Market Information
NZX Limited
Level 1, NZX Centre
11 Cable Street
Wellington
New Zealand

Company Announcements Office
ASX Limited
Exchange Centre
Level 6, 20 Bridge Street
Sydney NSW 2000
Australia

14 November 2017

# Tower Limited
## FY17 Full Year Results for Announcement to Market

In accordance with NZSX Listing Rule 10.3.1, I enclose the following for release to the market in relation to Tower Limited's (NZX/ASX: TWR) FY17 Full Year Results:

| | |
|---|---|
| 1 | Media Release |
| 2 | Management Review |
| 3 | NZX Appendix 1 |
| 4 | Financial Statements (including Independent Auditor's report) |
| 5 | Results announcement presentation |
| 6 | NZX Appendix 7 |
| 7 | ASX Appendix 3B |
| 8 | Rights issue cleansing notice |

Tower's Chairman Michael Stiassny, Chief Executive Officer Richard Harding and Chief Financial Officer Jeff Wright will discuss the full year results at 10:00am New Zealand time today.

Tower's Board confirms for the purposes of ASX Listing Rule 1.15.3 that Tower continues to comply with the NZX Main Board Listing Rules.

**ENDS**

David Callanan
Company Secretary
Tower Limited
ARBN 088 481 234
Incorporated in New Zealand

For further information, please contact:
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TOWER Limited,
Level 14, 45 Queen Street,
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14 November 2017

# IMPROVEMENT IN FULL YEAR RESULT AND CAPITAL RAISE TO ACCELERATE TRANSFORMATION

Tower Limited (NZX/ASX:TWR) has today reported a full year loss of $8 million for the year ended 30 September 2017 (FY17), an improvement of $13.5 million on the prior year.

Despite an unprecedented number of large natural events, underlying profit after tax of $18 million reflected the positive impact of transformation initiatives.

**Features of FY17 results announcement:**

- Reported full year loss after tax of $8 million impacted by Canterbury provisions, Kaikoura earthquake and corporate transaction activity

- Business initiatives driving improvements in core metrics demonstrating transformation is advancing well, providing confidence in strategy and future performance targets

- Further progress on Canterbury Earthquake claims with the number of open claims reducing by 241, down from 564 to 323

- The Tower Board has determined that an additional $70.8 million capital is required to enable investment in the business and manage inherent balance sheet risks

- Capital to be raised via pro-rata renounceable entitlement offer at a ratio of 1 New share for every 1 Existing share held. Issue price of NZ$0.42 cents. Vero has provided a commitment to participate in the Equity raise.

- Tower's Board remains strongly committed to paying dividends and to the efficient management of capital. It will review the dividend policy and look to recommence dividends in FY18.

**Overview**

Tower's full year result shows that its transformation into a leading digital challenger brand is well underway and the green shoots seen 12 months ago are now delivering growth.

Strong results in the New Zealand and the Pacific businesses have been delivered thanks to the continued drive to improve all aspects of the business and the customer experience:

- 12,441 policies were added to Tower's core NZ book in FY17
- Core GWP grew 5.8%, delivering full year GWP of $312.4 million
- Digital sales grew to 30% of new business transactions, up from 9% in March 2016
- Business as usual claims costs successfully contained at $124.2 million
- Management expenses reduced $3.9 million on the prior year

These significant improvements and a steady underlying profit have been delivered in the face of an unprecedented number of large natural events in 2017, industry wide claims inflation and an increasingly competitive market.

With significant opportunity in the business, Tower is confident its challenger brand transformation strategy will deliver long-term shareholder value.

TOWER Limited,
Level 14, 45 Queen Street,
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**Capital required to accelerate transformation**

Over the past 12 months, the Tower Board has focused on creating a sustainable structure to enable Tower to accelerate its transformation and confidently invest in its future, while also mitigating the fundamental uncertainty relating to the legacy of the Canterbury earthquakes.

Board Chairman, Michael Stiassny said it was in the best interests of policy and shareholders to now move to a durable capital structure that will support Tower's transformation programme while also managing inherent balance sheet risks.

"Following extensive, independent review of Tower's solvency capital, the Board determined that additional capital of $70 million is required to achieve those goals.

"That capital will provide Tower with a strong, durable base to appropriately manage risk and give confidence that the legacy of Canterbury is adequately provided for. It will also enable the acceleration of Tower's transformation through investment in IT and digital.

"The Board believes that improvements already achieved in the business core metrics are an indicator of the scale of opportunity within Tower. We are confident that investment will not only unlock that potential, but also deliver a true step change in results and long-term value for shareholders.

"Our commitment to paying dividends and efficient management of capital remains. The Board will review the dividend policy and look to recommence dividends in full year 2018," Mr Stiassny said.

**Powerful platform for future growth**

Tower CEO Richard Harding said that Tower's full year result demonstrates that the transformation of the business is well underway.

"As the third largest general insurer in New Zealand and one of the leading insurers in the Pacific, we have a powerful platform for future growth. The results we are delivering in the business are firm indicators that our strategy to transform Tower into a leading digital challenger brand is working.

"In the last 12 months we have grown our business, reduced management expense and contained claims costs, despite experiencing the highest number of natural event losses in over 25 years, excluding the Canterbury quakes.

"Importantly our focus on customers and delivering what they want through our digital channels has had a big impact, with 30% of sales now online, compared to 9%, eighteen months earlier.

**ENDS**

Richard Harding
Chief Executive Officer
Tower Limited
ARBN 088 481 234 Incorporated in New Zealand

**For media queries, please contact:**

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TOWER

## Tower management review – Full year to 30 September 2017

## Features of full year 2017

- Reported full year loss after tax of $8 million impacted by:
  - Increase in second-half Canterbury provisions of $1.6 million after tax, bringing the full after tax impact to $11.4 million for the year
  - $7.2 million after tax impact from an additional risk margin Tower's Board allocated for Canterbury claims
  - $4.1 million after tax impact from the Kaikoura earthquake
  - $3.1 million after tax impact from corporate transaction activity

- Following extensive, independent review of Tower's solvency capital, Tower's Board determined that an additional $70.8 million capital is required to enable investment in the business and manage inherent balance sheet risks

- Given the complexity of the Canterbury claims situation and the ongoing uncertainty in finalising these, Tower's Board has elected to create an additional risk margin of $10 million over and above the provision recommendation of the Appointed Actuary. This is currently equivalent to a probability of sufficiency between the 80-85th percentile.

- Underlying profit after tax of $18 million, with positive movements offset by unusually large number of natural events

- Transformation of core business continues with business initiatives delivering GWP and policy growth, closely contained claims costs and lower management expenses

- Further progress on Canterbury Earthquake claims with the number of open claims reducing by 241

## Full year summary

Tower reported a loss after tax of $8 million for the year ended 30 September 2017 (FY17), compared to a loss of $21.5 million for the year ended 30 September 2016 (FY16). Tower's FY17 result was impacted by further adjustments to Canterbury provisions, an additional risk margin Tower's Board allocated for Canterbury claims, Kaikoura earthquake and a number of other large loss events.

Tower delivered an underlying profit after tax of $18 million for FY17, a slight decline from $20.1 million in FY16 due to an unusually large number of natural events and the impact of lower interest rates on investment revenue.

Tower has strong underlying New Zealand and Pacific businesses with its strategic imperatives driving ongoing transformation.

During the year, Tower continued to improve the business, achieving policy growth in the core New Zealand book, growing its digital offering, delivering better claims performance, and reducing management expenses.

These improvements and positive results show Tower's transformation is well underway. However, this has been offset by an unusually large number of natural events in FY17 and the impact of lower interest rates on investment revenue.

Thanks to improvements in pricing risk and digital, Tower added 12,000 policies to its core New Zealand portfolio, seeing GWP grow 3% over the year to $312.4 million,

Tower's claims costs were controlled at $131.6 million despite experiencing one of the most severe natural disaster years in history. This was due to the success of initiatives launched in the past 12 months and continued focus on underwriting excellence.

A sharp focus on non-personnel costs saw the trend on management and sales expenses continue to decline. Expenses fell $3.9 million to $102.4 million for the year. These savings were achieved by driving high performance and productivity, building internal capability and close management of expenses.

Underlying profit in the Pacific increased to $7.2 million for FY17, compared to $5.5 million in FY16, due to a benign weather environment and improved underwriting.

Investment revenue fell $2.4 million to $6.1 million in FY17, as a result of lower interest rates and lower cash balances following Canterbury claims payments.

Tower continues to make solid progress settling claims in Canterbury, however, issues with EQC continue to hamper the entire industry.

In September 2016, Tower had 564 property claims remaining. In the intervening 12 months, the number of open Canterbury Earthquake claims was reduced by 241. However, new claims from the EQC continue to be received.

Tower's Appointed Actuary recommended a further $1.6m after-tax strengthening in second half, bringing the full after tax impact to $11.4 million for the year.

