has established a target capital of 1.45 to 1.50 times MCR.

Internal policies are in place to ensure significant deviations from this benchmark will result in the IAG Board considering how any shortfall should be made good or any surplus utilised.

I. Regulatory capital

All insurers within the IAG Group that carry on insurance business in Australia are registered with APRA and are subject to prudential standards that set out the basis for calculating the MCR which is a minimum level of capital that the regulator deems must be held to meet policyholder obligations. An insurer's capital base is expected to be adequate for the size, business mix, complexity and risk profile of its business and so the MCR utilises a risk based approach to capital adequacy. IAG uses the standardised framework for calculating the MCR detailed in the relevant prudential standard and referred to as the prescribed method which is determined to be the sum of the capital charges for insurance, investment, investment concentration and catastrophe concentration risk. It is IAG Group policy to ensure that each of the licensed insurers maintains an adequate capital position from an entity perspective.

It is IAG Group policy to hold regulatory capital levels in excess of the MCR as required by APRA. The current target capital multiple for the IAG Group is 1.45 to 1.50 times (2009—1.45 to 1.50 times) the MCR. The policy also requires management to not take any action that would further reduce the capital multiple if an identified MCR is reached, currently set as 1.30 times MCR for the IAG Group. APRA also imposes some restrictions on the composition of capital eligible to meet the MCR.

Capital calculations for regulatory purposes are based on the premium liabilities model which is different to the deferral and matching model which underpins the measurement of assets and liabilities in the financial statements. The premium liabilities model assesses future claims payments arising from future events insured under existing policies. This differs to the measurement of the outstanding claims liability on the balance sheet which considers claims relating to events that occur only up to and including the reporting date.

II. Economic capital

In conjunction with the considerations set out above, which are important to the functioning of the business, 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 IAG Group whilst suitably protecting policyholders and lenders.

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

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

B. CAPITAL COMPOSITION

The IAG Group's capital comprises ordinary equity and interest bearing liabilities. The balance sheet capital mix at reporting date was as shown in the table below.

		CONSOLIDATED	
	Target	2010	2009
	%	%	%
Ordinary equity less goodwill and intangible assets	60–70	64	71
Interest bearing liabilities hybrid securities and debt	30–40	36	29
Total capitalisation		100	100

The change in the balance sheet capital mix to reporting date has been primarily driven by the \$550 million of reset exchangeable securities (RES) brought on the balance sheet (post the RES amendments), the repayment of the USD subordinated term notes and the issuance of GBP subordinated exchangeable term notes.

C. REGULATORY CAPITAL COMPLIANCE

The Company and the insurers within the Consolidated entity have at all times during the current and prior financial year complied with the externally imposed capital requirements to which they are subject. The MCR calculation for the Consolidated entity provided below is based on applying the APRA Level 2 Insurance Group requirements.

	CONSOLIDATED	
	2010	2009
	\$m	\$m
I. Statutory capital		
a. TIER 1 CAPITAL		
i. Fundamental Tier 1 capital		
Ordinary shares	5,353	5,326
Reserves	(34)	(11)
Non-controlling interests	170	165
Retained earnings	(775)	(589)
Excess technical provisions (net of tax) ^(a)	522	438
ii. Innovative residual Tier 1 capital		
Hybrid equities	475	350
iii. Deductions from Tier 1 capital ^(b)		
Treasury shares held in trust ^(c)	(31)	(7)
Goodwill	(1,782)	(1,880)
Intangible assets	(301)	(398)
Net deferred tax assets	(267)	(343)
Other	(163)	(68)
Total Tier 1 capital	3,167	2,983
b. TIER 2 CAPITAL		
Ineligible Tier 1 capital	425	–
Subordinated term notes	536	590
Other	12	–
Total statutory capital	4,140	3,573
II. Minimum capital requirement		
Insurance risk	1,344	1,279
Investment risk	790	618
Investment concentration risk ^(d)	–	–
Catastrophe concentration risk	20	100
Total minimum capital requirement	2,154	1,997
III. Minimum capital requirement multiple	1.92	1.79

(a) The excess technical provisions represent the difference between the insurance liabilities incorporating a risk margin (refer to section G of the claims note) on the balance sheet based on the deferral and matching model and the insurance liabilities incorporating a risk margin equivalent to a probability of adequacy of 75% used for regulatory reporting purposes based on the premium liabilities model.

