



Tower Limited

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**2017**  
**half year**  
report



# Tower Limited **report**

For the **half year** ended  
31 March 2017

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# Tower Management **Review**

## Half year to 31 March 2017

### Features of half year 2017

- Reported half year loss after tax of \$8.2 million impacted by adjustments to Canterbury provisions, Kaikoura earthquake and large loss events
- Underlying profit after tax<sup>1</sup> of \$8.1 million, an increase of 7.6%, from \$7.6 million in H1 16
- Transformation of core business continues with business initiatives delivering growth, improved underwriting profit and lower claims and management expenses
- Further progress on Canterbury with just under one third of open property claims settled in the half; Tower's Appointed Actuary, Deloitte, has advised the Board to increase provision requirements, reducing post-tax profits by \$9.8 million for the half
- During May 2017, Tower Limited drew down \$30 million of a \$50 million liquidity facility with BNZ and used this to strengthen Tower Insurance Limited's solvency position
- Dividend payment suspension to continue

### Half year summary

Tower reported a loss after tax of \$8.2 million for the half year ended 31 March 2017 (H1 17), compared to a loss of \$8.7 million for the half year ended 31 March 2016 (H1 16). The result was impacted by further adjustments to Canterbury provisions, Kaikoura earthquake and a number of large loss events.

Despite this backdrop, Tower delivered an underlying profit after tax of \$8.1 million for H1 17, an increase of 7.6% compared to H1 16.

Tower has strong underlying New Zealand and Pacific businesses. It continues to be guided by the strategic imperatives already well established in the business.

During the half, Tower continued to improve the underlying business through implementing digital initiatives, delivering better claims performance, achieving policy growth in the core New Zealand book, and reducing management expenses.

Tower continues to make solid progress settling claims in Canterbury, however, issues with the Earthquake Commission (EQC) continue to confront the entire industry.

In September 2016, Tower had 564 property claims remaining. In the intervening six months, almost one third of those claims have been closed. However, new claims from the EQC continue to be received. Tower is part of an industry-wide taskforce that is improving the transparency of the number and type of outstanding claims remaining with EQC.

Against this difficult industry backdrop and challenges with Canterbury provisions in the past, Deloitte has advised Tower to increase provisions, reducing post-tax profits by \$9.8 million for the half. Increases have been partially offset by additional recoveries to be gained from the EQC.

1. Underlying profit after tax excludes the impact of Canterbury earthquakes, Kaikoura earthquake, impairment of intangibles, acquisition and separation costs and profit on businesses in run-off



## Financial performance

Tower's underlying profit increased 7.6%, to \$8.1 million after tax. This compares to \$7.6 million in H1 16.

This increase was driven primarily by continued focus on Tower's three strategic imperatives and improvements made to the underlying business. Positive results in key focus areas demonstrates a trend of core business improvement.

New Zealand and Pacific Gross Written Premium (GWP) remained stable and in line with prior periods. Underlying profit in the Pacific doubled to \$4.4 million compared to the same period last year due to a benign weather environment.

It is clear that the legacy of the Canterbury Earthquakes continues to overshadow the momentum building in the underlying business.

Tower's reported loss of \$8.2 million after tax, compares to a \$8.7 million loss in H1 16. This reflects a \$9.8 million after tax impact from movement in Canterbury provisions. There were also after-tax impacts of \$7.2 million for the Kaikoura earthquakes and \$3.6 million for the Port Hill fires and 'Tasman Tempest' storm.

### GROUP PROFIT SUMMARY

| \$ MILLION                                     | H1 17 | H1 16  | MOVEMENT % |
|------------------------------------------------|-------|--------|------------|
| Gross Written Premium                          | 145.8 | 146.2  | (0.2%)     |
| New Zealand underlying profit                  | 4.7   | 6.0    | (21.7%)    |
| Pacific underlying profit                      | 4.4   | 2.1    | 112%       |
| Corporate underlying profit                    | (1.0) | (0.5)  | (47.1%)    |
| Total underlying profit after tax <sup>2</sup> | 8.1   | 7.6    | 7.6%       |
| Canterbury impact                              | (9.8) | (2.1)  | 369%       |
| Impairment of intangibles                      | -     | (14.1) | n/a        |
| Impact of Kaikoura earthquake                  | (7.2) | -      | n/a        |
| Acquisition & separation costs                 | (1.0) | -      | n/a        |
| Business in runoff                             | 1.7   | -      | n/a        |
| Reported loss after tax                        | (8.2) | (8.7)  | n/a        |

Source: Tower Limited half year results announcement presentation to 31 March 2017 released on 24 May 2017

2. Underlying profit after tax excludes the impact of Canterbury earthquakes, Kaikoura earthquake, impairment of intangibles, acquisition and separation costs and profit on businesses in run-off

In the underlying business, Tower's claims costs reduced significantly by over \$3 million, to \$59.7 million,<sup>3</sup> compared to H1 16. This is due to the success of initiatives launched in the past 12 months. A sharp focus on non-personnel costs saw the trend on management and sales expenses continue to decline. Expenses<sup>4</sup> fell \$2.6 million to \$48.2 million compared to the same period last year. These savings were achieved through continued focus on efficiency and productivity, and reduced reliance on contractors and third parties.

Investment revenue fell from \$4.4 million in H1 16 to \$3.2 million in H1 17 as a result of lower interest rates and lower cash balances following Canterbury claims payments.

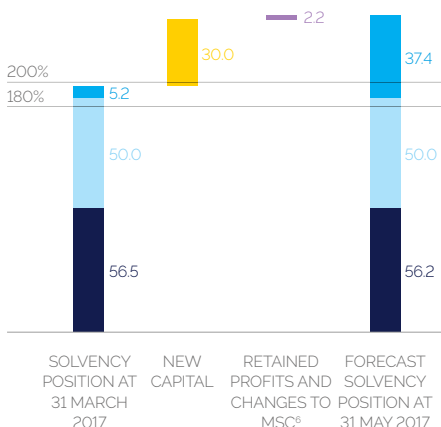
## Solvency position

During May 2017, Tower Limited drew down \$30 million of a \$50 million liquidity facility with BNZ and used this to strengthen Tower Insurance Limited's solvency position.

As at 31 May 2017, Tower Insurance Limited expects to hold \$37.4 million over and above the minimum solvency capital (MSC) and licence conditions required by the Reserve Bank of New Zealand (RBNZ).<sup>5</sup> This equates to a solvency ratio of 255% and includes operating profits for April and May 2017, offset by the impact of Cyclone Debbie.

**SOLVENCY POSITION**  
TOWER INSURANCE LIMITED  
\$ MILLIONS

● SURPLUS MARGIN  
● RBNZ MARGIN  
● MSC



3. Excludes claim handling expenses, Port Hills fires, Tasman Tempest, Kaikoura earthquake and change to Canterbury provisions

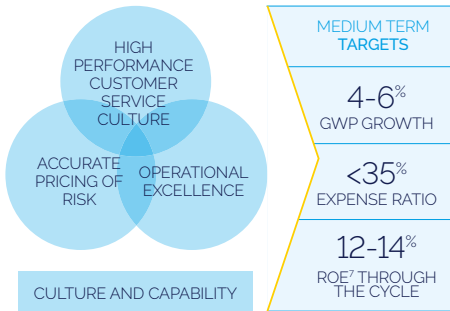
4. Management expenses excludes depreciation

5. \$37.4 million was the forecast as at the date of Tower Limited's half year results announcement presentation to 31 March 2017, released on 24 May 2017

6. Includes operating profits for April/May 2017, offset by impact of Cyclone Debbie

## A strong underlying business

Tower has strong underlying New Zealand and Pacific businesses. It continues to be guided by the strategic imperatives already well established in the business.



7. ROE is Return on Equity

Tower has seen solid improvements in crucial areas that will help it achieve its long-term targets:

- Focus on customers has delivered positive policy growth in Tower's core book and continues to trend upwards
- Management expenses continue the downward trend, decreasing significantly compared to the same period last year
- Tight management of claims processes and supplier networks continue delivering savings early in the financial year

## Focus on customers delivers growth

### ACHIEVEMENTS

- Roll out of digital programme, including quote to buy functionality, supporting core policy growth
- Launch of Airpoints partnership has proved attractive for both new and renewing customers
- Tower Direct retention has improved 1.3 percentage points compared to H1 16

Tower has continued to grow its core New Zealand portfolio adding 4,949 policies to the core book in H1 17.

Policy growth is being achieved through a combination of:

- building and refining Tower's digital offering
- working harder to attract new customers through the door, particularly in attractive segments which we will actively target
- retention improvements

The recent launch of Tower's new product suite online has enabled customers to research, quote and buy insurance from Tower through their mobile, tablet or computer, delivering a significant uplift in new business sales.

Tower's new online offering has been augmented with other innovative initiatives that are driving customer growth, including the launch of Tower's Airpoints partnership and increased marketing of the improved Trade Me Insurance platform.

Since announcing the Airpoints partnership, over 17,000 customers have registered their details with Tower.



A continued focus on encouraging existing customers to stay with Tower through targeted retention initiatives and offerings has delivered an increase in retention rates for Tower Direct of 1.3 percentage points to 82.1% in H1 17, up from 80.8% in H1 16.

## Underwriting excellence

### ACHIEVEMENTS

- Customers have more choice through a tiered product selection
- Easier for customers to purchase – less time on the phone makes them happier and increases our productivity
- Attracting the right customers is delivering positive movements in claims frequency

Increased attention on underwriting and attracting the right customers with better offerings has continued increasing underwriting profit. Tower increased pre-tax underwriting profit, excluding storms, by \$4.1 million from H1 16 to \$14.6 million. This positive result was impacted by the \$10 million pre-tax impact from the Kaikoura earthquake and \$5 million pre-tax impact from the Tasman Tempest storms and Port Hills Fires.

The increase in underwriting profit has been achieved through the re-pricing of portfolios and active targeting of profitable market segments.

Tower's new products have helped attract the right customers, with Tower experiencing a 39% reduction in claims frequency in its new comprehensive motor book when compared to its old policies, since launching in October 2016.

## Claims update

### ACHIEVEMENTS

- Claims expenses decreasing despite industry-wide claims cost inflation
- Closer management of claims supply chain has delivered material savings
- Continued focus on leakage and recoveries

Tower has delivered a significant improvement in claims expenses, reducing them to \$59.7 million in H1 17. This result was delivered despite New Zealand experiencing a number of large loss events during this period.

Initiatives introduced over the past 12 months have reduced Tower's claims expenses by over \$3 million compared to H1 16, as a result of:

- tighter management of Tower's end-to-end claims supply chain
- simpler policy wordings enabling customers and claims teams to easily understand exactly what customers are entitled to
- continued focus on claims leakage and recoveries

## Focus on management expenses

### ACHIEVEMENTS

- Increased focus on efficiency and driving greater productivity
- Lower technology expenditure for business and software support activity
- Reduced reliance on contractors and third party providers

Tower has strengthened its focus on non-personnel related costs, reducing management expenses<sup>8</sup> to \$48.2 million in H1 17, down from \$50.8 million in H1 16.

8. Management expenses excludes depreciation



Increased focus on cost reduction continues the positive momentum built in the past three halves and has enabled Tower to continue investing in long-term business improvement initiatives.