## GROUP PROFIT SUMMARY (NZ$m)

| $ million | FY17 | FY16 |
|---|---|---|
| Gross written premium | 312.4 | 303.2 |
| Gross earned premium | 306.8 | 302.9 |
| Reinsurance costs | (49.8) | (49.1) |
| **Net earned premium** | **256.9** | **253.8** |
| Net claims expense | (131.6) | (127.7) |
| Management and sales expenses | (102.4) | (106.3) |
| **Underwriting profit** | **22.9** | **19.8** |
| Investment revenue and other revenue | 6.1 | 8.5 |
| Financing costs | (0.8) | - |
| Underlying profit before tax | 28.2 | 28.3 |
| Income tax expense | (10.2) | (8.2) |
| **Underlying profit after tax** | **18.0** | **20.1** |
| Canterbury impact - Increase in outstanding claims | (11.4) | (25.3) |
| - Additional risk margin | (7.2) | - |
| Kaikoura impact | (4.1) | - |
| Impairment of intangibles | - | (14.1) |
| Business in runoff | 1.7 | - |
| Corporate transaction costs | (3.1) | - |
| Foreign tax credits written off | (1.9) | (2.2) |
| **Reported loss after tax** | **(8.0)** | **(21.5)** |

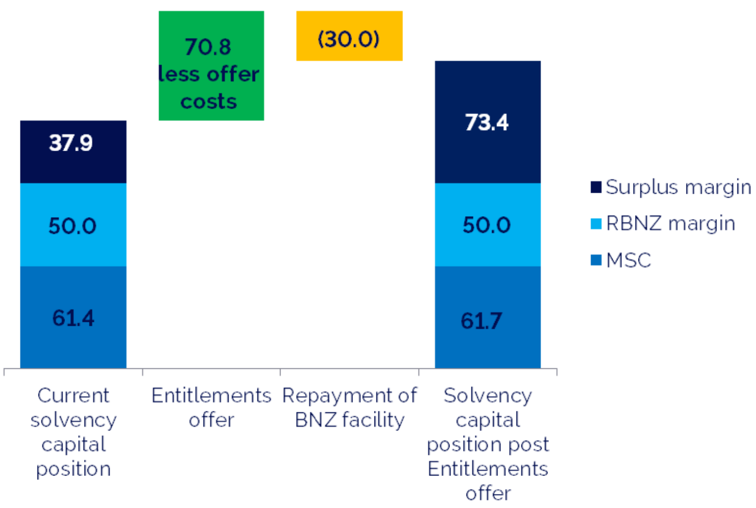
## Solvency position and capital requirements

Following extensive, independent review of Tower's solvency capital, Tower's Board determined that additional capital of $70.8 million is required to address the inherent uncertainty faced by the business, repay the BNZ facility, and to permit the signalled and ongoing reinvestment in Tower's NZ business.

If applied to Tower's solvency position at 30 September 2017, this would have resulted in Tower holding $123.4 million above minimum solvency capital requirements, or approximately 300% MSC.

Tower recognises the need for capital in the medium-term, however remains strongly committed to paying dividends and to the efficient management of capital. The Tower Board will review the dividend policy and look to recommence dividends in FY18.

**TOWER INSURANCE LIMITED SOLVENCY POSITION** ($m)




Note: Solvency capital calculation based on $70.8m entitlement offer less offer costs

## A New Zealand and Pacific general insurer

Being the third largest general insurer in New Zealand and one of the leading insurers in the Pacific provides the business with a powerful platform for future growth.

Tower has seen solid improvements in crucial areas that demonstrate the business' transformation into the leading digital challenger brand is well underway:

- Focus on customers has delivered policy and GWP growth
- Management expenses continue the downward trend, decreasing $3.9 million when compared to the prior year
- Tight management of claims processes and supplier networks resulted in contained claims costs

**Focus on customers delivers growth**

Achievements

- New digital programme supporting core GWP growth of 5.8% over prior year
- Tower Direct retention improved 2.0% points on prior year
- Online sales increased from 9% of new business transactions in March 2016, to 30% in September 2017
- New, simple and easy products improving lead conversion – currently 4% points above target

Tower's focus on customers has seen continued growth in its core New Zealand portfolio in FY17, with 12,441 policies added to the core book and GWP increasing 5.8%.

With Tower's new product suite fully available online, more customers can research, quote and buy insurance from Tower through their mobile, tablet or computer, delivering a significant uplift in new business sales.

Encouraging existing customers to stay with Tower through targeted retention initiatives and offerings has delivered an increase in retention rates for the direct Tower business, up 2 percentage points.

This positive result is being achieved through a combination of:

- building and refining Tower's digital offering, including the relaunch of the new Trade Me Insurance platform
- working harder to attract new customers to Tower, particularly in attractive segments which are actively targeted
- new products making it easier for Tower's team to convert sales leads
- tailored, targeted insurance offers available for customers using digital channels

**Claims and underwriting update**

Achievements

- Over 30 product updates, pricing reviews and targeted rate changes across all New Zealand portfolios
- Supply chain and preferred supplier initiatives delivered material savings
- New vehicle risk ratings further reducing claims frequency
- Excess changes significantly improved average claims costs

Tower is actively managing its portfolio and delivering simple and easy insurance, which is helping attract the right customers to Tower. This focus on underwriting excellence has helped control claims costs despite an unprecedented number of large natural events.

The New Zealand insurance industry is also experiencing inflation in the frequency and cost of motor claims. This is due to the greater number of cars on the road and the increased costs and constraints in the repair industry supply chain.

Recent storms have resulted in large event claims increasing by $3.6 million, to $7.4 million, compared to the same period last year.

While industry inflation has eroded some of the gains made in the first half of the year, initiatives introduced over the past 12 months have contained business as usual claims costs at $124.2 million.

This positive result in controlling claims costs is as a result of:

- better risk selection and underwriting processes
- tighter management of end-to-end claims supply chain

- simpler policy wordings enabling customers and claims teams to easily understand exactly what customers are entitled to
- regular review and improvements to policy wordings, including the capping of meth benefits and removal of excess refund
- continued focus on claims leakage and recoveries

**Kaikoura earthquake and storm events**

Achievements
- 100% of Tower motor claims, 97% of contents and 79% of over-cap and other house claims finalised
- 99% of EQC contents claims and 82% of EQC home claims that relate to Tower's Kaikoura customers closed
- $3.1m reduction of after tax impact of Kaikoura earthquakes from H1, from $7.2m to $4.1m
- $1.5m reduction of after tax impact of Ex-Cyclone Debbie and associated flooding in Edgecumbe since April 2017, from $3.6m to $2.1m

While Tower's aggregate reinsurance cover is helping to absorb some of the costs of the recent storm volatility; efficient and proactive management of claims has had the biggest impact in reducing the total cost of these events.

Tower's team has been working hard to set things right for customers in Kaikoura, Edgecumbe and other areas that have experienced large natural events.

The after tax impact of the Kaikoura earthquakes, attributable to Tower, reduced by $3.1 million from the first half (down from $7.2 million to $4.1 million).

The after tax impact of Ex-Cyclone Debbie claims, attributable to Tower, reduced by $1.8 million since April 2017 (down from $3.6 million to $1.8 million).

Thanks to dedicated claims teams, Tower's customers impacted by the Kaikoura earthquake can be confident that their claims will be finalised in early 2018. Tower is confident that most, if not all customers impacted by the Edgecumbe floods will have their claim finalised, or where repairs are being undertaken, will be back in their homes by Christmas.

This pleasing result is thanks to:
- a focus on early intervention and effective claims management
- a single point of contact for customers enabling quick resolution of claims
- new ways of working with EQC providing insurers with complete visibility of all claims relating to their customers

**Focus on costs**

Achievements
- Increased focus on efficiency and productivity
- Significant saving through in-housing IT service desk and other key support functions
- Whole of business procurement review and close management of contract negotiations
- Some costs deferred as a result of acquisition and separation activity

Tower has strengthened its focus on non-personnel related costs, reducing management expenses to $102.4 million in FY17, down from $106.3 million in FY16.

Tower's savings of approximately $3.9 million in its core underlying expenses, compared to FY16, 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 and building capability internally

Tower expects expenses will continue to decrease as simplification programme initiatives are embedded. A step change in productivity gains and expense reduction will be dependent on long-term IT investment.

**IT simplification**

Tower has continued stabilising core legacy systems and enhancing its digital offerings to deliver a consistent customer experience.

While some improvements have been made, there are many operational efficiencies to be derived from moving from four core IT systems with dozens of ancillary systems, to a single core system with a small number of critical interfaces.

Tower has selected EIS as its preferred partner to complete the formal scoping and costing processes following a comprehensive tender. Some work has already commenced, with EIS working with the Tower team to establish a firm implementation timeline and itemised project deliverables. Board approval will be sought once costs and the timeline are confirmed.

The new build is likely to take 12 months, following which new business will immediately go live on the new platform and migration of the legacy book can start.

**Canterbury update**

As has been regularly reiterated by Tower and other industry players, the ongoing legacy of the Canterbury earthquakes has resulted in significant issues for customers and insurers, with the receipt of EQC over-cap claims continuing in 2017.

Tower is making good progress closing Canterbury Earthquake claims. In September 2016, Tower had 564 property claims remaining. In the past 12 months, 403 have been closed, while receiving 73 completely new over-cap claims form the EQC, and 33 new under-cap claims in the interim. This resulted in the number of open Canterbury claims reducing by 241 in FY17.

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

Tower's Appointed Actuary recommended a further $1.6m after-tax strengthening in second half, bringing the full after tax impact to $11.4 million for the year.

Given the complexity of the Canterbury claims situation and the ongoing uncertainty in finalising these, Tower's Board has elected to create an additional risk margin of $10 million over and above the provision recommendation of the Appointed Actuary. This is currently equivalent to a probability of sufficiency between the 80-85th percentile.