(b) Certain assets that are considered acceptable from an accounting perspective are, from a supervisory perspective, considered to be generally not available or of reduced value should an insurer encounter difficulties. Holdings of such assets are therefore required to be deducted from the regulatory capital base.

(c) The portion of the treasury shares held in trust that does not meet eligibility criteria under APRA prudential standards.

(d) The investment concentration risk charge is zero reflecting that the holding of particular assets, including reinsurance recoveries, and exposure to a particular counterparty, are sufficiently diversified for the purposes of the regulatory capital calculations.

IV. Factors impacting the minimum capital requirement multiple

The IAG Group's MCR increased primarily due to the RES being recognised as Innovative Tier 1 capital, partially offset by the net movement in risk charges as below.

a. INSURANCE RISK

The increase in the insurance risk charge is due to strengthening of insurance liabilities primarily in the United Kingdom as well as premium growth.

b. INVESTMENT RISK

The increase in the investment risk charge is due to the growth in the IAG Group's investment portfolio and increase investment in growth assets (refer to the investments note).

c. CATASTROPHE CONCENTRATION RISK

The decrease in catastrophe concentration risk charge reflects the triggering of the IAG Group's second and third event protection and the operation of its aggregate cover which reduces the maximum event retention following the high natural perils in 2010.

As at 30 June 2009, before the RES amendments, the MCR calculation does not include the \$550 million of contingent capital made available through the RES (refer to section AH of the summary of significant accounting policies note), which if exchanged, would have brought the MCR multiple to 2.03.

D. CREDIT RATING

Key wholly owned insurers within the IAG Group had the following ratings published by Standard & Poor's as at the current reporting date.

ENTITY	ISSUER CREDIT RATING	FINANCIAL STRENGTH RATING
Parent		
Insurance Australia Group Limited	A+ / Stable	n/a
Licensed insurers		
Insurance Australia Limited	AA- / Stable	AA- / Stable
IAG New Zealand Limited	AA- / Stable	AA- / Stable
CGU Insurance Limited	AA- / Stable	AA- / Stable
Swann Insurance (Aust) Pty Ltd	AA- / Stable	AA- / Stable
IAG Re Labuan (L) Berhad	n/a	A+ / Stable
IAG Re Australia Limited	AA- / Stable	AA- / Stable

NOTE 37. NET TANGIBLE ASSETS

	CONSOLIDATED	
	2010	2009
	\$	\$
Net tangible assets per ordinary share	1.16	1.16

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

NOTE 38. EVENTS SUBSEQUENT TO REPORTING DATE

As the following transactions occurred after reporting date and did not relate to conditions existing at reporting date, no account has been taken of them in the financial statements for the current reporting period ended 30 June 2010.

A. FINAL DIVIDEND

On 26 August 2010, the IAG Board determined to pay a final dividend of 4.5 cents per share, 100% franked. The dividend will be paid on 6 October 2010. The Dividend Reinvestment Plan will operate by acquiring shares on market to participants with no discount applied.

B. OTHER

I. Acquisition of underwriting agency in Australia

On 1 July 2010, the IAG Group entered into an arrangement to acquire 50% of the ownership of Accident & Health International Underwriting Pty Limited (AHI). AHI is an underwriting agency in Australia that has been in operation since 1998 and currently underwrites personal accident and sickness insurance and travel insurance.

II. Executive team changes

On 27 July 2010, IAG announced the following changes to the executive team:

- IR Foy has been appointed to the role of Chief Executive Officer, UK, effective 1 September 2010;
- JS Johnson has been appointed to the role of Chief Executive Officer, New Zealand, effective 1 November 2010;
- LC Murphy has been appointed to the role of Chief Executive Officer, The Buzz, effective 1 November 2010 in addition to her current role as Group Executive, Corporate Office;
- K Armstrong has been appointed as acting Chief Executive Officer, New Zealand for the period from 1 September 2010 to 1 November 2010 until JS Johnson moves into this role; and
- N Utley will cease as Chief Executive Officer, UK, effective 31 August 2010.