Tower's savings of approximately \$2.6 million in its core underlying expenses compared to H1 16 has been driven by:

- Implementing new performance, development and achievement frameworks that drive performance, resulting in greater efficiency and productivity
- Identifying and reducing expenditure for business and technology support services - building capability internally
- Reducing reliance on third party providers and contractors, again building capability to deliver sustainable savings

Tower expects expenses to continue decreasing as strategic initiatives continue to be embedded. A step change in productivity gains will be dependent on long-term IT investment.

## Leveraging digital capability

With Tower's new product suite available online, access is opened to a whole new range of customers through:

- increased online presence and capability
- Trade Me Insurance and Airpoints partnerships giving access to digitally savvy customers
- tailored, targeted insurance offers for customers using digital channels

Including Tower's partnerships with digital brands, online sales are up from 9% of total transactions in March 2016, to 24% of total transactions in March 2017.

## Canterbury update

The receipt of EQC over-cap claims has continued well beyond industry expectations, offsetting the positive closure of claims.

Tower is part of an industry-wide taskforce which has been working to identify the full extent of outstanding claims remaining within the EQC.

The industry taskforce is currently reviewing approximately 8,000 EQC claims. The information uncovered is assisting Tower to identify, quantify and expedite the settlement of the last remaining claims.

In September 2016, Tower had 564 property claims remaining. In the intervening 6 months, around one third of those claims have been closed. However, new claims from the EQC continue to be received.

Despite this difficult environment, Tower is closing claims at a faster rate and settlement outcomes are in line with expectations.

Tower's independent, statutory Appointed Actuary, Rick Shaw from Deloitte, considers all liabilities and receivables relating to the Canterbury Earthquakes. The Tower Board continues to rely on this advice to enable it to establish appropriate provisions.

Against this difficult industry backdrop and challenges with provisions in the past, Deloitte has advised Tower to increase provisions. The three main drivers for this are:

- the potential for additional over-cap claims from the EQC that have been identified through the industry taskforce process;
- potential for increased litigation and higher litigation costs;
- increase in risk margins

These increases have been partially offset by additional recoveries to be gained from the EQC. As overall claims costs continue to grow, this naturally flows through to these recoveries. Deloitte has advised increasing this receivable, partly offsetting the higher risk margins.

The net result of the Appointed Actuary's recommendations is that Tower's claims incurred but not reported (IBNR) and risk margin allowance have increased from 60% to 89% of underlying case estimates.

| \$ MILLION                    | Mar 17       | Sep 16       |
|-------------------------------|--------------|--------------|
| Case estimates                | 73.9         | 93.2         |
| IBNR/IBNER <sup>9</sup>       | 47.4         | 44.0         |
| Risk margin                   | 18.2         | 11.9         |
| <b>Outstanding claims</b>     | <b>139.5</b> | <b>149.1</b> |
| Adverse development cover     | 43.8         | 43.8         |
| Other reinsurance recoveries  | 2.2          | 7.1          |
| EQC receivables               | 66.6         | 57.6         |
| <b>Total receivables</b>      | <b>112.5</b> | <b>108.4</b> |
| <b>Net outstanding claims</b> | <b>27.0</b>  | <b>40.7</b>  |

9. IBNR/IBNER includes claims handling expenses

While Tower is making significant progress closing claims, as previously advised, many of the remaining claims are more complex and contentious, with dispute resolution increasingly achieved through litigation.

## Outlook

The challenges that face the general insurance industry remain — high claims necessitating pricing reviews, a low interest rate environment, increasing digital competition and the existing EQC framework.

Tower's strategy to transform into a high performing general insurer will help deliver positive results in light of this tough market background.

Tower's Board has made the decision to delay the IT simplification programme pending the outcome of the Fairfax scheme vote and the non-binding proposal.

While a replacement IT solution is further away than planned, Tower continues to pursue all other aspects of its strategy to:

- drive GWP growth through increased focus on customers
- reduce operating expenses and claims costs
- deliver shareholder value

Tower remains focussed on the implementation of its strategic imperatives to continue driving the transformation of the business. ►

# ► Tower Limited **Interim Financial Statements** and Independent Review Report

For the **half year** ended  
31 March 2017

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Consolidated **Income** StatementFor the **half year** ended 31 March 2017

FOR THE HALF YEAR ENDED

|                                                     | NOTE | 31 MARCH<br>2017<br>UNAUDITED<br>\$'000 | 31 MARCH<br>2016<br>UNAUDITED<br>\$'000 |
|-----------------------------------------------------|------|-----------------------------------------|-----------------------------------------|
| <b>Revenue</b>                                      |      |                                         |                                         |
| Premium revenue                                     | 4    | 150,540                                 | 151,452                                 |
| Less: Outwards reinsurance expense                  |      | (23,763)                                | (24,500)                                |
| <b>Net premium revenue</b>                          |      | <b>126,777</b>                          | <b>126,952</b>                          |
| Investment revenue                                  | 5    | 3,553                                   | 4,748                                   |
| Fee and other revenue                               |      | 1,441                                   | 1,288                                   |
| <b>Net operating revenue</b>                        |      | <b>131,771</b>                          | <b>132,988</b>                          |
| <b>Expenses</b>                                     |      |                                         |                                         |
| Claims expense                                      |      | 133,558                                 | 116,220                                 |
| Less: Reinsurance recoveries revenue                |      | (36,092)                                | (36,549)                                |
| <b>Net claims expense</b>                           | 6, 7 | <b>97,466</b>                           | <b>79,671</b>                           |
| Management and sales expenses                       |      | 44,098                                  | 44,611                                  |
| Impairment expense                                  | 11   | -                                       | 19,649                                  |
| Acquisition proposal expenses                       | 2    | 721                                     | -                                       |
| Financing expenses                                  |      | 164                                     | -                                       |
| <b>Total expenses</b>                               |      | <b>142,449</b>                          | <b>143,931</b>                          |
| <b>(Loss) attributed to shareholders before tax</b> |      | <b>(10,678)</b>                         | <b>(10,943)</b>                         |
| Tax benefit attributed to shareholders' profits     |      | 2,496                                   | 2,264                                   |
| <b>(Loss) for the half year</b>                     |      | <b>(8,182)</b>                          | <b>(8,679)</b>                          |
| <b>(Loss) attributed to:</b>                        |      |                                         |                                         |
| Shareholders                                        |      | (8,447)                                 | (9,187)                                 |
| Non-controlling interest                            |      | 265                                     | 508                                     |
|                                                     |      | <b>(8,182)</b>                          | <b>(8,679)</b>                          |
| Basic and diluted (loss) per share (cents)          |      | (5.01)                                  | (5.42)                                  |

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

# Consolidated Statement of Comprehensive Income

For the **half year** ended 31 March 2017

|                                                     | FOR THE HALF YEAR ENDED                |                                        |
|-----------------------------------------------------|----------------------------------------|----------------------------------------|
|                                                     | 31 MARCH<br>2017<br>UNAUDITED<br>\$000 | 31 MARCH<br>2016<br>UNAUDITED<br>\$000 |
| <b>Loss for the half year</b>                       | <b>(8,182)</b>                         | <b>(8,679)</b>                         |
| <b>Other comprehensive income</b>                   |                                        |                                        |
| Currency translation differences                    | 769                                    | (3,774)                                |
| <b>Other comprehensive income (loss) net of tax</b> | <b>769</b>                             | <b>(3,774)</b>                         |
| <b>Total comprehensive loss for the half year</b>   | <b>(7,413)</b>                         | <b>(12,453)</b>                        |
| <b>Total comprehensive (loss) attributed to:</b>    |                                        |                                        |
| Shareholders                                        | (7,742)                                | (12,284)                               |
| Non-controlling interest                            | 329                                    | (169)                                  |
|                                                     | <b>(7,413)</b>                         | <b>(12,453)</b>                        |

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

Consolidated **Balance Sheet**

As at 31 March 2017

|                                                |       | AS AT                                   |                                       |
|------------------------------------------------|-------|-----------------------------------------|---------------------------------------|
|                                                | NOTE  | 31 MARCH<br>2017<br>UNAUDITED<br>\$'000 | 31 MARCH<br>2016<br>AUDITED<br>\$'000 |
| <b>Assets</b>                                  |       |                                         |                                       |
| Cash and cash equivalents                      |       | 70,101                                  | 92,228                                |
| Receivables                                    | 9     | 270,591                                 | 254,685                               |
| Investments                                    | 18    | 183,306                                 | 188,522                               |
| Derivative financial assets                    | 18    | 173                                     | 57                                    |
| Deferred acquisition costs                     |       | 19,947                                  | 19,973                                |
| Current tax assets                             |       | 13,785                                  | 13,168                                |
| Property, plant and equipment                  |       | 9,181                                   | 9,511                                 |
| Intangible assets                              | 11    | 33,255                                  | 31,982                                |
| Deferred tax assets                            | 10    | 35,722                                  | 30,155                                |
| <b>Total assets</b>                            |       | <b>636,061</b>                          | <b>640,281</b>                        |
| <b>Liabilities</b>                             |       |                                         |                                       |
| Payables                                       |       | 48,719                                  | 49,500                                |
| Current tax liabilities                        |       | 128                                     | 123                                   |
| Provisions                                     |       | 4,816                                   | 4,177                                 |
| Derivative financial liabilities               | 18    | 35                                      | 735                                   |
| Insurance liabilities                          | 7, 12 | 364,192                                 | 361,009                               |
| Deferred tax liabilities                       | 10    | 1,777                                   | 785                                   |
| <b>Total liabilities</b>                       |       | <b>419,667</b>                          | <b>416,329</b>                        |
| <b>Net assets</b>                              |       | <b>216,394</b>                          | <b>223,952</b>                        |
| <b>Equity</b>                                  |       |                                         |                                       |
| Contributed equity                             |       | 382,172                                 | 382,172                               |
| Accumulated losses                             |       | (51,272)                                | (42,822)                              |
| Reserves                                       |       | (116,067)                               | (116,772)                             |
| <b>Total equity attributed to shareholders</b> |       | <b>214,833</b>                          | <b>222,578</b>                        |
| Non-controlling interest                       |       | 1,561                                   | 1,374                                 |
| <b>Total equity</b>                            |       | <b>216,394</b>                          | <b>223,952</b>                        |

The interim financial statements were approved for issue by the Board on 24 May 2017.