The net result of the Appointed Actuary's recommendations is that Tower's IBNR and risk margin allowance have increased from 60% in September 2016 to 99% of underlying case estimates in September 2017.

| (NZ$m) | Sep-17 | % of case estimates[2] | Mar-17 | % of case estimates[2] | Sep-16 | % of case estimates[2] |
|---|---|---|---|---|---|---|
| Case estimates | 58.9 | | 73.9 | | 93.2 | |
| IBNR/IBNER[1] | 34.4 | | 47.4 | | 44.0 | |
| Risk margin | 13.9 | | 18.2 | | 11.9 | |
| Additional risk margin | 10.0 | | - | | - | |
| Combined IBNR/IBNER/risk margin | 58.3 | 99% | 65.6 | 89% | 55.9 | 60% |
| **Gross outstanding claims** | **117.2** | | **139.5** | | **149.1** | |

While Tower is making significant progress closing claims, more certainty is still required. EQC Act reform will assist in ensuring past experience is not repeated. It is also important that the changes in EQC protocols that have made Kaikoura successful are included in any future reform. Tower continues to strongly believe more needs to be done by the EQC and New Zealand government.

## Outlook

Tower remains confident that it can continue the transformation of the underlying business and deliver long-term shareholder value.

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

- drive GWP growth of 4 – 6%
- reduce expense ratio to below 35%
- deliver return on equity of 12 – 14% through the cycle

The implementation of these strategic imperatives will continue driving the transformation of the business.

However, a fundamental step change in Tower's performance will be delivered through IT simplification. Significant management focus will go into this in FY18, with benefits expected to flow through from FY19.

In the longer term, the results of the work being delivered will strengthen Tower's performance, unlock further opportunities and create long term, sustainable shareholder value.

| Tower Limited | |
|---|---|
| **Results for announcement to the market** | |
| Reporting Period | 12 months to 30 September 2017 |
| Previous Reporting Period | 12 months to 30 September 2016 |

| | Amount (000s) | Percentage change |
|---|---|---|
| Revenue from ordinary activities | $NZ317,443 | 0.7% increase |
| Profit (loss) from ordinary activities after tax attributable to security holder | $NZ(8,000) | 62.8% decrease |
| Net profit (loss) attributable to security holders | $NZ(8,000) | 62.8% decrease |

| Interim/Final Dividend | Amount per security | Imputed amount per security |
|---|---|---|
| | $NZ nil. It is not proposed to pay dividends. | $NZ nil. |

| Record Date | Not Applicable |
|---|---|
| Dividend Payment Date | Not Applicable |

| Comments: | For the year-ended 30 September 2017, Tower Limited's reported loss from ordinary activities after tax was NZ$8.0 million due to increased outstanding claims provisions in respect of Canterbury earthquakes (NZ$11.4 million after tax); the inclusion of an additional risk margin of $7.2 million after tax and claim provisions relating to the Kaikoura earthquakes (NZ$4.1 million after tax). |
|---|---|
| | The loss of NZ$8.0 million, including minority interest profit of NZ$ 0.5 million, is a decrease of 62% from the prior comparable period (FY16: NZ$21.5m loss including minority interest profit of NZ$ 0.8 million). |

Refer to the attached 30 September 2017 audited Financial Statements for Tower Limited and its subsidiaries and Investor Presentation for more detailed analysis and explanation (including the Net Tangible Asset amount per security for the current and previous reporting period).

# TOWER LIMITED
# FINANCIAL STATEMENTS

**FOR THE YEAR ENDED 30 SEPTEMBER 2017**

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## CONSOLIDATED INCOME STATEMENT

| $ thousands<br>For the year ended 30 September | Note | 2017 | 2016 |
|---|---|---|---|
| **Revenue** | | | |
| Premium revenue | 5 | **306,760** | 302,940 |
| Less: Outwards reinsurance expense | | **(49,845)** | (49,106) |
| **Net premium revenue** | | **256,915** | 253,834 |
| Investment revenue | 6 | **7,643** | 8,998 |
| Fee and other revenue | | **3,040** | 3,413 |
| **Net operating revenue** | | **267,598** | 266,245 |
| | | | |
| **Expenses** | | | |
| Claims expense | | **217,547** | 240,138 |
| Less: Reinsurance recoveries revenue | | **(29,996)** | (54,526) |
| **Net claims expense** | 7 | **187,551** | 185,612 |
| | | | |
| Management and sales expenses | 9 | **81,744** | 87,410 |
| Acquisition proposal expenses | 4 | **3,467** | - |
| Impairment expense | 15 | **-** | 19,649 |
| Financing expenses | | **835** | - |
| **Total expenses** | | **273,597** | 292,671 |
| | | | |
| **Profit (Loss) attributed to shareholders before tax** | | **(5,999)** | (26,426) |
| Tax (expense) benefit attributed to shareholders' profits | 10A | **(2,001)** | 4,911 |
| **Profit (Loss) for the year** | | **(8,000)** | (21,515) |
| | | | |
| **Profit (Loss) attributed to:** | | | |
| Shareholders | | **(8,461)** | (22,328) |
| Non-controlling interest | | **461** | 813 |
| | | **(8,000)** | (21,515) |
| | | | |
| Basic and diluted profit (loss) per share (cents) | 26 | **(5.02)** | (13.21) |

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

# CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

| $ thousands<br>For the year ended 30 September | Note | 2017 | 2016 |
|---|---|---|---|
| **Profit (Loss) for the year** | | **(8,000)** | (21,515) |
| **Other comprehensive income (loss)** | | | |
| Currency translation differences | | **105** | (5,910) |
| Gain on asset revaluation | 17 | **247** | 181 |
| Deferred income tax relating to asset revaluation | 10D | **(29)** | (23) |
| **Other comprehensive income (loss) net of tax** | | **323** | (5,752) |
| **Total comprehensive income (loss) for the year** | | **(7,677)** | (27,267) |
| **Total comprehensive income (loss) attributed to:** | | | |
| Shareholders | | **(8,143)** | (27,404) |
| Non-controlling interest | | **466** | 137 |
| | | **(7,677)** | (27,267) |

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

## CONSOLIDATED BALANCE SHEET

| $ thousands<br>As at 30 September | Note | 2017 | 2016 |
|---|---|---|---|
| **Assets** | | | |
| Cash and cash equivalents | 12 | **102,876** | 92,228 |
| Receivables | 14 | **261,375** | 254,685 |
| Investments | 28 | **167,702** | 188,522 |
| Derivative financial assets | 28 | **231** | 57 |
| Deferred acquisition costs | 16 | **20,961** | 19,973 |
| Current tax assets | 10B | **13,462** | 13,168 |
| Property, plant and equipment | 17 | **8,780** | 9,511 |
| Intangible assets | 15 | **31,334** | 31,982 |
| Deferred tax assets | 10D | **32,745** | 30,155 |
| **Total assets** | | **639,466** | 640,281 |
| **Liabilities** | | | |
| Payables | 18 | **51,124** | 49,500 |
| Current tax liabilities | 10C | **560** | 123 |
| Provisions | 19 | **5,773** | 4,177 |
| Derivative financial liabilities | 28 | **-** | 735 |
| Insurance liabilities | 20 | **336,004** | 361,009 |
| Borrowings | 22 | **29,921** | - |
| Deferred tax liabilities | 10D | **340** | 785 |
| **Total liabilities** | | **423,722** | 416,329 |
| **Net assets** | | **215,744** | 223,952 |
| **Equity** | | | |
| Contributed equity | 23 | **382,172** | 382,172 |
| Accumulated (losses) profit | | **(51,299)** | (42,822) |
| Reserves | 24 | **(116,454)** | (116,772) |
| **Total equity attributed to shareholders** | | **214,419** | 222,578 |
| Non-controlling interest | | **1,325** | 1,374 |
| **Total equity** | | **215,744** | 223,952 |

**The financial statements were approved for issue by the Board on 14 November 2017.**

Michael P Stiassny
**Chairman**

Graham R Stuart
**Director**

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

## CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

| $ thousands | Note | Attributed to shareholders<br>Contributed equity | Accumulated (losses) profit | Reserves | Total | Non-controlling interest | Total Equity |
|---|---|---|---|---|---|---|---|
| **Year Ended 30 September 2017** | | | | | | | |
| At the beginning of the year | | **382,172** | **(42,822)** | **(116,772)** | **222,578** | **1,374** | **223,952** |
| **Comprehensive income (loss)** | | **-** | **(8,461)** | **318** | **(8,143)** | **466** | **(7,677)** |
| **Transactions with shareholders** | | | | | | | |
| Dividends paid | 21 | **-** | **-** | **-** | **-** | **(515)** | **(515)** |
| Other | | **-** | **(16)** | **-** | **(16)** | **-** | **(16)** |
| **Total transactions with shareholders** | | **-** | **(16)** | **-** | **(16)** | **(515)** | **(531)** |
| **At the end of the year** | | **382,172** | **(51,299)** | **(116,454)** | **214,419** | **1,325** | **215,744** |
| **Year Ended 30 September 2016** | | | | | | | |
| At the beginning of the year | | 384,585 | 6,376 | (111,696) | 279,265 | 1,644 | 280,909 |
| **Comprehensive income (loss)** | | - | (22,328) | (5,076) | (27,404) | 137 | (27,267) |
| **Transactions with shareholders** | | | | | | | |
| Capital repayment plan | 21, 23 | (2,413) | - | - | (2,413) | - | (2,413) |
| Dividends paid | 21 | - | (27,024) | - | (27,024) | (407) | (27,431) |
| Other | | - | 154 | - | 154 | - | 154 |
| **Total transactions with shareholders** | | (2,413) | (26,870) | - | (29,283) | (407) | (29,690) |
| **At the end of the year** | | 382,172 | (42,822) | (116,772) | 222,578 | 1,374 | 223,952 |