Michael P Stiasny  
Chairman



Graham R Stuart  
Director

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

# Consolidated Statement of Changes in Equity

For the **half year** ended 31 March 2017

ATTRIBUTED TO SHAREHOLDERS  
UNAUDITED

|                                             | CONTRIBUTED<br>EQUITY<br>\$000 | ACCUMULATED<br>LOSS<br>\$000 | RESERVES<br>\$000 | TOTAL<br>\$000  | NON-<br>CONTROLLING<br>INTEREST<br>\$000 | TOTAL<br>EQUITY<br>\$000 |
|---------------------------------------------|--------------------------------|------------------------------|-------------------|-----------------|------------------------------------------|--------------------------|
| <b>Half year ended 31 March 2017</b>        |                                |                              |                   |                 |                                          |                          |
| At the beginning of the half year           | 382,172                        | (42,822)                     | (116,772)         | 222,578         | 1,374                                    | 223,952                  |
| <b>Comprehensive income</b>                 |                                |                              |                   |                 |                                          |                          |
| (Loss) Profit for the half year             | –                              | (8,447)                      | –                 | (8,447)         | 265                                      | (8,182)                  |
| Currency translation differences            | –                              | –                            | 705               | 705             | 64                                       | 769                      |
| <b>Total comprehensive loss</b>             | –                              | (8,447)                      | 705               | (7,742)         | 329                                      | (7,413)                  |
| <b>Transactions with shareholders</b>       |                                |                              |                   |                 |                                          |                          |
| Dividends paid                              | –                              | –                            | –                 | –               | (142)                                    | (142)                    |
| Other                                       | –                              | (3)                          | –                 | (3)             | –                                        | (3)                      |
| <b>Total transactions with shareholders</b> | –                              | (3)                          | –                 | (3)             | (142)                                    | (145)                    |
| <b>At the end of the half year</b>          | <b>382,172</b>                 | <b>(51,272)</b>              | <b>(116,067)</b>  | <b>214,833</b>  | <b>1,561</b>                             | <b>216,394</b>           |
| <b>Half year ended 31 March 2016</b>        |                                |                              |                   |                 |                                          |                          |
| At the beginning of the half year           | 384,585                        | 6,376                        | (111,696)         | 279,265         | 1,644                                    | 280,909                  |
| <b>Comprehensive income</b>                 |                                |                              |                   |                 |                                          |                          |
| (Loss) Profit for the half year             | –                              | (9,187)                      | –                 | (9,187)         | 508                                      | (8,679)                  |
| Currency translation differences            | –                              | –                            | (3,097)           | (3,097)         | (677)                                    | (3,774)                  |
| <b>Total comprehensive loss</b>             | –                              | (9,187)                      | (3,097)           | (12,284)        | (169)                                    | (12,453)                 |
| <b>Transactions with shareholders</b>       |                                |                              |                   |                 |                                          |                          |
| Capital repayment plan                      | (2,413)                        | –                            | –                 | (2,413)         | –                                        | (2,413)                  |
| Dividends paid                              | –                              | (12,688)                     | –                 | (12,688)        | –                                        | (12,688)                 |
| Other                                       | –                              | (3)                          | –                 | (3)             | –                                        | (3)                      |
| <b>Total transactions with shareholders</b> | <b>(2,413)</b>                 | <b>(12,691)</b>              | <b>–</b>          | <b>(15,104)</b> | <b>–</b>                                 | <b>(15,104)</b>          |
| <b>At the end of the half year</b>          | <b>382,172</b>                 | <b>(15,502)</b>              | <b>(114,793)</b>  | <b>251,877</b>  | <b>1,475</b>                             | <b>253,352</b>           |

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

Consolidated Statement of **Cash Flows**For the **half year** ended 31 March 2017

FOR THE HALF YEAR ENDED

|                                                                 | NOTE      | 31 MARCH<br>2017<br>UNAUDITED<br>\$000 | 31 MARCH<br>2016<br>UNAUDITED<br>\$000 |
|-----------------------------------------------------------------|-----------|----------------------------------------|----------------------------------------|
| <b>Cash flows from operating activities</b>                     |           |                                        |                                        |
| Premiums received                                               |           | 153,152                                | 146,072                                |
| Interest received                                               |           | 3,771                                  | 5,469                                  |
| Net realised investment gains (losses)                          |           | (2,247)                                | 852                                    |
| Fee and other income received                                   |           | 1,439                                  | 1,288                                  |
| Reinsurance received                                            |           | 24,819                                 | 45,758                                 |
| Reinsurance paid                                                |           | (24,099)                               | (23,183)                               |
| Claims paid                                                     |           | (135,367)                              | (154,660)                              |
| Payments to suppliers and employees                             |           | (42,114)                               | (39,756)                               |
| Income tax paid                                                 |           | (2,698)                                | (1,624)                                |
| <b>Net cash outflow from operating activities</b>               | <b>17</b> | <b>(23,344)</b>                        | <b>(19,784)</b>                        |
| <b>Cash flows from investing activities</b>                     |           |                                        |                                        |
| Net proceeds from financial assets                              |           | 6,986                                  | 8,231                                  |
| Purchase of property, plant and equipment and intangible assets |           | (5,107)                                | (3,217)                                |
| <b>Net cash inflow from investing activities</b>                |           | <b>1,879</b>                           | <b>5,014</b>                           |
| <b>Cash flows from financing activities</b>                     |           |                                        |                                        |
| Capital repayment                                               |           | -                                      | (2,413)                                |
| Dividends paid                                                  |           | -                                      | (12,691)                               |
| Facility fees                                                   |           | (287)                                  | -                                      |
| Payment of non-controlling interest dividends                   |           | (142)                                  | -                                      |
| <b>Net cash outflow from financing activities</b>               |           | <b>(429)</b>                           | <b>(15,104)</b>                        |
| <b>Net decrease in cash and cash equivalents</b>                |           | <b>(21,894)</b>                        | <b>(29,874)</b>                        |
| Foreign exchange movement in cash                               |           | (233)                                  | (573)                                  |
| Cash and cash equivalents at the beginning of the half year     |           | 92,228                                 | 125,113                                |
| <b>Cash and cash equivalents at the end of the half year</b>    |           | <b>70,101</b>                          | <b>94,666</b>                          |

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



# Notes to the Interim Financial Statements

For the **half year** ended 31 March 2017

## 1. Summary of general accounting policies

### Entities reporting

The interim financial statements presented are those of Tower Limited (the Company) and its subsidiaries. The Company and its subsidiaries together are referred to in this financial report as Tower or the Group.

### Statutory base

Tower Limited is a company incorporated in New Zealand under the Companies Act 1993 and listed on the NZX Main Board and the Australian Securities Exchange. The Company is a FMC reporting entity under Part 7 of the Financial Markets Conduct Act 2013.

### Basis of preparation

The interim financial statements of the Group have been prepared in accordance with New Zealand Generally Accepted Accounting Practice (NZ GAAP), and for the purposes of NZ GAAP, the Group is a for-profit entity. They comply with NZ IAS 34 *Interim Financial Reporting* and IAS 34 *Interim Financial Reporting* and consequently include a lower level of disclosure than is required for annual financial statements.

The interim financial statements of the Group have been prepared in accordance with the requirements of the NZX Main Board Listing Rules.

The interim financial statements should be read in conjunction with the annual financial statements for the year ended 30 September 2016, which have been prepared in accordance with International Financial Reporting Standards and New Zealand Equivalents to International Financial Reporting Standards.

The interim financial statements for the six months ended 31 March 2017 are unaudited.

### Accounting policies

The principal accounting policies adopted in the preparation of the interim financial statements are consistent with those of the audited annual financial statements for the year ended 30 September 2016.

### Cash flows

The consolidated statement of cash flows presents the net changes in cash flow for financial assets. Tower considers that knowledge of gross receipts and payments is not essential to understanding certain activities of Tower based on either: the turnover of these items is quick, the amounts are large, and the maturities are short or the value of the sales are immaterial.

### Impact of amendments to NZ IFRS

The application of new or amended accounting standards as of 1 October 2016 has not had a material impact on the financial statements.

# Notes to the Interim Financial Statements

For the **half year** ended 31 March 2016

## 2. Acquisition proposals

### Fairfax Financial Holdings Limited (Fairfax)

On 9 February 2017, Tower Limited announced it had entered into a Scheme Implementation Arrangement (SIA) with Fairfax. Under this agreement, Fairfax agreed to acquire 100% of the Company's shares at \$1.17 per share for an aggregate purchase price of \$197 million (the Fairfax proposal).

Two of Tower's major shareholders representing more than 18% of issued shares entered into firm voting agreements under which they agreed to vote in favour of the Fairfax proposal. Given the substantial premium to the Company's share price at the time the SIA was announced, the certainty provided by the Fairfax proposal and the support it had received from two major shareholders, the Tower Board determined to unanimously recommend the Fairfax proposal to shareholders in the absence of a superior proposal.

The Fairfax proposal is subject to customary conditions and approvals, including approvals from the Reserve Bank of New Zealand (RBNZ); the New Zealand Overseas Investment Office; the High Court of New Zealand; Pacific Island regulatory authorities and Tower shareholders. Shareholder approval of the scheme at the meeting must be by at least 75% of votes cast, representing more than 50% of the total voting rights of the company. Under the SIA the parties provided for the conditions to be satisfied by 31 August 2017, or such later date as may be agreed. At the date of this report the parties are continuing to work towards satisfaction of the conditions.

### Suncorp Group Limited / Vero Insurance New Zealand Limited (Suncorp)

On 22 February 2017, Tower announced that it had received a non-binding indicative proposal from Suncorp to acquire 100% of the Company's shares at an indicative price of \$1.30 per share (the Suncorp proposal).

On 15 March 2017, Suncorp announced that it had purchased 19.99% of the Company's shares for which it has paid \$1.40 per share.

The Suncorp proposal was stated to be subject to customary conditions and approvals, including clearance from the New Zealand Commerce Commission; and approvals from the Reserve Bank of New Zealand; the New Zealand Overseas Investment Office; the High Court of New Zealand; and Pacific Island regulatory authorities. The Commerce Commission have extended their deadline for decision on the Suncorp clearance application to 30 June 2017. At the date of this report the Company has not agreed any contract with Suncorp and there is no certainty that the Suncorp proposal will proceed.

### Interim Reporting

At 31 March 2017, Tower has provided for all costs incurred to that date in respect of the acquisition proposals. These have been recorded in the Consolidated Income Statement as a separate line item (Acquisition proposal expenses).

If either acquisition proposal is successful, there will be a number of financial impacts on the Group, including further expected costs and payments as described below. The impact of these has not been reflected in the interim financial statements for the six months ended 31 March 2017.

### Adviser fees

The Company is working with various legal, financial and Board advisers to assist with the acquisition proposals. Costs for work completed by these advisers on the acquisition proposals prior to 31 March 2017 have been included in the interim financial statements. Where no invoice has been received, an estimate of likely costs up to 31 March 2017 has been made on the basis of best information available at the time.

Tower has engaged Goldman Sachs New Zealand Limited (Goldman) to act as lead financial adviser in relation to the acquisition proposals. Goldman advisory fees are linked to the outcome of any acquisition proposal. In the event that either acquisition proposal is completed, advisory fees estimated at \$4.5 million before tax will become payable to Goldman.

At 31 March 2017, no provision has been made for Goldman advisory fees because at that date, the obligation to pay fees remained contingent upon the successful implementation of an acquisition proposal.

# Notes to the Interim Financial Statements

For the **half year** ended 31 March 2017

## Taxation

The recoverability of tax losses will be impacted by either acquisition proposal, if completed. Accounting standards require de-recognition of deferred tax assets arising from loss carry forwards, where it is not probable that the entity will have sufficient income to use against the losses. Under New Zealand tax legislation losses are forfeited where there is a change of shareholding of more than 49%. Further information is included in Note 10.

## Break fee

The Company has agreed to pay Fairfax a break fee in certain circumstances described in the SIA. The break fee is \$1.97 million (plus GST if applicable), before tax. The purpose of the break fee is to compensate Fairfax for advisory costs; its management and directors' time; out of pocket expenses; and opportunity costs of pursuing the SIA in place of other initiatives should the SIA not proceed. No provision has been made for break fees at 31 March 2017 as circumstances which give rise to the break fee becoming payable under the SIA have not occurred.

## Reimbursement of costs

Tower has agreed to reimburse Fairfax for reasonably incurred costs, capped at \$0.4 million (plus GST if applicable), if certain conditions described in the SIA occur and the break fee provision does not apply. The purpose of this payment is to compensate Fairfax for advisory costs and expenses. No provision has been made for cost reimbursement at 31 March 2017 as circumstances which give rise to costs becoming payable under the SIA have not occurred.

## 3. Critical accounting judgements and estimates

The Group makes estimates and judgements in respect of certain key assets and liabilities. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Key areas where critical accounting estimates and judgements have been applied are noted below.

### Claims estimation

Valuation of net outstanding claims is an area of significant judgement and estimation. Key elements of judgement included within claims estimations are: the rate of claims closure; the quantum of closed claims reopening; the level of future increases in building and other claims costs; future claim management expenses; assessments of risk margin; apportionment of claims costs between the four main earthquake events; and the quantum of new claims being received from EQC and the average cost of these claims.

Key elements of judgement included within recoveries estimations are: the collectability of reinsurance recoveries (includes consideration of factors such as counterparty and credit risk); recoveries from EQC in respect of land damage and building costs; and the assessments of risk margin. The nature of estimation uncertainties, including from those factors listed above, mean that actual claims experience may deviate from reported results.

Refer to Note 7 for further detail on the Canterbury Earthquakes.

### EQC recoveries

Valuation of additional EQC recoveries in respect of building costs and land damage is an area of significant judgement and estimation. Areas of judgement and subjectivity exist in assessments of: claim file review of earthquake event allocation; the quality of assessment information; litigation risk factors; and portfolio conservatism. Tower has filed a statement of claim against EQC in respect of land damage recoveries.

Refer to Note 7 and Note 9 for further detail on EQC recoveries for Canterbury earthquakes and Note 9 for details on EQC recoveries in relation to the Kaikoura region earthquake.

# Notes to the Interim Financial Statements

For the **half year** ended 31 March 2016

## 3. Critical accounting judgements and estimates (continued)

### Acquisition proposal implications

Accounting implications arising from the potential acquisition proposals include areas of significant judgement and estimation. There is considerable uncertainty surrounding the acquisition proposals from Fairfax and Suncorp. There is uncertainty around completion and timing of either acquisition proposal – specifically satisfaction of conditions precedent including regulatory approvals (RBNZ; Pacific Island insurance supervisors; Commerce Commission; Overseas Investment Office; High Court of New Zealand) and shareholder approval and in the case of the Suncorp proposal, any contractual agreement. The continued recognition of certain balance sheet items (including deferred taxation and capitalised IT development costs discussed below) include judgement around the acquisition proposal outcomes. Accounting implications which may arise from the acquisition proposals include judgements and estimation which are discussed in Note 2.

### Deferred taxation

Recognition of deferred tax assets is an area of significant judgement and estimation. Deferred tax assets are recognised for all unused tax losses to the extent it is probable that future taxable profits will be available against which the losses can be utilised and there is continuity of ownership (of greater than 49%). Significant management judgement and estimation is required to determine the amount of deferred tax assets recognised, based on the likely timing and quantum of future taxable profits. This assessment is completed on the basis of the approved strategic plans of Tower Insurance Limited and subsidiaries within the consolidated tax group. The recoverability of tax losses outlined above is also subject to ongoing assessment in respect of active acquisition proposals. If it becomes probable that either acquisition proposal to purchase 100% of the shares in Tower would result in a shareholder change of more than 49%, remaining deferred tax assets from loss carry forwards will be de-recognised and removed from the balance sheet. For further detail refer to Note 10.

### Capitalised IT development costs

Capitalisation of IT development costs is an area of significant judgement and estimation. The application of NZ IAS 38 "Intangible Assets" includes accounting considerations required for capitalisation of IT projects. When applying NZ IAS 38, areas of judgement include consideration of impairment indicators, economic useful life, previous Board impairment decisions and potential impacts from acquisition proposals.

## 4. Premium revenue

|                               | FOR THE HALF YEAR ENDED                |                                        |
|-------------------------------|----------------------------------------|----------------------------------------|
|                               | 31 MARCH<br>2017<br>UNAUDITED<br>\$000 | 31 MARCH<br>2016<br>UNAUDITED<br>\$000 |
| Gross written premiums        | 145,825                                | 146,165                                |
| Less: Gross unearned premiums | 4,715                                  | 5,287                                  |
| <b>Premium revenue</b>        | <b>150,540</b>                         | <b>151,452</b>                         |

**Notes** to the Interim Financial StatementsFor the **half year** ended 31 March 2017**5. Investment revenue**

| FOR THE HALF YEAR ENDED                |                                        |                                        |
|----------------------------------------|----------------------------------------|----------------------------------------|
|                                        | 31 MARCH<br>2017<br>UNAUDITED<br>\$000 | 31 MARCH<br>2016<br>UNAUDITED<br>\$000 |
| <b>Fixed interest securities</b>       |                                        |                                        |
| Interest income                        | 3,771                                  | 5,470                                  |
| Net realised (loss) gain               | (325)                                  | 620                                    |
| Net unrealised gain (loss)             | 1,213                                  | (1,302)                                |
| <b>Total fixed interest securities</b> | <b>4,659</b>                           | <b>4,788</b>                           |
| <b>Equity securities</b>               |                                        |                                        |
| Net unrealised gain (loss)             | -                                      | (163)                                  |
| <b>Total equity securities</b>         | <b>-</b>                               | <b>(163)</b>                           |
| <b>Other</b>                           |                                        |                                        |
| Net realised (loss) gain               | (1,922)                                | 232                                    |
| Net unrealised gain (loss)             | 816                                    | (109)                                  |
| <b>Total other</b>                     | <b>(1,106)</b>                         | <b>123</b>                             |
| Total interest and dividend income     | 3,771                                  | 5,470                                  |
| Total net realised (loss) gain         | (2,247)                                | 852                                    |
| Total net unrealised gain (loss)       | 2,029                                  | (1,574)                                |
| <b>Total investment revenue</b>        | <b>3,553</b>                           | <b>4,748</b>                           |

**6. Net claims expense**

|                                             |      | FOR THE HALF YEAR ENDED                |                                        |
|---------------------------------------------|------|----------------------------------------|----------------------------------------|
|                                             | NOTE | 31 MARCH<br>2017<br>UNAUDITED<br>\$000 | 31 MARCH<br>2016<br>UNAUDITED<br>\$000 |
| Canterbury earthquake claims (4 key events) | 7    | 13,600                                 | 2,900                                  |
| Kaikoura earthquake claims                  |      | 10,000                                 | –                                      |
| Other claims                                |      | 73,866                                 | 76,771                                 |
| <b>Total net claims expense</b>             |      | <b>97,466</b>                          | <b>79,671</b>                          |

# Notes to the Interim Financial Statements

For the **half year** ended 31 March 2016

## 7. Canterbury earthquakes

Tower has received over 16,081 individual claims from customers as a result of earthquakes impacting the Canterbury region during 2010 and 2011 (30 September 2016: 15,990 claims). Like other industry participants, Tower continues to receive 'over-cap' claims from the Earthquake Commission (EQC). The growth in new claims received has impacted Tower's settlement rates during the year. Of all claims received, Tower has settled over 15,607 claims at 31 March 2017 (30 September 2016: 15,426 claims), representing a 97% settlement rate by number of claims and 91% by value (30 September 2016: 96% by number and 89% by value). To date, Tower has paid out more than \$793 million to customers (30 September 2016: \$749 million) in respect of the four main earthquakes that occurred on 4 September 2010; 22 February 2011; 13 June 2011 and 23 December 2011.

As at 31 March 2017, Tower has estimated gross ultimate incurred claims of \$892.7 million in respect of the four main Canterbury earthquake events (30 September 2016: \$869.6 million).

The financial cost to Tower of the Canterbury earthquakes is reduced through reinsurance and is reflected within net outstanding claims. Tower continues to work closely with its catastrophe reinsurance partners as it works through its Canterbury claims settlement programme. Catastrophe reinsurance partners are required to have a financial strength rating of at least A- issued by a recognised international rating agency. Tower has a commercial dispute with the provider of its adverse development cover, Peak Reinsurance Company Limited (Peak Re), which is discussed further in Note 9.

The table below presents a financial representation of Tower's net outstanding claims provision at 31 March 2017 in relation to the four main earthquake events.

### Canterbury earthquake provisions

|                                        | 31 MARCH<br>2017<br>UNAUDITED<br>\$000 | 30 SEPTEMBER<br>2016<br>AUDITED<br>\$000 |
|----------------------------------------|----------------------------------------|------------------------------------------|
| <b>Insurance liabilities</b>           |                                        |                                          |
| Outstanding claims                     | (139,500)                              | (149,100)                                |
| <b>Receivables</b>                     |                                        |                                          |
| Reinsurance recovery receivables       |                                        |                                          |
| Adverse development cover – Peak Re    | 43,750                                 | 43,750                                   |
| Other reinsurance recovery receivables | 2,150                                  | 7,050                                    |
| Other receivables                      | 66,600                                 | 57,600                                   |
| <b>Total receivables</b>               | <b>112,500</b>                         | <b>108,400</b>                           |
| <b>Net outstanding claims</b>          | <b>(27,000)</b>                        | <b>(40,700)</b>                          |

Outstanding claims comprises case estimates, claims incurred but not reported (IBNR) and risk margins. In the six months to 31 March 2017, case estimates have reduced as claims have been settled and paid. These decreases have been offset however, by increased costs on remaining open claims; new overcap claims being received from EQC; and the Appointed Actuary increasing IBNR and risk margins, particularly in respect of litigated claims and additional EQC recoveries.

# Notes to the Interim Financial Statements

For the **half year** ended 31 March 2017

## 7. Canterbury earthquakes (continued)

The following table presents the cumulative impact of the four main Canterbury earthquake events on the income statement.

|                                                                    | 31 MARCH<br>2017<br>UNAUDITED<br>\$000 | 31 MARCH<br>2016<br>UNAUDITED<br>\$000 |
|--------------------------------------------------------------------|----------------------------------------|----------------------------------------|
| <b>Cumulative expenses associated with Canterbury earthquakes:</b> |                                        |                                        |
| Earthquake claims estimate                                         | (892,660)                              | (822,300)                              |
| Reinsurance recoveries                                             | 744,133                                | 719,583                                |
| <b>Claim expense net of reinsurance recoveries</b>                 | <b>(148,527)</b>                       | <b>(102,717)</b>                       |
| Reinsurance expense                                                | (25,045)                               | (25,045)                               |
| <b>Cumulative impact of Canterbury earthquakes before tax</b>      | <b>(173,572)</b>                       | <b>(127,762)</b>                       |
| Income tax                                                         | 49,288                                 | 36,454                                 |
| <b>Cumulative impact of Canterbury earthquakes after tax</b>       | <b>(124,284)</b>                       | <b>(91,308)</b>                        |
| <b>Recognised in current period (net of tax)</b>                   | <b>(9,792)</b>                         | <b>(2,088)</b>                         |

The Board are actively engaged in monitoring Canterbury earthquake developments. Board process relies on the Appointed Actuary's determination of earthquake ultimate incurred claims estimates and the derivation of estimated outcomes. Tower had 474 open claims at 31 March 2017 (30 September 2016: 564 open claims). Recognising relative complexities which exist within remaining open claims, the Appointed Actuary has reviewed each remaining property file with Tower claims staff. This individual claim methodology included review of the latest specialist assessment reports and scope of works to repair or rebuild properties to determine the propensity for future costs to vary. In addition, further provision was made for claims re-opening; claims moving over the EQC cap of \$100,000; claims in litigation and other claim categories. A risk margin has been allowed for at 75% probability of sufficiency.