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

## CONSOLIDATED STATEMENT OF CASH FLOWS

| $ thousands<br>For the year ended 30 September | Note | **2017** | 2016 |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Premiums received | | **309,147** | 295,867 |
| Interest received | | **7,734** | 10,088 |
| Dividends received | | **-** | 9 |
| Net realised investment gain (loss) | | **(1,928)** | 3,251 |
| Fee and other income received | | **3,040** | 3,413 |
| Reinsurance received | | **28,962** | 67,935 |
| Reinsurance paid | | **(50,228)** | (47,248) |
| Claims paid | | **(248,183)** | (261,779) |
| Payments to suppliers and employees | | **(76,408)** | (77,248) |
| Income tax paid | | **(4,908)** | (4,598) |
| **Net cash inflow (outflow) from operating activities** | 13 | **(32,772)** | (10,310) |
| **Cash flows from investing activities** | | | |
| Net proceeds from financial assets | | **21,852** | 18,380 |
| Purchase of property, plant and equipment and intangible assets | | **(6,883)** | (9,175) |
| Disposal of property, plant and equipment and intangible assets | | **136** | 70 |
| **Net cash inflow (outflow) from investing activities** | | **15,105** | 9,275 |
| **Cash flows from financing activities** | | | |
| Capital repayment | | **-** | (2,413) |
| Dividends paid | | **-** | (27,024) |
| Facility fees and interest paid | | **(778)** | - |
| Proceeds of borrowings | | **30,000** | - |
| Capital raise costs | | **-** | - |
| Payment of non-controlling interest dividends | | **(515)** | (407) |
| **Net cash inflow (outflow) from financing activities** | | **28,707** | (29,844) |
| **Net increase (decrease) in cash and cash equivalents** | | **11,040** | (30,879) |
| Foreign exchange movement in cash | | **(392)** | (2,006) |
| Cash and cash equivalents at the beginning of year | | **92,228** | 125,113 |
| **Cash and cash equivalents at the end of year** | 12 | **102,876** | 92,228 |

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

# NOTES TO THE FINANCIAL STATEMENTS

## 1 SUMMARY OF GENERAL ACCOUNTING POLICIES

### Entities reporting

The financial statements presented are those of Tower Limited (the Company) and its subsidiaries (the Group). The Company and its subsidiaries together are referred to in this financial report as Tower or the Group or the consolidated entity. The address of the Company's registered office is 45 Queen Street, Auckland, New Zealand.

During the periods presented, the principal activity of Tower Limited Group was the provision of general insurance. The Group predominantly operates in New Zealand with some of its operations based in the Pacific Islands region.

### Statutory base

Tower Limited is a company incorporated in New Zealand under the Companies Act 1993 and listed on the New Zealand and Australian Stock Exchanges. The Company is a Financial Markets Conduct Act 2013 reporting entity under Part 7 of the Financial Markets Conduct Act 2013.

### Basis of preparation

The financial statements of the Group have been prepared in accordance with New Zealand Generally Accepted Accounting Practice (NZ GAAP). They comply with International Financial Reporting Standards (IFRS) and also New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS) and other applicable financial reporting standards, as appropriate for Tier 1 for-profit entities.

The financial statements of the Group have been prepared in accordance with the requirements of Part 7 of the Financial Markets Conduct Act 2013 and the NZX Main Board Listing Rules.

The Group financial statements are presented in New Zealand dollars and rounded to the nearest thousand dollars. They have been prepared on a fair value measurement basis with any exceptions noted in the accounting policies below, or in the notes to the financial statements.

### Principles of consolidation

The Group financial statements incorporate the assets and liabilities of all subsidiaries of the Company at balance date and the results of all subsidiaries for the year.

Subsidiaries are those entities over which the consolidated entity has control, being power over the investee; exposure, or rights to variable returns from its involvement with the investee; and the ability to use its power over the investee to affect the amount of the investor’s returns.

The results of any subsidiaries acquired during the year are consolidated from the date on which control was transferred to the consolidated entity and the results of any subsidiaries disposed of during the year are consolidated up to the date control ceased.

The acquisition of controlled entities from external parties is accounted for using the acquisition method of accounting. The share of net assets of controlled entities attributable to minority interests is disclosed separately in the balance sheet, income statement and statement of comprehensive income. Acquisition related costs are expensed as incurred.

When the Group ceases to have control, any retained interest in the entity is re-measured to its fair value at the date when control is lost, with the change in carrying amount recognised in profit or loss.

Intercompany transactions and balances between Group entities are eliminated on consolidation.

### Foreign currency

*(i) Functional and presentation currencies*

The financial statements of each Group entity are presented in the currency of the primary economic environment in which the entity operates. The consolidated Group financial statements are presented in New Zealand dollars and rounded to the nearest thousand dollars unless stated otherwise.

# NOTES TO THE FINANCIAL STATEMENTS

## 1 SUMMARY OF GENERAL ACCOUNTING POLICIES (continued)

*(ii) Transactions and balances*

In preparing the financial statements of the individual entities, transactions denominated in foreign currencies are translated into New Zealand dollars using the exchange rates in effect at the transaction dates. Monetary items receivable or payable in a foreign currency are translated at reporting date at the closing exchange rate.

Translation differences on non-monetary items such as financial assets held at fair value through profit or loss are reported as part of their fair value gain or loss.

Exchange differences arising on the settlement or retranslation of monetary items at year end exchange rates are recognised in the income statements unless the items form part of a net investment in a foreign operation. In this case, exchange differences are taken to the Foreign Currency Translation Reserve and recognised in the statements of comprehensive income and the statements of changes in equity.

*(iii) Consolidation*

For the purpose of preparing consolidated financial statements the assets and liabilities of subsidiaries with a functional currency different to the Company are translated at the closing rate at the balance date. Income and expense items for each subsidiary are translated at a weighted average of exchange rates over the period, as a surrogate for the spot rates at transaction dates. Foreign currency translation differences are taken to the Foreign Currency Translation Reserve and recognised in the statements of comprehensive income and the statements of changes in equity.

Goodwill and fair value adjustments arising on the acquisition of a foreign operation are treated as assets and liabilities of the foreign operation and are translated at the closing rate with movements recorded through the Foreign Currency Translation Reserve in the statements of changes in equity.

On disposal of a foreign entity, the deferred cumulative amount recognised in equity relating to that particular foreign operation is recognised in the income statements.

**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.

## 2 IMPACT OF AMENDMENTS TO NZ IFRS

### 2A Standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the Group

The following standards, amendments and interpretations to existing standards have been published and are mandatory for the Group's accounting periods beginning after 1 October 2017 or later periods, and the Group has not adopted them early. The Group expects to adopt the following new standards on 1 October after the effective date.

- **NZ IFRS 15 Revenue from Contracts with Customers** is effective for periods beginning on or after 1 January 2018. The standard will provide a single source of requirements for accounting for all contracts with customers (except for some specific exceptions, such as lease contracts, insurance contracts and financial instruments) and will replace all current accounting pronouncements on revenue. New revenue disclosures are also introduced. Tower is assessing the effect of adopting NZ IFRS 15 on its financial statements.

- **NZ IFRS 16 Leases** is effective for periods beginning on or after 1 January 2019. The standard replaces the current guidance in NZ IAS 17 Leases. Under NZ IFRS 16, a contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. Under NZ IAS 17, a lessee was required to make a distinction between a finance lease (on balance sheet) and an operating lease (off balance sheet). NZ IFRS 16 now requires a lessee to recognise a lease liability reflecting future lease payments and a 'right-of-use asset' for virtually all lease contracts. Work continues on assessing the impact of adopting IFRS 16 on Tower's financial statements. Preliminary assessments indicate the treatment of office buildings, motor vehicles, and other equipment leases will change. The potential financial impact of changes will result in the creation of a 'right of use asset' of approximately $11 million, with a corresponding lease liability amount to be recognised, in effect as a gross up to the balance sheet, of approximately $11 million to $12 million.

- **NZ IFRS 9 Financial instruments** is effective for periods beginning on or after 1 January 2018. The complete version of NZ IFRS 9 was issued in September 2014. It replaces the guidance in NZ IAS 39 that relates to the classification and measurement of financial instruments. NZ IFRS 9 retains but simplifies the mixed measurement model and establishes three primary measurement categories for financial assets: amortised cost, fair value through other comprehensive income and fair value through profit or loss. The basis of classification depends on the entity's business model and the contractual cash flow characteristics of the financial asset. Investments in equity instruments are required to be measured at fair value through profit or loss with the irrevocable option at inception to present changes in fair value in other comprehensive income not recycling. There is now a new expected credit losses model that replaces the incurred loss impairment model used in NZ IAS 39. For financial liabilities there were no changes to classification and measurement except for the recognition of changes in own credit risk in other comprehensive income, for liabilities designated at fair value through profit or loss. NZ IFRS 9 relaxes the requirements for hedge effectiveness by replacing the bright line hedge effectiveness tests. It requires an economic relationship between the hedged item and hedging instrument and for the 'hedged ratio' to be the same as the one management actually use for risk management purposes. Contemporaneous documentation is still required but is different to that currently prepared under NZ IAS 39. The Group intends to adopt NZ IFRS 9 on its effective date and is assessing the effect of adopting NZ IFRS 9 on its financial statements.