The actuarial reviews performed during the half year to 31 March 2017 identified the following as key contributors to the increase in expected earthquake claims costs:

- Greater than anticipated new claims from EQC;
- Growth in the level of litigation and customer disputes;
- Continued development of claim costs as they progress through the claims life cycle; and
- Refinement of actuarial assumptions incorporating claims incurred but not reported.

The key elements of judgement within the claims estimation are as follows:

### Claims

- the level of future increases in building and other claims costs
- the number of new claims being received from EQC and the average cost of these claims
- the uncertainty surrounding litigated cases and potential for increased costs
- the rate of closed claims reopening
- apportionment of claim costs to each of the four main earthquake events
- risk margin
- future claim management expenses, and

### Recoveries

- collectability of reinsurance recoveries
- recoveries from EQC (including litigation risks) in respect of land damage and building costs
- risk margin.

# Notes to the Interim Financial Statements

For the **half year** ended 31 March 2016

## 7. Canterbury earthquakes (continued)

Given the nature of estimation uncertainties (including those listed above) actual claims experience may still deviate, perhaps substantially, from the gross outstanding claims liabilities recorded as at 31 March 2017. Any further changes to estimates will be recorded in the accounting period when they become known.

Tower has exceeded its catastrophe reinsurance and adverse development cover limits in relation to the February 2011 event. The estimated ultimate incurred claims cost of the February 2011 event totals \$506.9 million. Tower has reinsurance for \$375.0 million on this event including catastrophe cover, proportional reinsurance and adverse development cover. During the half year ended 31 March 2017, Tower expensed \$13.6 million in relation to the February 2011 event (31 March 2016: \$2.9 million).

For the three other main earthquake events, the catastrophe reinsurance cover headroom remaining is included in the table below.

|                      |  | CATASTROPHE REINSURANCE<br>COVER REMAINING |                                           |
|----------------------|--|--------------------------------------------|-------------------------------------------|
|                      |  | 31 MARCH<br>2017<br>UNAUDITED<br>\$'000    | 30 SEPTEMBER<br>2016<br>AUDITED<br>\$'000 |
| <b>Date of event</b> |  |                                            |                                           |
| September 2010       |  | 2,000                                      | 7,700                                     |
| June 2011            |  | 255,700                                    | 256,500                                   |
| December 2011        |  | 486,600                                    | 487,500                                   |

## Sensitivity analysis – impact of changes in key variables

Net outstanding claims are comprised of several key elements, as set out earlier in this note. Sensitivity of net outstanding claims is therefore driven by changes to the assumptions underpinning each of these elements. The impact of changes in significant assumptions on the net outstanding claims liabilities, and hence on Tower's profit, are shown in the table below. Each change in assumption has been calculated in isolation of any other changes in assumptions.

The impact of a change to claims costs is offset by reinsurance where there is reinsurance capacity remaining. The impact will be nil where the change in claims costs is less than the remaining reinsurance capacity. However, if the change in claims costs exceeds the reinsurance capacity then Tower's profit will be impacted by the amount of claims costs in excess of the reinsurance capacity.



# Notes to the Interim Financial Statements

For the **half year** ended 31 March 2017

## 7. Canterbury earthquakes (continued)

The changes in the table below reflect the impact on Tower's profit before tax should that event occur.

|                                                                                                                                                                                                                                    |                    | SPLIT BETWEEN EVENTS            |                                 |                                 |                                 | FOUR MAIN EARTHQUAKES              |                                  |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------|---------------------------------|---------------------------------|---------------------------------|---------------------------------|------------------------------------|----------------------------------|
|                                                                                                                                                                                                                                    | CHANGE<br>VARIABLE | SEP<br>2010<br>UNAUDITED<br>\$M | FEB<br>2011<br>UNAUDITED<br>\$M | JUN<br>2011<br>UNAUDITED<br>\$M | DEC<br>2011<br>UNAUDITED<br>\$M | 31 MAR<br>2017<br>UNAUDITED<br>\$M | 30 SEP<br>2016<br>AUDITED<br>\$M |
| <b>Outstanding claims:</b>                                                                                                                                                                                                         |                    |                                 |                                 |                                 |                                 |                                    |                                  |
| (i) Change to costs and quantity of expected claim estimates including building costs and other impacts.                                                                                                                           | + 5%               | –                               | (4.0)                           | –                               | –                               | (4.0)                              | (4.1)                            |
|                                                                                                                                                                                                                                    | - 5%               | –                               | 4.0                             | –                               | –                               | 4.0                                | 4.1                              |
| (ii) Change in apportionment of claim costs to / from February 2011 event.                                                                                                                                                         | + 1%               | –                               | (9.3)                           | –                               | –                               | (9.3)                              | (9.0)                            |
|                                                                                                                                                                                                                                    | - 1%               | (4.4)                           | 9.3                             | –                               | –                               | 4.9                                | 9.0                              |
| <b>Receivables:</b>                                                                                                                                                                                                                |                    |                                 |                                 |                                 |                                 |                                    |                                  |
| <i>Reinsurance recovery receivables</i>                                                                                                                                                                                            |                    |                                 |                                 |                                 |                                 |                                    |                                  |
| (iii) Adverse development cover                                                                                                                                                                                                    | - 50%              | –                               | (21.9)                          | –                               | –                               | (21.9)                             | (21.9)                           |
|                                                                                                                                                                                                                                    | - 100%             | –                               | (38.8)                          | –                               | –                               | (38.8)                             | (38.8)                           |
| (iv) Recoveries from EQC in respect of land damage                                                                                                                                                                                 | + 10%              | –                               | 0.7                             | –                               | –                               | 0.7                                | 0.7                              |
|                                                                                                                                                                                                                                    | - 10%              | –                               | (0.7)                           | –                               | –                               | (0.7)                              | (0.8)                            |
| (v) Recoveries from EQC in respect of building costs                                                                                                                                                                               | + 10%              | –                               | 0.5                             | –                               | –                               | 0.5                                | 0.1                              |
|                                                                                                                                                                                                                                    | - 10%              | (1.8)                           | (0.5)                           | –                               | –                               | (2.3)                              | (0.1)                            |
| (i) Calculated as the change in case estimates (net of EQC contributions) plus IBNR/IBNER and the impact on Tower's profit quantified. Changes in case estimates include overcap claims, closed claims re-opening and risk margin. |                    |                                 |                                 |                                 |                                 |                                    |                                  |
| (ii) Calculated as 1% of total reported costs (net of EQC contributions) plus IBNR/IBNER moved to/from Feb 2011 event and the impact on Tower's profit quantified.                                                                 |                    |                                 |                                 |                                 |                                 |                                    |                                  |
| (iii) Calculated as the impact on net outstanding claims due to 50% or 100% lower recoveries being received.                                                                                                                       |                    |                                 |                                 |                                 |                                 |                                    |                                  |

# Notes to the Interim Financial Statements

For the **half year** ended 31 March 2016

## 8. Segmental reporting

|                                                    | NEW ZEALAND<br>\$000 | PACIFIC ISLANDS<br>\$000 | OTHER (HOLDING<br>COMPANIES &<br>ELIMINATIONS)<br>\$000 | TOTAL<br>\$000 |
|----------------------------------------------------|----------------------|--------------------------|---------------------------------------------------------|----------------|
| <b>Half year ended 31 March 2017 (Unaudited)</b>   |                      |                          |                                                         |                |
| <b>Revenue</b>                                     |                      |                          |                                                         |                |
| Revenue – external                                 | 109,452              | 22,115                   | 204                                                     | 131,771        |
| <b>Total revenue</b>                               | <b>109,452</b>       | <b>22,115</b>            | <b>204</b>                                              | <b>131,771</b> |
| <b>Profit (Loss) before income tax</b>             | (16,777)             | 6,696                    | (597)                                                   | (10,678)       |
| Income tax credit (expense)                        | 4,401                | (2,283)                  | 378                                                     | 2,496          |
| <b>Profit (Loss) for the half year</b>             | <b>(12,376)</b>      | <b>4,413</b>             | <b>(219)</b>                                            | <b>(8,182)</b> |
| <b>Half year ended 31 March 2016 (Unaudited)</b>   |                      |                          |                                                         |                |
| <b>Revenue</b>                                     |                      |                          |                                                         |                |
| Revenue – external                                 | 108,947              | 23,277                   | 764                                                     | 132,988        |
| <b>Total revenue</b>                               | <b>108,947</b>       | <b>23,277</b>            | <b>764</b>                                              | <b>132,988</b> |
| <b>Profit (Loss) before income tax</b>             | 3,476                | 6,117                    | (20,536)                                                | (10,943)       |
| Income tax credit (expense)                        | (1,799)              | (1,636)                  | 5,699                                                   | 2,264          |
| <b>Profit (Loss) for the half year</b>             | <b>1,677</b>         | <b>4,481</b>             | <b>(14,837)</b>                                         | <b>(8,679)</b> |
| <b>Total assets 31 March 2017 (Unaudited)</b>      | <b>477,981</b>       | <b>82,114</b>            | <b>75,966</b>                                           | <b>636,061</b> |
| Total assets 30 September 2016 (Audited)           | 479,420              | 79,104                   | 81,757                                                  | 640,281        |
| <b>Total liabilities 31 March 2017 (Unaudited)</b> | <b>365,286</b>       | <b>51,109</b>            | <b>3,272</b>                                            | <b>419,667</b> |
| Total liabilities 30 September 2016 (Audited)      | 360,613              | 51,981                   | 3,735                                                   | 416,329        |

### Description of segments and other segment information

An operating segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different to those of other operating segments.

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker who reviews the operating results on a regular basis and makes decisions on resource allocation and assessing performance. The chief operating decision-maker has been identified as the Company's Board of Directors.

New Zealand segment comprised general insurance business written in New Zealand. Pacific Islands segment includes general insurance business with customers in Pacific Islands written by Tower subsidiaries and branch operations. Other includes head office expenses, financing costs and eliminations.

Tower operates predominantly in two geographical segments, New Zealand and the Pacific region. Inwards reinsurance operations in run-off in the United Kingdom and the United States are a negligible part of the Group's operations and net assets.

# Notes to the Interim Financial Statements

For the **half year** ended 31 March 2017

## 9. Receivables

|                                            | 31 MARCH<br>2017<br>UNAUDITED<br>\$000 | 30 SEPTEMBER<br>2016<br>AUDITED<br>\$000 |
|--------------------------------------------|----------------------------------------|------------------------------------------|
| Reinsurance recovery receivables           | 80,715                                 | 68,406                                   |
| Outstanding premiums and trade receivables | 118,529                                | 125,855                                  |
| Other                                      | 71,347                                 | 60,424                                   |
| <b>Total receivables</b>                   | <b>270,591</b>                         | <b>254,685</b>                           |

### Earthquake Commission receivables

#### Kaikoura Region Earthquake

In December 2016 Tower Insurance Limited, along with other private insurers, signed a Memorandum of Understanding (MOU) with EQC whereby private insurers would act as agents for the Crown agency in relation to the Kaikoura region earthquake. Under the agreement, Tower will directly lodge, assess and settle home and contents claims arising from the 14 November 2016 earthquake in the Kaikoura region, including claims under EQC's \$100,000 cap for house claims and \$15,000 cap for contents claims. Claims from earlier earthquakes in the Canterbury region which are still open or unresolved are not part of this agreement with EQC. The agreement with EQC provides for private insurers to get reimbursed for claim costs, including costs of settlement and handling. The amount due from EQC for reimbursement of claims handling expenses and claims paid in relation to the Kaikoura event is \$1.4 million.

#### Canterbury Earthquakes

Other receivables includes an amount of \$66.6 million (30 September 2016: \$57.6 million) due from EQC for land damage and building costs relating to the Canterbury earthquake provisions as disclosed in Note 7. Tower has filed a statement of claim against EQC in respect of a portion of the \$66.6 million. An amount of \$17.5 million (30 September 2016: \$20.7 million) will be payable to reinsurers in relation to this balance, which has been provided for.

EQC recoveries relating to Canterbury earthquakes are an area of significant accounting estimation and judgement. Judgement and subjectivity included in the assessment of these EQC recoveries include: earthquake event allocation, litigation risk factors and other actuarial assumptions discussed in Note 7.

#### Reinsurance Contract In Dispute

Tower has a commercial dispute with Peak Re, the provider of the Adverse Development Cover (ADC) entered into in April 2015. As a result the parties have agreed to an arbitration process in accordance with the ADC agreement. Tower anticipates the arbitration will take place in the second half of 2017. Tower has received external legal advice and believes that it has a strong position and remains confident of full recovery. Tower will take every step to fully recover the amounts due.

The ADC provides for recovery of claims costs on the February 2011 earthquake. The maximum value of the ADC recovery is \$43.75 million which has been fully recognised in the calculation of Tower's net claims expense in respect of the Canterbury earthquakes (refer to Note 7).

Tower notes that, while it has confidence in its position, the process of legal redress has risk and collection of the \$43.75 million receivable cannot be certain.

# Notes to the Interim Financial Statements

For the **half year** ended 31 March 2016

## 10. Deferred tax

The value of deferred tax assets recognised in the financial statements involves a significant degree of judgement around the future profitability, ownership and legislative outcomes impacting the Group. In making the required judgements, management take account of all circumstances of which they are aware and current economic forecasts which might have a bearing on the tax situation concerned. Deferred tax assets held for any unused tax losses may only be recognised to the extent that it is probable that future profit will be available to offset the losses.

As at 31 March 2017, Tower Insurance Limited and companies within the Tower Limited consolidated tax group recognised deferred tax assets on loss carry forwards and other temporary differences. This is because on the basis of the approved strategic plans of Tower Insurance Limited and subsidiaries within the consolidated tax group, the Group considers it probable that the tax loss carry-forwards and temporary differences can be offset against future taxable profits.

### Potential impact of acquisition proposals

The recoverability of tax losses outlined above is subject to ongoing assessment. Accounting standards require de-recognition of deferred tax assets arising from loss carry forwards, where it is not probable that the entity will have sufficient income to use against the losses. Under New Zealand tax legislation losses are forfeited where there is a change of shareholding of more than 49%. If it becomes probable that either acquisition proposal to purchase 100% of the shares in Tower would result in a shareholder change of more than 49%, remaining deferred tax assets from loss carry forwards will be de-recognised and removed from the balance sheet.

The movement in deferred income tax assets and liabilities is as follows:

|                                                           | OPENING<br>BALANCE AT<br>1 OCTOBER<br>\$000 | (CHARGED)<br>CREDITED<br>TO INCOME<br>STATEMENT<br>\$000 | (CHARGED)<br>CREDITED TO<br>COMPREHENSIVE<br>INCOME<br>\$000 | CLOSING<br>BALANCE<br>\$000 |
|-----------------------------------------------------------|---------------------------------------------|----------------------------------------------------------|--------------------------------------------------------------|-----------------------------|
| <b>For the Half Year Ended 31 March 2017</b>              |                                             |                                                          |                                                              |                             |
| <b>Movement in deferred tax assets</b>                    |                                             |                                                          |                                                              |                             |
| Provisions and accruals                                   | 3,141                                       | 62                                                       | –                                                            | 3,203                       |
| Property, plant and equipment                             | 3,288                                       | (199)                                                    | –                                                            | 3,089                       |
| Tax losses                                                | 29,086                                      | 4,996                                                    | –                                                            | 34,082                      |
| <b>Total deferred tax assets</b>                          | <b>35,515</b>                               | <b>4,859</b>                                             | <b>–</b>                                                     | <b>40,374</b>               |
| Set-off of deferred tax liabilities pursuant to NZ IAS 12 |                                             |                                                          |                                                              | (4,652)                     |
| <b>Net deferred tax assets</b>                            |                                             |                                                          |                                                              | <b>35,722</b>               |
| <b>Movement in deferred tax liabilities</b>               |                                             |                                                          |                                                              |                             |
| Deferred acquisition costs                                | (4,851)                                     | 23                                                       | –                                                            | (4,828)                     |
| Other                                                     | (1,294)                                     | (307)                                                    | –                                                            | (1,601)                     |
| <b>Total deferred tax liabilities</b>                     | <b>(6,145)</b>                              | <b>(284)</b>                                             | <b>–</b>                                                     | <b>(6,429)</b>              |
| Set-off of deferred tax liabilities pursuant to NZ IAS 12 |                                             |                                                          |                                                              | 4,652                       |
| <b>Net deferred tax liabilities</b>                       |                                             |                                                          |                                                              | <b>(1,777)</b>              |

**Notes** to the Interim Financial StatementsFor the **half year** ended 31 March 2017**10. Deferred tax** (continued)

|                                                           | OPENING<br>BALANCE AT<br>1 OCTOBER<br>\$000 | (CHARGED)<br>CREDITED<br>TO INCOME<br>STATEMENT<br>\$000 | (CHARGED)<br>CREDITED TO<br>COMPREHENSIVE<br>INCOME<br>\$000 | CLOSING<br>BALANCE<br>\$000 |
|-----------------------------------------------------------|---------------------------------------------|----------------------------------------------------------|--------------------------------------------------------------|-----------------------------|
| <b>For the Year Ended 30 September 2016</b>               |                                             |                                                          |                                                              |                             |
| <b>Movement in deferred tax assets</b>                    |                                             |                                                          |                                                              |                             |
| Provisions and accruals                                   | 2,321                                       | 820                                                      | –                                                            | 3,141                       |
| Property, plant and equipment                             | 3,431                                       | (120)                                                    | (23)                                                         | 3,288                       |
| Tax losses                                                | 19,034                                      | 10,052                                                   | –                                                            | 29,086                      |
| <b>Total deferred tax assets</b>                          | <b>24,786</b>                               | <b>10,752</b>                                            | <b>(23)</b>                                                  | <b>35,515</b>               |
| Set-off of deferred tax liabilities pursuant to NZ IAS 12 |                                             |                                                          |                                                              | (5,360)                     |
| <b>Net deferred tax assets</b>                            |                                             |                                                          |                                                              | <b>30,155</b>               |
| <b>Movement in deferred tax liabilities</b>               |                                             |                                                          |                                                              |                             |
| Deferred acquisition costs                                | (4,885)                                     | 34                                                       | –                                                            | (4,851)                     |
| Other                                                     | (1,123)                                     | (171)                                                    | –                                                            | (1,294)                     |
| <b>Total deferred tax liabilities</b>                     | <b>(6,008)</b>                              | <b>(137)</b>                                             | <b>–</b>                                                     | <b>(6,145)</b>              |
| Set-off of deferred tax liabilities pursuant to NZ IAS 12 |                                             |                                                          |                                                              | 5,360                       |
| <b>Net deferred tax liabilities</b>                       |                                             |                                                          |                                                              | <b>(785)</b>                |

# Notes to the Interim Financial Statements

For the **half year** ended 31 March 2016

## 11. Intangible assets

### Impairment

The Group has reviewed the carrying value of software intangible assets for indicators of impairment as at 31 March 2017. Assessment of impairment indicators included reviewing the technical feasibility of completing the software development so it would be available for use; the intention to complete the software development; and whether the software would generate probable future economic benefits.

As at 31 March 2017 no impairment has been identified (31 March 2016: An impairment charge of \$19.65 million was recognised relating to internally developed software and software under development categories).

|                                                      | SOFTWARE          |                   |                                  |                               |                 |
|------------------------------------------------------|-------------------|-------------------|----------------------------------|-------------------------------|-----------------|
|                                                      | GOODWILL<br>\$000 | ACQUIRED<br>\$000 | INTERNALLY<br>DEVELOPED<br>\$000 | UNDER<br>DEVELOPMENT<br>\$000 | TOTAL<br>\$000  |
| <b>Half year ended 31 March 2017<br/>(Unaudited)</b> |                   |                   |                                  |                               |                 |
| <b>Cost:</b>                                         |                   |                   |                                  |                               |                 |
| Opening balance                                      | 17,744            | 5,020             | 31,305                           | 4,554                         | 58,623          |
| Additions                                            | –                 | 81                | 4,732                            | 4,332                         | 9,145           |
| Disposals                                            | –                 | –                 | –                                | (17)                          | (17)            |
| Transfers                                            | –                 | –                 | –                                | (4,732)                       | (4,732)         |
| Foreign exchange movements                           | –                 | (3)               | –                                | –                             | (3)             |
| <b>Closing balance</b>                               | <b>17,744</b>     | <b>5,098</b>      | <b>36,037</b>                    | <b>4,137</b>                  | <b>63,016</b>   |
| <b>Accumulated amortisation:</b>                     |                   |                   |                                  |                               |                 |
| Opening balance                                      | –                 | (4,265)           | (22,376)                         | –                             | (26,641)        |
| Amortisation charge                                  | –                 | (123)             | (2,997)                          | –                             | (3,120)         |
| <b>Closing balance</b>                               | <b>–</b>          | <b>(4,388)</b>    | <b>(25,373)</b>                  | <b>–</b>                      | <b>(29,761)</b> |
| <b>Net book value</b>                                |                   |                   |                                  |                               |                 |
| At cost                                              | 17,744            | 5,098             | 36,037                           | 4,137                         | 63,016          |
| Accumulated amortisation                             | –                 | (4,388)           | (25,373)                         | –                             | (29,761)        |
| <b>Closing net book value</b>                        | <b>17,744</b>     | <b>710</b>        | <b>10,664</b>                    | <b>4,137</b>                  | <b>33,255</b>   |