- **NZ IFRS 17 Insurance Contracts** is effective for periods beginning on or after 1 January 2021. The standard replaces the current guidance in NZ IFRS 4, and establishes the principles for recognition, measurement, presentation and disclosure of insurance contracts. The implementation date for the Group will be for the year ending 30 September 2022. A detailed assessment of the effect of adopting NZ IFRS 17 will be commenced during 2018.

- **Amendments to NZ IAS 7 Statement of Cash Flows** is effective for periods beginning on or after 1 October 2017 unless early adopted. Comparatives are not required on first application. The standard requires additional disclosures regarding both cash and non-cash changes in liabilities arising from financing activities. The standard is not expected to have a material impact.

### 2B Standards, amendments and interpretations to existing standards effective 30 September 2017 or early adopted by the Group

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

### 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 8 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 8 and Note 14 for further detail on EQC recoveries for Canterbury earthquakes.

**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 Limited and subsidiaries within the consolidated tax group. If a change in ownership (of greater than 49%) becomes probable, 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, assessments of economic useful life, previous Board impairment decisions and potential impacts from the active acquisition proposal. For further detail refer to Note 15.

**Reinsurance recovery receivables**

Valuation of reinsurance recovery receivables is an area of significant judgement and estimation. Key elements of judgement included within recovery estimations are: counterparty and credit risk; and risks around the arbitration process for the reinsurance contract in dispute. The nature of estimation uncertainties, including from those factors listed above, mean that actual reinsurance recoveries may differ from expected outcomes. Refer to Note 14 for further detail.

**Goodwill**

Goodwill is an area of significant judgement and estimation. Areas of judgement and subjectivity exist in the assessment of cash generating units and assumptions underlying goodwill impairment testing. Refer to Note 15 and Note 27 for further details of key assumptions used.

## 4 ACQUISITION PROPOSALS

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

On 27 June 2017, Tower Limited announced it had entered into a Scheme Implementation Arrangement (SIA) with Suncorp. Under this agreement, Suncorp agreed to acquire 100% of the Company's shares at $1.40 per share for an aggregate purchase price of $236 million. On 26 July 2017, the New Zealand Commerce Commission announced that it had declined Suncorp's application to purchase 100% of Tower shares.

On 23 August 2017, Suncorp advised that they would be appealing the Commerce Commission decision. On 5 September 2017 the Tower Board lodged its own cross appeal against the Commerce Commission's decision to decline Suncorp's application to acquire 100% of Tower.

On 7 November 2017, Tower advised that the SIA with Suncorp had passed its end date and had been terminated. Suncorp subsequently announced that as a result, it would no longer be proceeding with its appeal of the Commerce Commission's decision to decline its application to acquire Tower.

The Tower Board has withdrawn its cross appeal against the Commerce Commission's decision.

**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).

The Fairfax SIA was terminated on 29 June 2017 following Tower's announcement on 27 June 2017 that it had entered into a SIA with Suncorp. Tower has reimbursed $400,000 of Fairfax's costs under the conditions of its discontinued scheme. Under the Fairfax mutual termination agreement, a break fee of a further $1.57 million is payable to Fairfax if another party completes an acquisition of Tower by 31 August 2018. Refer to Note 34 Contingent Liabilities.

**Acquisition Proposal Expenses**

At 30 September 2017, Tower has provided for all costs incurred to that date in respect of the acquisition activity. These have been recorded in the Consolidated Income Statement as a separate line item (Acquisition proposal expenses).

*Adviser fees*

The Company has worked 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 30 September 2017 have been included in the Income Statement. Where no invoice has been received, an estimate of likely costs up to 30 September 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 and potential capital raising. Goldman advisory fees are linked to the outcome of any acquisition proposal and capital raising. In the event that an acquisition proposal or capital raising is completed, advisory fees estimated up to $4.5 million before tax will become payable to Goldman.

At 30 September 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 or completion of capital raising.

# NOTES TO THE FINANCIAL STATEMENTS

## 5 PREMIUM REVENUE

| $ thousands | Note | 2017 | 2016 |
|---|---|---|---|
| Gross written premiums | | **312,396** | 303,236 |
| Less: Gross unearned premiums | | **(5,636)** | (296) |
| **Premium revenue** | | **306,760** | 302,940 |

Premium revenue is recognised in the period in which the premiums are earned during the term of the contract. The proportion of premiums not earned in the income statement at reporting date is recognised in the balance sheet as unearned premiums.

Premiums on unclosed business are brought to account using estimates based on the previous year's actual unclosed business with due allowance made for any changes in the pattern of new business and renewals.

Premiums ceded to reinsurers under reinsurance contracts are recorded as outwards reinsurance expense and are recognised over the period of the reinsurance contract. Accordingly, a portion of outwards reinsurance premium is treated at balance date as a prepayment.

## 6 INVESTMENT REVENUE

| $ thousands | Note | 2017 | 2016 |
|---|---|---|---|
| **Fixed interest securities** | | | |
| Interest income | | **7,734** | 10,088 |
| Net realised gain (loss) | | **(631)** | 441 |
| Net unrealised gain (loss) | | **913** | (3,142) |
| **Total fixed interest securities** | | **8,016** | 7,387 |
| **Equity securities** | | | |
| Dividend income | | **-** | 9 |
| Net unrealised gain (loss) | | **(3)** | (163) |
| **Total equity securities** | | **(3)** | (154) |
| **Other** | | | |
| Net realised gain (loss) | | **(1,297)** | 2,810 |
| Net unrealised gain (loss) | | **927** | (1,045) |
| **Total other** | | **(370)** | 1,765 |
| Total investment revenue | | **7,734** | 10,097 |
| Total net realised gain (loss) | | **(1,928)** | 3,251 |
| Total net unrealised gain (loss) | | **1,837** | (4,350) |
| **Total investment revenue** | | **7,643** | 8,998 |

Investment revenue is recognised as follows:

*(i)* *Interest income on fixed interest securities*

Interest income is recognised using the effective interest method.

*(ii)* *Dividend income on equity securities*

Revenue is recognised on an accrual basis when the right to receive payment is established.

*(iii)* *Fair value gains and losses*

Fair value gains and losses on investments are recognised through the income statement in the period in which they arise. The gains and losses from fixed interest, equity and property securities have been generated by financial assets designated on initial recognition at fair value through profit or loss. Other investment gains and losses have been generated by derivative financial assets and financial liabilities classified as held for trading at fair value through profit or loss.

## 7 NET CLAIMS EXPENSE

| $ thousands | Note | 2017 | 2016 |
|---|---|---|---|
| Canterbury earthquake claims (4 key events) | 8 | **15,916** | 35,084 |
| Additional risk margin | 8 | **10,000** | - |
| Kaikoura earthquake claims | | **5,739** | - |
| Other claims | | **155,896** | 150,528 |
| **Total net claims expense** | | **187,551** | 185,612 |

Claims expense is recognised when claims are notified. Provision is made at the end of the year for the estimated cost of claims incurred but not settled at balance date, including the cost of claims incurred but not yet reported to the Group.

The estimated cost of claims includes direct expenses incurred in settling claims net of any expected salvage value and other recoveries. The Group takes all reasonable steps to ensure that it has appropriate information regarding its claims exposures. However, given the uncertainty in establishing claims provisions, it is likely that the final outcome will prove to be different from the original liability established.

The estimation of claims incurred but not reported (IBNR) is generally subject to a greater degree of uncertainty than the estimation of the cost of settling claims already notified to the Group, where more information about the claim event is generally available. IBNR claims may often not be apparent to the insured until many years after the events giving rise to the claims have happened. In calculating the estimated cost of unpaid claims the Group uses a variety of estimation techniques, generally based on statistical analyses of historical experience, which assumes that the development pattern of current claims will be consistent with past experience. Allowance is made for changes or uncertainties which may create distortions in underlying statistics or which may cause the cost of unsettled claims to increase or reduce when compared with the cost of previously settled claims including:

- changes in Group processes which might accelerate or slow down the development and (or) recording of paid or incurred claims, compared with statistics from previous periods;
- the effects of inflation; and
- the impact of large losses.

A component of these estimation techniques is usually the estimation of the cost of notified but not paid claims. In estimating the cost of these, the Group has regard to the claim circumstances reported, any information available from loss adjusters and information on the cost of settling claims with similar characteristics in previous periods.

Provisions are calculated gross of any reinsurance recoveries except risk margin, which is net of reinsurance recoveries. A separate estimate is made of the amounts that will be recoverable from reinsurers based on the gross provisions. Details of specific assumptions used in deriving the outstanding claims liability at year end are detailed in Note 27.

Reinsurance recoveries are recognised as revenue. Amounts recoverable are assessed in accordance with the terms of the reinsurance contracts in a manner similar to the assessment of outstanding claims. Recoveries are measured as the present value of expected future receipts.

## 8 CANTERBURY EARTHQUAKES

Tower has received over 16,106 individual claims from customers as a result of earthquakes impacting the Canterbury region during 2010 and 2011 (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 15,783 claims at 30 September 2017 (2016: 15,426 claims), representing a 98% settlement rate by number of claims and 93% by value (2016: 96% by number and 89% by value). To date, Tower has paid out more than $825 million to customers (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 30 September 2017, Tower has estimated gross ultimate incurred claims of $897.4 million in respect of the four main Canterbury earthquake events (2016: $869.6 million).