# Notes to the Interim Financial Statements

For the **half year** ended 31 March 2017

## 11. Intangible assets (continued)

|                                            | SOFTWARE          |                   |                                  |                               |                 |
|--------------------------------------------|-------------------|-------------------|----------------------------------|-------------------------------|-----------------|
|                                            | GOODWILL<br>\$000 | ACQUIRED<br>\$000 | INTERNALLY<br>DEVELOPED<br>\$000 | UNDER<br>DEVELOPMENT<br>\$000 | TOTAL<br>\$000  |
| <b>Year Ended 30 September 2016</b>        |                   |                   |                                  |                               |                 |
| <b>(Audited)</b>                           |                   |                   |                                  |                               |                 |
| <b>Cost:</b>                               |                   |                   |                                  |                               |                 |
| Opening balance                            | 17,744            | 4,223             | 34,861                           | 14,279                        | 71,107          |
| Additions                                  | –                 | 846               | 339                              | 7,070                         | 8,255           |
| Disposals                                  | –                 | (39)              | –                                | –                             | (39)            |
| Transfers                                  | –                 | –                 | –                                | (339)                         | (339)           |
| Foreign exchange movements                 | –                 | (10)              | –                                | –                             | (10)            |
| Transfers to Property, plant and equipment | –                 | –                 | –                                | (702)                         | (702)           |
| Impairment expense                         | –                 | –                 | (3,895)                          | (15,754)                      | (19,649)        |
| <b>Closing balance</b>                     | <b>17,744</b>     | <b>5,020</b>      | <b>31,305</b>                    | <b>4,554</b>                  | <b>58,623</b>   |
| <b>Accumulated amortisation:</b>           |                   |                   |                                  |                               |                 |
| Opening balance                            | –                 | (4,047)           | (18,687)                         | –                             | (22,734)        |
| Amortisation charge                        | –                 | (261)             | (3,689)                          | –                             | (3,950)         |
| Amortisation on disposals                  | –                 | 40                | –                                | –                             | 40              |
| Foreign exchange movements                 | –                 | 3                 | –                                | –                             | 3               |
| <b>Closing balance</b>                     | <b>–</b>          | <b>(4,265)</b>    | <b>(22,376)</b>                  | <b>–</b>                      | <b>(26,641)</b> |
| <b>Net book value</b>                      |                   |                   |                                  |                               |                 |
| At cost                                    | 17,744            | 5,020             | 31,305                           | 4,554                         | 58,623          |
| Accumulated amortisation                   | –                 | (4,265)           | (22,376)                         | –                             | (26,641)        |
| <b>Closing net book value</b>              | <b>17,744</b>     | <b>755</b>        | <b>8,929</b>                     | <b>4,554</b>                  | <b>31,982</b>   |

**Notes** to the Interim Financial StatementsFor the **half year** ended 31 March 2016**12. Insurance liabilities**

|                                    | 31 MARCH<br>2017<br>UNAUDITED<br>\$000 | 30 SEPTEMBER<br>2016<br>AUDITED<br>\$000 |
|------------------------------------|----------------------------------------|------------------------------------------|
| Unearned premiums                  | 145,928                                | 150,807                                  |
| Outstanding claims                 | 218,264                                | 210,202                                  |
| <b>Total insurance liabilities</b> | <b>364,192</b>                         | <b>361,009</b>                           |

**13. Distributions to shareholders****Dividend payments**

There were no dividend payments during the half year ended 31 March 2017.

On 24 November 2015 the Directors declared a final dividend for the 2015 financial year of 7.5 cents per share. The dividend was paid on 3 February 2016. The total amount paid was \$12,687,553. There were no imputation credits attached to the dividend and the Company did not offer its Dividend Reinvestment Plan for this dividend.

**Return of capital**

On 24 May 2016 the Directors announced the voluntary on-market share buyback would stop with immediate effect. Consequently there was no on-market share buyback during the half year ended 31 March 2017.

On 26 May 2015, following the Company's half year results announcement, the Company commenced an on market share buyback of up to \$34 million. Capital of \$2.4 million was bought back in the half year to 31 March 2016. In total \$14.6 million of capital was bought back and cancelled during the period to 31 March 2016.

**14. Net assets per share**

|                               | 31 MARCH<br>2017<br>UNAUDITED<br>\$ | 30 SEPTEMBER<br>2016<br>AUDITED<br>\$ |
|-------------------------------|-------------------------------------|---------------------------------------|
| Net assets per share          | 1.28                                | 1.33                                  |
| Net tangible assets per share | 0.88                                | 0.96                                  |

Net assets per share represent the value of the Group's total net assets divided by the number of ordinary shares on issue at the period end. Net tangible assets per share represent the net assets per share adjusted for the effect of intangible assets and deferred tax balances.



# Notes to the Interim Financial Statements

For the **half year** ended 31 March 2017

## 15. Solvency requirements

The minimum solvency capital required to be retained by Tower Insurance Limited Group to meet solvency requirements under the Insurance (Prudential Supervision) Act 2010 is shown below. Actual solvency capital exceeds the minimum solvency capital requirement for the Tower Insurance Limited Group by \$66.7 million (30 September 2016: \$73.8 million) and \$55.2 million for Tower Insurance Limited (30 September 2016: \$64.3 million).

|                          | TOWER INSURANCE LIMITED                |                                          | TOWER INSURANCE LIMITED GROUP          |                                          |
|--------------------------|----------------------------------------|------------------------------------------|----------------------------------------|------------------------------------------|
|                          | 31 MARCH<br>2017<br>UNAUDITED<br>\$000 | 30 SEPTEMBER<br>2016<br>AUDITED<br>\$000 | 31 MARCH<br>2017<br>UNAUDITED<br>\$000 | 30 SEPTEMBER<br>2016<br>AUDITED<br>\$000 |
| Actual solvency capital  | 111,710                                | 120,684                                  | 134,071                                | 140,827                                  |
| Minimum solvency capital | 56,548                                 | 56,350                                   | 67,386                                 | 67,047                                   |
| <b>Solvency margin</b>   | <b>55,162</b>                          | <b>64,334</b>                            | <b>66,685</b>                          | <b>73,780</b>                            |
| <b>Solvency ratio</b>    | <b>198%</b>                            | <b>214%</b>                              | <b>199%</b>                            | <b>210%</b>                              |

On 22 August 2014 the Reserve Bank of New Zealand imposed a condition of licence requirement for Tower Insurance Limited to maintain a minimum solvency margin of \$50.0 million. This minimum solvency requirement was confirmed on 15 September 2015 by the Reserve Bank of New Zealand.

The methodology and bases for determining the solvency margin are in accordance with the requirements of the Solvency Standard for Non-life Insurance Business published by the Reserve Bank of New Zealand.

## 16. Subsequent events

### Acquisition proposals

The acquisition proposals described in Note 2 remain under consideration by the Board. Timing of the proposed special meeting of shareholders to consider the Fairfax proposal remains uncertain. Both acquisition proposals remain subject to satisfactory completion of contractual conditions and regulatory approvals and in the case of the Suncorp proposal, contractual agreement.

### Weather events

Large parts of New Zealand were impacted in early April by Cyclone Debbie as it passed down the country. Edgecumbe was hardest hit when the Rangitaiki River breached stop banks and flooded the township. Tower estimates losses from Cyclone Debbie to be in the range of \$9.0 million to \$13.0 million.

Events occurring prior to 31 March 2017 (including scrub fires in the Port Hills, Christchurch and rain storms in Auckland and the North Island) had contributed to Tower's aggregate loss reinsurance programme excess being reached. As a result, the early April flooding event is covered up to \$5.0 million within Tower's aggregate loss reinsurance protection. Should ultimate claim costs for this event exceed \$5.0 million, Tower's full year profit will be impacted.

Tower has not been significantly impacted with claims arising from Cyclone Cook, which covered eastern areas of the North Island in mid-April. Similarly, Cyclone Donna which impacted the lower and central North Island in early May, did not result in significant claims for Tower.

### Facility drawdown

During May 2017, the Company utilised the Cash Advance Facility Agreement it has with BNZ. An amount of \$30.0 million was drawn (from an available \$50.0 million) and applied to additional solvency capital in Tower Insurance Limited.

**Notes** to the Interim Financial StatementsFor the **half year** ended 31 March 2016**17. Reconciliation of profit for the half year to net cash flows from operating activities**

|                                                                                                                     |  | FOR THE HALF YEAR ENDED                 |                                         |
|---------------------------------------------------------------------------------------------------------------------|--|-----------------------------------------|-----------------------------------------|
|                                                                                                                     |  | 31 MARCH<br>2017<br>UNAUDITED<br>\$'000 | 31 MARCH<br>2016<br>UNAUDITED<br>\$'000 |
| <b>Loss for the half year</b>                                                                                       |  | <b>(8,182)</b>                          | <b>(8,679)</b>                          |
| <b>Add (less) non-cash items</b>                                                                                    |  |                                         |                                         |
| Depreciation of property, plant and equipment                                                                       |  | 1,187                                   | 1,228                                   |
| Amortisation of software                                                                                            |  | 3,120                                   | 1,496                                   |
| Impairment of software                                                                                              |  | –                                       | 19,649                                  |
| Unrealised (gain) loss on financial assets                                                                          |  | (2,029)                                 | 1,574                                   |
| Gain on disposal of property, plant and equipment                                                                   |  | (51)                                    | –                                       |
| Decrease in deferred tax                                                                                            |  | (4,592)                                 | (5,636)                                 |
|                                                                                                                     |  | <b>(2,365)</b>                          | <b>18,311</b>                           |
| <b>Add (less) movements in working capital<br/>(excluding the effects of exchange differences on consolidation)</b> |  |                                         |                                         |
| (Increase) decrease in receivables                                                                                  |  | (16,010)                                | 12,056                                  |
| Decrease in payables                                                                                                |  | 3,529                                   | (43,220)                                |
| (Increase) decrease in taxation                                                                                     |  | (603)                                   | 1,748                                   |
|                                                                                                                     |  | <b>(13,084)</b>                         | <b>(29,416)</b>                         |
| <b>Add (less) other items classified as investing / financing activities</b>                                        |  |                                         |                                         |
| Financing costs                                                                                                     |  | 287                                     | –                                       |
|                                                                                                                     |  | <b>287</b>                              | <b>–</b>                                |
| <b>Net cash outflows from operating activities</b>                                                                  |  | <b>(23,344)</b>                         | <b>(19,784)</b>                         |

# Notes to the Interim Financial Statements

For the **half year** ended 31 March 2017

## 18. Fair value of financial assets and liabilities

Fair value is the price that would be received to sell an asset, or paid to transfer a liability, in an orderly transaction between market participants at the measurement date. Refer below for details of valuation methods and assumptions used by Tower for each category of financial assets and liabilities.

### (i) Cash and cash equivalents

The carrying amount of cash and cash equivalents reasonably approximates its fair value.

### (ii) Financial assets at fair value through profit or loss and held for trading

The fair value of financial instruments traded in active markets is based on quoted market prices at the balance sheet date. A market is regarded as active if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service, or regulatory agency, and those prices represent actual and regularly occurring market transactions on an arm's length basis. The quoted market price used for financial assets held by the Group is the current bid price. These instruments are included in Level 1.

The fair value of financial instruments that are not traded in an active market (for example, over-the-counter derivatives) is determined by using valuation techniques. These valuation techniques maximise the use of observable market data where it is available and rely as little as possible on entity specific estimates. If all significant inputs required to fair value an instrument are observable, the instrument is included in Level 2. The following fair value measurements are used:

- The fair value of fixed interest securities is based on the maturity profile and price/yield.
- The fair value of forward foreign exchange contracts is determined using forward exchange rates at the balance sheet date, with the resulting value discounted back to present value.
- Other techniques, such as discounted cash flow analysis, are used to determine fair value for the remaining financial instruments.

If one or more of the significant inputs is not based on observable market data, the instrument is included in Level 3. At 31 March 2017, the Level 3 category includes investment in equity securities of \$1,442,000 (30 September 2016: \$1,406,000). These investments are in unlisted shares of a company which provides reinsurance to Tower and a company which owns a building used by Tower. The fair value is calculated based on the net assets of the company from the most recently available financial information. In the case of the property owning company, the property is periodically independently valued. The valuation has been calculated using the Income Capitalisation Approach.

### (iii) Loans and receivables and other financial liabilities held at amortised cost

Carrying values of loans and receivables, adjusted for impairment values, and carrying values of other financial liabilities held at amortised cost reasonably approximate their fair values.

### (iv) Derivative financial liabilities and assets

The fair value of derivative financial liabilities and assets is determined by reference to market accepted valuation techniques using observable market inputs. There have been no transfers between levels of the fair value hierarchy during the current financial period (30 September 2016: nil).

**Notes** to the Interim Financial StatementsFor the **half year** ended 31 March 2016**18. Fair value of financial assets and liabilities** (continued)

The following tables present the Group's assets and liabilities which were measured at fair value, categorised by fair value measurement hierarchy levels.

|                                          | TOTAL<br>\$'000 | LEVEL 1<br>\$'000 | LEVEL 2<br>\$'000 | LEVEL 3<br>\$'000 |
|------------------------------------------|-----------------|-------------------|-------------------|-------------------|
| <b>As at 31 March 2017 (Unaudited)</b>   |                 |                   |                   |                   |
| <b>Assets</b>                            |                 |                   |                   |                   |
| Investment in equity securities          | 1,442           | –                 | –                 | 1,442             |
| Investments in fixed Interest securities | 181,830         | –                 | 181,830           | –                 |
| Investments in property securities       | 34              | –                 | 34                | –                 |
| Investments                              | 183,306         | –                 | 181,864           | 1,442             |
| Derivative financial assets              | 173             | –                 | 173               | –                 |
| <b>Total financial assets</b>            | <b>183,479</b>  | <b>–</b>          | <b>182,037</b>    | <b>1,442</b>      |
| <b>Liabilities</b>                       |                 |                   |                   |                   |
| Derivative financial liabilities         | 35              | –                 | 35                | –                 |
| <b>Total financial liabilities</b>       | <b>35</b>       | <b>–</b>          | <b>35</b>         | <b>–</b>          |
| <b>As at 30 September 2016 (Audited)</b> |                 |                   |                   |                   |
| <b>Assets</b>                            |                 |                   |                   |                   |
| Investment in equity securities          | 1,406           | –                 | –                 | 1,406             |
| Investments in fixed Interest securities | 187,082         | –                 | 187,082           | –                 |
| Investments in property securities       | 34              | –                 | 34                | –                 |
| Investments                              | 188,522         | –                 | 187,116           | 1,406             |
| Derivative financial assets              | 57              | –                 | 57                | –                 |
| <b>Total financial assets</b>            | <b>188,579</b>  | <b>–</b>          | <b>187,173</b>    | <b>1,406</b>      |
| <b>Liabilities</b>                       |                 |                   |                   |                   |
| Derivative financial liabilities         | 735             | –                 | 735               | –                 |
| <b>Total financial liabilities</b>       | <b>735</b>      | <b>–</b>          | <b>735</b>        | <b>–</b>          |

# Notes to the Interim Financial Statements

For the **half year** ended 31 March 2017

## 18. Fair value of financial assets and liabilities (continued)

The following table represents the changes in Level 3 instruments:

|                                                      | INVESTMENT IN EQUITY SECURITIES                 |                                                   |
|------------------------------------------------------|-------------------------------------------------|---------------------------------------------------|
|                                                      | AS AT<br>31 MARCH<br>2017<br>UNAUDITED<br>\$000 | AS AT<br>30 SEPTEMBER<br>2016<br>AUDITED<br>\$000 |
| <b>Opening balance</b>                               | 1,406                                           | 1,972                                             |
| Total gains and losses recognised in profit and loss | -                                               | (163)                                             |
| Foreign currency movement                            | 36                                              | (403)                                             |
| <b>Closing balance</b>                               | <b>1,442</b>                                    | <b>1,406</b>                                      |

The following table shows the impact of increasing or decreasing the combined inputs used to determine the fair value of the level 3 investments by 10%:

|                                             | CARRYING<br>AMOUNT<br>\$000 | FAVOURABLE<br>CHANGES OF 10%<br>\$000 | UNFAVOURABLE<br>CHANGES OF 10%<br>\$000 |
|---------------------------------------------|-----------------------------|---------------------------------------|-----------------------------------------|
| <b>As at 31 March 2017</b>                  |                             |                                       |                                         |
| Investment in equity securities (Unaudited) | 1,442                       | 144                                   | (144)                                   |
| <b>As at 30 September 2016</b>              |                             |                                       |                                         |
| Investment in equity securities (Audited)   | 1,406                       | 141                                   | (141)                                   |



## *Independent review report*

To the shareholders of Tower Limited

### *Report on the interim financial statements*

We have reviewed the accompanying financial statements of Tower Limited, ("the Group") on pages 10 to 35, which comprise the consolidated balance sheet as at 31 March 2017, and the consolidated income statement, the consolidated statement of comprehensive income, the consolidated statement of changes in equity and the consolidated statement of cash flows for the period ended 31 March 2017, and selected explanatory notes.

### *Directors' responsibility for the interim financial statements*

The Directors of Tower Limited are responsible for the preparation and presentation of these financial statements in accordance with New Zealand Equivalent to International Accounting Standard 34 Interim Financial Reporting (NZ IAS 34) and for such internal controls as the Directors determine are necessary to enable the preparation and fair presentation of the financial statements that are free from material misstatement, whether due to fraud or error.

### *Our responsibility*

Our responsibility is to express a conclusion on the accompanying financial statements based on our review. We conducted our review in accordance with the New Zealand Standard on Review Engagements 2410 *Review of Financial Statements Performed by the Independent Auditor of the Entity* (NZ SRE 2410). NZ SRE 2410 requires us to conclude whether anything has come to our attention that causes us to believe that the financial statements, taken as a whole, are not prepared in all material respects, in accordance with NZ IAS 34. As the auditors of the Group, NZ SRE 2410 requires that we comply with the ethical requirements relevant to the audit of the annual financial statements.

A review of financial statements in accordance with NZ SRE 2410 is a limited assurance engagement. The auditor performs procedures, primarily consisting of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. The procedures performed in a review are substantially less than those performed in an audit conducted in accordance with International Standards on Auditing (New Zealand) and International Standards on Auditing. Accordingly, we do not express an audit opinion on these financial statements.

We are independent of the Group. Our firm carries out other services for the Group in the areas of assurance and advisory. The provision of these other services has not impaired our independence. In addition, certain partners and employees of our firm may deal with the Group on normal terms within the ordinary course of trading activities of the Group. These matters have not impaired our independence. We have no other interests in the Group.

### *Conclusion*

Based on our review, nothing has come to our attention that causes us to believe that these financial statements of the Group are not prepared, in all material respects, in accordance with NZ IAS 34.

### *Who we report to*

This report is made solely to the Company's shareholders, as a body. Our review work has been undertaken so that we might state to the Company's shareholders those matters which we are required to state to them in our review report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the shareholders, as a body, for our review procedures, for this report, or for the conclusion we have formed.

For and on behalf of:

Chartered Accountants  
24 May 2017

Auckland

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PricewaterhouseCoopers, 188 Quay Street, Private Bag 92162, Auckland 1142, New Zealand  
T: +64 9 355 8000, F: +64 9 355 8001, pwc.co.nz

# Tower Directory

## Board of Directors

Michael Stiasny (Chairman)  
David Hancock  
Warren Lee  
Steve Smith  
Graham Stuart

## Chief Executive Officer

Richard Harding

## Company Secretary

David Callanan

## Executive leadership team

Richard Harding  
Tony Antonucci  
David Callanan  
Michelle James  
Faye Luxton  
Glenys Talivai  
Glenn Vade

## Registered Office

### NEW ZEALAND

Level 14  
Tower Centre  
45 Queen Street  
PO Box 90347  
Auckland  
Telephone: +64 9 369 2000  
Facsimile: +64 9 369 2245

### AUSTRALIA

C/- PricewaterhouseCoopers  
Nominees (N.S.W) Pty Ltd  
PricewaterhouseCoopers  
Darling Park Tower 2  
Level 1  
201 Sussex Street  
Sydney NSW 2000  
Australia

## Auditor

PricewaterhouseCoopers

## Banker

Westpac New Zealand Limited

## Enquiries

For customer enquiries, call Tower  
on 0800 808 808 or visit [tower.co.nz](http://tower.co.nz)

For investor enquiries:  
Telephone: +64 9 369 2000  
Email: [investor.relations@tower.co.nz](mailto:investor.relations@tower.co.nz)  
Website: [tower.co.nz](http://tower.co.nz)

## Company numbers

### TOWER LIMITED (INCORPORATED IN NEW ZEALAND)

NZ Incorporation 979635  
NZBN 9429 0374 84576  
ARBN 088 481 234

## Stock exchanges

The Company's ordinary shares are  
listed on the NZSX and the ASX. On  
Wednesday 18 May 2016, Tower's  
ASX admission category changed to  
"ASX Foreign Exempt Listing".

## Registrar

### NEW ZEALAND

Computershare Investor Services Limited  
Level 2, 159 Hurstmere Road  
Takapuna, Auckland  
Private Bag 92119  
Auckland 1142  
Freephone within New Zealand: 0800 222 065  
Telephone New Zealand: +64 9 488 8777  
Facsimile New Zealand: +64 9 488 8787

### AUSTRALIA

Computershare Investor Services Pty Limited  
Yarra Falls, 452 Johnston Street  
Abbotsford VIC 3067  
GPO Box 3329  
Melbourne Vic 3000  
Freephone within Australia: 1800 501 366  
Telephone Australia: +61 3 9415 4083  
Facsimile Australia: +61 3 9473 2500  
Email: [enquiry@computershare.co.nz](mailto:enquiry@computershare.co.nz)  
Website: [investorcentre.com/nz](http://investorcentre.com/nz)

You can also manage your holdings  
electronically by using Computershare's  
secure website [investorcentre.com/nz](http://investorcentre.com/nz)

This website enables holders to view  
balances, change addresses, view payment  
and tax information and update payment  
instruction and report options.

Tower recommends shareholders elect to  
have any payments direct credited to their  
nominated bank account in New Zealand or  
Australia to minimise the risk of fraud and  
misplacement of cheques.

Please quote your CSN number or  
shareholder number when contacting  
Computershare.

#### TOWER LIMITED INVESTOR RELATIONS

Telephone: +64 9 369 2000

Email: [investor.relations@tower.co.nz](mailto:investor.relations@tower.co.nz)

Website: [tower.co.nz](http://tower.co.nz)

#### REGISTRAR

Computershare Investor Services Limited

Freephone within New Zealand: 0800 222 065

Telephone New Zealand: +64 9 488 8777

Freephone within Australia: 1800 501 366

Telephone Australia: +61 3 9415 4083

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Website: [investorcentre.com/nz](http://investorcentre.com/nz)