Outstanding claims comprises case estimates, claims incurred but not reported (IBNR) and risk margins. In the year ended 30 September 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 over-cap claims being received from EQC; and the Appointed Actuary increasing IBNR and risk margins, particularly in respect of litigated claims and additional EQC recoveries.

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 completes 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 14.

The table below presents a financial representation of Tower's net outstanding claims provision at 30 September 2017 in relation to the four main earthquake events.

**Canterbury earthquake provisions**

| $ thousands | **2017** | 2016 |
|---|---|---|
| **Insurance liabilities** | | |
| Gross outstanding claims | **(107,200)** | (149,100) |
| Additional risk margin | **(10,000)** | - |
| | **(117,200)** | (149,100) |
| **Receivables** | | |
| Reinsurance recovery receivables | **13,600** | 50,800 |
| EQC related to open claims | **5,800** | 57,600 |
| Less: EQC payable to reinsurers | **(1,700)** | - |
| | **17,700** | 108,400 |
| **Net outstanding claims** | **(99,500)** | (40,700) |

**Change in presentation of comparative insurance liabilities and receivables**

The 2016 comparative information in the table above includes receivables from Peak Re and EQC as deductions from gross outstanding claims relating to both open and closed claims. As the gross outstanding claims liability continues to reduce, only EQC recoveries for open claims have been deducted from gross outstanding claims liability for the September 2010 and February 2011 events. For the other earthquakes, EQC recoveries for open claims and reinsurance recoveries are deducted. Due to the nature of EQC recoveries, the categorisation between open claims and closed claims is an approximation that takes into account the split between open and closed claims for EQC recoveries already received as well as EQC recoveries expected to be received.

# NOTES TO THE FINANCIAL STATEMENTS

## 8 CANTERBURY EARTHQUAKES (continued)

Tower has two significant receivable amounts related to closed Canterbury earthquake claims, being $43.75 million from Peak Re and $65.1 million from EQC (2016: $57.6 million). $17.7 million of this EQC amount is payable to reinsurers which has been allowed for (2016: $20.7 million). A risk margin of $10.7 million has been allowed for on the receivable from EQC (2016: $4.3 million).

Recognising the challenging history of Canterbury earthquake claims and the potential for ongoing complexity in finalising remaining claims and potential new over-cap claims, the Board has elected to create an additional risk margin of $10.0 million over and above the provision of the Appointed Actuary, which is set at the 75th percentile probability of sufficiency.

This additional risk margin approximates the 80-85th percentile probability of sufficiency of the Appointed Actuary's central estimate as at 30 September 2017. This provision will remain at $10.0 million, subject to review by the Board each half year and will be released once Canterbury Outstanding Claims Liability has sufficiently run off.

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

| $ thousands | **2017** | 2016 |
|---|---|---|
| **Cumulative expenses associated with Canterbury earthquakes:** | | |
| Earthquake claims estimate | **(897,440)** | (869,600) |
| Reinsurance recoveries | **746,623** | 734,699 |
| Claim expense net of reinsurance recoveries | **(150,817)** | (134,901) |
| Reinsurance expense | **(25,045)** | (25,045) |
| Additional risk margin | **(10,000)** | - |
| Cumulative impact of Canterbury earthquakes before tax | **(185,862)** | (159,946) |
| Income tax | **52,710** | 45,454 |
| **Cumulative impact of Canterbury earthquakes after tax** | **(133,152)** | (114,492) |
| **Recognised in current period (net of tax)** | **(18,660)** | (25,272) |

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 has 323 open claims at 30 September 2017 (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.

### 8 CANTERBURY EARTHQUAKES (continued)

The actuarial reviews performed during the year ended 30 September 2017 identified the following as key contributors to the increase in expected earthquake claims costs:

- Continued growth in the level of litigation claims received;
- Continued development of claim costs as they progress through the claims life cycle;
- Greater than anticipated new over-cap claims received from EQC;
- Increase in the level of future claims handling expenses; and
- Refinement of actuarial assumptions, including the setting of risk margins.

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 litigated claims received and the average cost of these claims
- the number of new claims expected from EQC and the average cost of these claims
- the rate of closed claims reopening
- 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.

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 30 September 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 $507.0 million including risk margin. Tower has reinsurance for $375.4 million on this event including catastrophe cover, proportional reinsurance and adverse development cover. During the year ended 30 September 2017, Tower expensed $13.3 million in relation to the February 2011 event (2016: $35.1 million).

Tower has also exceeded its catastrophe reinsurance cover limit in relation to the September 2010 event. The estimated ultimate incurred claims cost of the September 2010 event totals $303.4 million including risk margin. Tower has reinsurance for $295.8 million on this event including catastrophe cover and proportional reinsurance cover. During the year ended 30 September 2017, Tower expensed $2.6 million in relation to the September 2010 event (2016: nil).

The catastrophe reinsurance cover headroom remaining is included in the table below.

| **Date of event** | **Catastrophe reinsurance cover remaining** | |
|---|---|---|
| $ thousands | **2017** | 2016 |
| September 2010 | **-** | 7,700 |
| February 2011 | **-** | - |
| June 2011 | **254,200** | 256,500 |
| December 2011 | **486,500** | 487,500 |

# NOTES TO THE FINANCIAL STATEMENTS

## 8 CANTERBURY EARTHQUAKES (continued)

**Sensitivity analysis - impact of changes in key variables**

Net outstanding claims are comprised of several key elements, as described 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.

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

| $ millions | Change variable | Split between events | | | | Four main earthquakes | |
|---|---|---|---|---|---|---|---|
| | | **Sep 2010** | **Feb 2011** | **Jun 2011** | **Dec 2011** | **30-Sep-17** | 30-Sep-16 |
| <u>Outstanding claims:</u> | | | | | | | |
| (i) Change to costs and quantity of expected claim estimates including building costs and other impacts. | + 5% | **(1.3)** | **(3.0)** | **-** | **-** | **(4.3)** | (4.1) |
| | - 5% | **1.3** | **3.0** | **-** | **-** | **4.3** | 4.1 |
| (ii) Change in apportionment of claim costs to / from February 2011 event. | + 1% | **4.9** | **(9.0)** | **-** | **-** | **(4.1)** | (9.0) |
| | - 1% | **(7.0)** | **9.0** | **-** | **-** | **2.0** | 9.0 |
| <u>Receivables:</u> | | | | | | | |
| *Reinsurance recovery receivables* | | | | | | | |
| (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% | **0.1** | **0.7** | **-** | **-** | **0.8** | 0.7 |
| | - 10% | **(0.1)** | **(0.7)** | **-** | **-** | **(0.8)** | (0.8) |
| (v) Recoveries from EQC in respect of building costs | + 10% | **3.2** | **0.9** | **-** | **-** | **4.1** | 0.1 |
| | - 10% | **(3.2)** | **(0.9)** | **-** | **-** | **(4.1)** | (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 over-cap 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 FINANCIAL STATEMENTS

## 9 MANAGEMENT AND SALES EXPENSES

**Included in total management and sales expenses are the following requiring separate disclosures:**

| $ thousands | Note | **2017** | 2016 |
|---|---|---|---|
| Amortisation of deferred acquisition costs | | **19,973** | 20,277 |
| Bad debts written off | | **176** | 162 |
| Change in provision for doubtful debts | | **(945)** | (307) |
| Amortisation of software | | **6,395** | 3,950 |
| Depreciation | | **2,032** | 2,438 |
| Office equipment and furniture | | **928** | 840 |
| Motor vehicles | | **93** | 170 |
| Computer equipment | | **1,011** | 1,428 |
| Directors' fees | | **509** | 565 |
| Employee benefits expense | | **53,600** | 54,396 |
| (Gain) on disposal of property, plant and equipment | | **(42)** | (43) |
| Claims related management expenses reclassified to claims expense | | **(25,998)** | (22,846) |

| | | |
|---|---|---|
| **Auditors remuneration** | | |
| **Fees paid to Group's auditors:** | | |
| Audit of financial statements [1] | **495** | 364 |
| Other assurance related services [2] | **30** | 30 |
| Non-assurance advisory related services [3] | **6** | 149 |
| **Total fees paid to Group's auditors** | **531** | 543 |
| **Fees paid to subsidiaries' auditors different to Group auditors:** | | |
| Audit of financial statements [4] | **45** | 51 |
| **Total fees paid to auditors** | **576** | 594 |

(1) Audit of financial statements includes fees for both the audit of annual financial statements and the review of interim financial statements.

(2) Other assurance related services includes annual solvency return assurance and Pacific Island regulatory return audits.

(3) Non-assurance advisory related services related to Annual Shareholders' Meeting procedures and IT Platform review (in 2016).

(4) Tower Insurance Limited paid all fees for audit services provided to the Group, other than the audit fees of National Pacific Insurance Limited and Tower Insurance (Vanuatu) Limited.

# NOTES TO THE FINANCIAL STATEMENTS

## 10 TAX

The Group is subject to income taxes in New Zealand and jurisdictions where it has foreign operations. Significant management judgement is required in determining the worldwide provision for income taxes. There are some transactions and calculations undertaken during the ordinary course of business for which the ultimate tax determination is uncertain. The Group estimates its tax liabilities based on its understanding of tax law in each relevant jurisdiction. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the current and deferred income tax assets and liabilities in the period in which such determination is made. Deferred tax assets are recognised for all unused tax losses to the extent it is probable that taxable profits will be available against which the losses can be utilised. Significant management judgement is required to determine the amount of deferred tax assets that can be recognised based on the likely timing and quantum of future taxable profits.

### 10A TAX EXPENSE

**Analysis of tax expense**

| $ thousands | Note | **2017** | 2016 |
|---|---|---|---|
| Current tax | | **4,468** | 6,026 |
| Deferred tax | | **(3,064)** | (10,615) |
| Under (over) provided in prior years | | **597** | (322) |
| **Total tax expense (benefit)** | | **2,001** | (4,911) |

The tax benefit can be reconciled to the accounting profit as follows:

| | | |
|---|---|---|
| **Loss before tax from continuing operations** | **(5,999)** | (26,426) |
| Income tax at the current rate of 28% | **(1,680)** | (7,399) |
| *Tax effect of:* | | |
| Prior period adjustments | **597** | (322) |
| Non-deductible expenditure/non-assessable income | **967** | 216 |
| Foreign tax credits written off | **1,874** | 2,226 |
| Non-taxable dividend from subsidiaries | **-** | - |
| Other | **243** | 368 |
| **Total tax expense (benefit)** | **2,001** | (4,911) |

*(i) Current tax*

Current tax is the amount of income taxes payable or recoverable in respect of the taxable profit or loss for the period. It is calculated using tax rates and laws that have been enacted or substantively enacted by the reporting date. Current tax for current and prior periods is recognised as a liability (or asset) to the extent that it is unpaid (or refundable).

*(ii) Tax consolidation*

Tower Limited and its subsidiaries are part of a single consolidated group for tax purposes, with the exception of Tower Insurance Limited.

*(iii) Income tax expense*

The income tax expense is the tax payable on taxable income for the current period, based on the income tax rate for each jurisdiction and adjusted for changes in deferred tax assets and liabilities attributable to temporary differences and unused tax losses.

*(iv) GST*

All revenues, expenses and certain assets are recognised net of goods and services taxes (GST) except where the GST is not recoverable. In these circumstances the GST is included in the related asset or expense. Receivables and payables are reported inclusive of GST. The net GST payable to or recoverable from the tax authorities as at balance date is included as a receivable or payable in the balance sheet.

# NOTES TO THE FINANCIAL STATEMENTS

## 10 TAX (continued)

*(v) Tax cash flows*

Tax cash flows are included in the statements of cash flows on a net basis other than to the extent that the GST is not recoverable and has been included in the expense or asset.

### 10B CURRENT TAX ASSETS

**Analysis of current tax assets**

| $ thousands | Note | 2017 | 2016 |
|---|---|---|---|
| Current | | **1,206** | 912 |
| Non-current | | **12,256** | 12,256 |
| **Total current tax assets** | | **13,462** | 13,168 |

A non-current tax asset of $12,256,000 is recognised in the financial statements of the Group as at 30 September 2017 in relation to excess tax payments made in previous years (2016: $12,256,000). Non-current tax assets are expected to be recovered from 2021, as determined by the Board approved operational plan for financial years 2018 to 2021. A current tax asset of $1,206,000 is recognised in relation to excess tax payments made in the Pacific Islands over and above the estimated tax liabilities for the year (2016: $595,000).

### 10C CURRENT TAX LIABILITIES

Current tax liabilities of $560,000 relate to taxes payable to off shore tax authorities in the Pacific Islands (2016: $123,000).

### 10D DEFERRED TAX ASSETS AND LIABILITIES

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

| $ thousands | Opening balance at 1 October | (Charged) credited to income statement | (Charged) credited to comprehensive income | Closing balance at 30 September |
|---|---|---|---|---|
| **For the Year Ended 30 September 2017** | | | | |
| **Movement in deferred tax assets** | | | | |
| Provisions and accruals | **3,141** | **(876)** | **-** | **2,265** |
| Property, plant and equipment | **3,288** | **4,493** | **-** | **7,781** |
| Tax losses | **29,086** | **(2,128)** | **-** | **26,958** |
| Other | **-** | **778** | **-** | **778** |
| **Total deferred tax assets** | **35,515** | **2,267** | **-** | **37,782** |
| Set-off of deferred tax liabilities pursuant to NZ IAS 12 | | | | **(5,037)** |
| **Net deferred tax assets** | | | | **32,745** |
| **Movement in deferred tax liabilities** | | | | |
| Deferred acquisition costs | **(4,851)** | **(227)** | **-** | **(5,078)** |
| Other | **(1,294)** | **1,024** | **(29)** | **(299)** |
| **Total deferred tax liabilities** | **(6,145)** | **797** | **(29)** | **(5,377)** |
| Set-off of deferred tax liabilities pursuant to NZ IAS 12 | | | | **5,037** |
| **Net deferred tax liabilities** | | | | **(340)** |

## 10 TAX (continued)

| $ thousands | Opening balance at 1 October | (Charged) credited to income statement | (Charged) credited to comprehensive income | Closing balance at 30 September |
|---|---|---|---|---|
| For the Year Ended 30 September 2016 | | | | |
| **Movement in deferred tax assets** | | | | |
| 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 |
| **Total deferred tax assets** | 24,786 | 10,752 | (23) | 35,515 |
| Set-off of deferred tax liabilities pursuant to NZ IAS 12 | | | | (5,360) |
| **Net deferred tax assets** | | | | 30,155 |
| **Movement in deferred tax liabilities** | | | | |
| Deferred acquisition costs | (4,885) | 34 | - | (4,851) |
| Other | (1,123) | (171) | - | (1,294) |
| **Total deferred tax liabilities** | (6,008) | (137) | - | (6,145) |
| Set-off of deferred tax liabilities pursuant to NZ IAS 12 | | | | 5,360 |
| **Net deferred tax liabilities** | | | | (785) |

**Deferred tax**

Deferred tax is accounted for using the comprehensive balance sheet liability method in respect of temporary differences arising from differences between the carrying amount of assets and liabilities in the financial statements and the corresponding tax base of those items.

Deferred tax assets and liabilities are recognised for temporary differences at the tax rates expected to apply when the assets are recovered or liabilities settled, based on the tax rates enacted or substantively enacted for each jurisdiction. Deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences or unused tax losses can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of the other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

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

Recognition of deferred tax assets is a key area of judgement. Management expects to utilise the tax losses against future profits over the next 4 years.

Deferred tax liabilities of $946,000 have not been recognised in respect of temporary differences associated with investments in subsidiaries (2016: liabilities of $166,000).

### 10E IMPUTATION CREDITS

The Group imputation credit account reflects the imputation credits held by the Company as the representative member of the Group.

| $ thousands | **2017** | 2016 |
|---|---|---|
| Imputation credits available for use in subsequent reporting periods | **489** | 489 |

The balance of the imputation account at the end of the year is determined having adjusted for imputation credits that will arise from the payment of income tax provided; dividends recognised as a liability; and the receipt of dividends recognised as receivables at the reporting date.

# NOTES TO THE FINANCIAL STATEMENTS

## 11 SEGMENTAL REPORTING

| $ thousands | New Zealand | Pacific Islands | Other (Holding companies & eliminations) | Total |
|---|---|---|---|---|
| **Year Ended 30 September 2017** | | | | |
| **Revenue** | | | | |
| Net operating revenue | **222,117** | **44,816** | **665** | **267,598** |
| **Total revenue** | **222,117** | **44,816** | **665** | **267,598** |
| **Earnings before interest, tax, depreciation and amortisation** | **(15,648)** | **12,688** | **6,223** | **3,263** |
| Interest expense | **-** | **-** | **(835)** | **(835)** |
| Depreciation and amortisation | **(1,529)** | **(521)** | **(6,377)** | **(8,427)** |
| **Profit (Loss) before income tax** | **(17,177)** | **12,167** | **(989)** | **(5,999)** |
| Income tax credit (expense) | **2,470** | **(4,958)** | **487** | **(2,001)** |
| **Profit (Loss) for the year** | **(14,707)** | **7,209** | **(502)** | **(8,000)** |
| Total assets 30 September 2017 | **481,532** | **82,664** | **75,270** | **639,466** |
| Total liabilities 30 September 2017 | **335,602** | **54,483** | **33,637** | **423,722** |
| Acquisition of property plant and equipment and intangibles | **819** | **295** | **12,059** | **13,173** |
| **Year Ended 30 September 2016** | | | | |
| **Revenue** | | | | |
| Net operating revenue | 218,992 | 45,765 | 1,488 | 266,245 |
| **Total revenue** | 218,992 | 45,765 | 1,488 | 266,245 |
| **Earnings before interest, tax, depreciation and amortisation** | (12,577) | 9,617 | (17,078) | (20,038) |
| Depreciation and amortisation | (2,076) | (379) | (3,933) | (6,388) |
| **Profit (Loss) before income tax** | (14,653) | 9,238 | (21,011) | (26,426) |
| Income tax credit (expense) | 2,760 | (3,729) | 5,880 | 4,911 |
| **Profit (Loss) for the year** | (11,893) | 5,509 | (15,131) | (21,515) |
| Total assets 30 September 2016 | 479,420 | 79,104 | 81,757 | 640,281 |
| Total liabilities 30 September 2016 | 360,613 | 51,981 | 3,735 | 416,329 |
| Acquisition of property plant and equipment and intangibles | 481 | 1,523 | 7,553 | 9,557 |

**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.

Tower Group operates predominantly in two geographical segments, New Zealand and the Pacific region.

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

The Group does not derive revenue from any individual or entity that represents 10% or more of the Group's total revenue.

## 12 CASH AND CASH EQUIVALENTS

| $ thousands | 2017 | 2016 |
|---|---|---|
| Cash at bank and in hand | **21,981** | 25,792 |
| Deposits at call | **76,689** | 60,932 |
| Restricted cash | **4,206** | 5,504 |
| **Total cash and cash equivalents** | **102,876** | 92,228 |

Cash and cash equivalents includes cash on hand and deposits held at call with financial institutions, other short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value, and bank overdrafts.

The effective interest rate at 30 September 2017 for deposits at call is 2.60% (2016: 2.60%). There was no offsetting within cash and cash equivalents (2016: nil).

Tower is a party to the Canterbury Earthquake Shared Property Process – Insurer Contract (SPP) which sets out obligations for insurers and appoints a lead insurer to act on behalf of other insurers with respect to the repair and rebuild of shared properties (known as multi-units). As lead insurer on Canterbury multi-unit repairs or rebuilds, Tower receives cash from other insurance companies as settlement of their obligations under building contracts covered within the SPP. Tower separately holds this cash on behalf of other insurers in a segregated bank account.

At 30 September, Tower was holding $4.2 million (2016: $5.5 million) cash in respect of multi-unit claims as lead insurer on Canterbury claims. This is recognised within Cash and cash equivalents on the balance sheet. Related to this are corresponding amounts being $1.6 million (2016: $2.7 million) recorded within Insurance liabilities for Tower's portion of multi-unit outstanding claims; and $2.6 million (2016: $2.8 million) recorded within Payables as held on behalf of other insurers in respect of SPP claims.

## 13 RECONCILIATION OF LOSS FOR THE PERIOD TO NET CASH FLOWS FROM OPERATING ACTIVITIES

| $ thousands | 2017 | 2016 |
|---|---|---|
| **Loss for the year** | **(8,000)** | (21,515) |
| **Add (less) non-cash items** | | |
| Depreciation of property, plant and equipment | **2,032** | 2,438 |
| Amortisation of software | **6,395** | 3,950 |
| Impairment of software | **-** | 19,649 |
| Unrealised (gain) loss on financial assets | **(1,837)** | 4,350 |
| Movement on disposal of property, plant and equipment | **(42)** | (43) |
| Change in deferred tax | **(3,024)** | (10,560) |
| | **3,524** | 19,784 |
| **Add (less) movements in working capital (excluding the effects of exchange differences on consolidation)** | | |
| Change in receivables | **(7,653)** | 1,984 |
| Change in payables | **(21,537)** | (11,614) |
| Change in taxation | **116** | 1,051 |
| | **(29,074)** | (8,579) |
| **Add (less) other items classified as investing / financing activities** | | |
| Financing costs | **778** | - |
| | **778** | - |
| **Net cash inflows (outflows) from operating activities** | **(32,772)** | (10,310) |

# NOTES TO THE FINANCIAL STATEMENTS

## 14 RECEIVABLES

| $ thousands | 2017 | 2016 |
|---|---|---|
| Reinsurance recovery receivables | **63,947** | 68,406 |
| Outstanding premiums and trade receivables | **127,319** | 125,855 |
| Other | **70,109** | 60,424 |
| **Total receivables** | **261,375** | 254,685 |
| **Analysed as** | | |
| Current | **192,466** | 173,613 |
| Non current | **68,909** | 81,072 |
| **Total receivables** | **261,375** | 254,685 |

Outstanding premiums and trade receivables are presented net of allowance for credit losses and impairment. The tables below include reconciliations of outstanding premiums and trade receivables, together with the provision for cancellation at the reporting date.

| | | |
|---|---|---|
| Outstanding premiums and trade receivables | **128,124** | 127,605 |
| Allowance for credit losses and impairment | **(805)** | (1,750) |
| | **127,319** | 125,855 |

| | | |
|---|---|---|
| **Opening balance** | **(1,750)** | (2,057) |
| Provisions added during the year | **(41)** | (45) |
| Provisions released during the year | **978** | 224 |
| Foreign exchange movements | **8** | 128 |
| **Closing balance** | **(805)** | (1,750) |

Trade and other receivables are recognised initially at fair value and subsequently measured at amortised cost, less provision for impairment.

Collectability of trade receivables is reviewed on an on-going basis. The allowance for credit losses and impairment in relation to trade receivables is provided for based on estimated recoverable amounts determined by reference to current customer circumstances and past default experience. In determining the recoverability of a trade receivable the Group considers any change in the credit quality of the trade receivable from the date the credit was initially granted up to the reporting date. The Group has provided fully for receivables over 120 days past due. Trade receivables between 60 and 120 days past due are provided for based on estimated irrecoverable amounts.

Trade and other receivables, including EQC reinsurance recoveries, are included in current assets except for those with maturities greater than 12 months after the reporting date, which are classified as non-current assets.

**Assets arising from reinsurance contracts**

Assets arising from reinsurance contracts are also determined using the above methods. In addition, the recoverability of these assets is assessed on a periodic basis to ensure that the balance is reflective of the amounts that will ultimately be received, taking into consideration factors such as counterparty and credit risk. Impairment is recognised where there is objective evidence that the Group may not receive amounts due to it and these amounts can be reliably measured.

# NOTES TO THE FINANCIAL STATEMENTS

## 14 RECEIVABLES (continued)

**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 act as agents for the Crown agency in relation to the Kaikoura region earthquake. Under the agreement, Tower directly lodges, assesses and settles 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. At 30 September 2017, the amount due from EQC for reimbursement of claims handling expenses and claims paid in relation to the Kaikoura event is $1.3 million (2016: nil).

*Canterbury Earthquakes*

Other receivables include an amount of $65.1 million due from EQC for land damage and building costs relating to the Canterbury earthquake provisions as disclosed in Note 8.

Tower estimates the gross amount receivable due from EQC is significantly higher than the $65.1 million, but has adopted this amount, which is the actuarial valuation of the Appointed Actuary. The method by which the actuarial valuation is completed recognises the inherent risk and uncertainty with recovery of the full gross amount. An amount of $17.7 million (2016: $20.7 million) will be payable to reinsurers on receipt from EQC of these balances. The amount payable to reinsurers may vary depending on the balance collected from EQC.

Tower acknowledges that the EQC recoveries relating to Canterbury earthquakes are an area of significant accounting estimation and judgement, including earthquake event allocation, litigation risk factors and other actuarial assumptions discussed in Note 8.

**Reinsurance Contract in Dispute**

Tower is party to an arbitration process with Peak Re regarding an Adverse Development Cover (ADC) policy entered into in 2015 with the recovery valued at $43.75 million. Currently Tower anticipates the arbitration will take place in March 2018 with a decision by mid-2018. Tower remains confident that it will be successful but both the process and the hearing hold risk and collection of the owed amount is not certain. An adverse outcome could lead to a nil recovery due to the binary nature of the process.

The ADC provides for recovery of claims cost 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 8).

# NOTES TO THE FINANCIAL STATEMENTS

## 15 INTANGIBLE ASSETS

| | | Software | | | |
|---|---|---|---|---|---|
| $ thousands | Goodwill | Acquired | Internally developed | Under development | Total |
| **Year Ended 30 September 2017** | | | | | |
| **Cost:** | | | | | |
| Opening balance | **17,744** | **5,020** | **31,305** | **4,554** | **58,623** |
| Additions | **-** | **82** | **5,740** | **6,237** | **12,059** |
| Disposals | **-** | **(6)** | **-** | **(17)** | **(23)** |
| Transfers | **-** | **-** | **-** | **(5,822)** | **(5,822)** |
| Foreign exchange movements | **-** | **1** | **-** | **-** | **1** |
| Transfers to Property, plant and equipment | **-** | **-** | **-** | **(468)** | **(468)** |
| **Closing balance** | **17,744** | **5,097** | **37,045** | **4,484** | **64,370** |
| **Accumulated amortisation:** | | | | | |
| Opening balance | **-** | **(4,265)** | **(22,376)** | **-** | **(26,641)** |
| Amortisation charge | **-** | **(235)** | **(6,160)** | **-** | **(6,395)** |
| Foreign exchange movements | **-** | **(1)** | **1** | **-** | **-** |
| **Closing balance** | **-** | **(4,501)** | **(28,535)** | **-** | **(33,036)** |
| **Net book value** | | | | | |
| At cost | **17,744** | **5,097** | **37,045** | **4,484** | **64,370** |
| Accumulated amortisation | **-** | **(4,501)** | **(28,535)** | **-** | **(33,036)** |
| **Closing net book value** | **17,744** | **596** | **8,510** | **4,484** | **31,334** |
| Year Ended 30 September 2016 | | | | | |
| **Cost:** | | | | | |
| 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) |
| Transfers to Property, plant and equipment | - | - | - | (702) | (702) |
| Foreign exchange movements | - | (10) | - | - | (10) |
| Impairment expense | - | - | (3,895) | (15,754) | (19,649) |
| **Closing balance** | 17,744 | 5,020 | 31,305 | 4,554 | 58,623 |
| **Accumulated amortisation:** | | | | | |
| 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 |
| **Closing balance** | - | (4,265) | (22,376) | - | (26,641) |
| **Net book value** | | | | | |
| At cost | 17,744 | 5,020 | 31,305 | 4,554 | 58,623 |
| Accumulated amortisation | - | (4,265) | (22,376) | - | (26,641) |
| **Closing net book value** | 17,744 | 755 | 8,929 | 4,554 | 31,982 |

## 15 INTANGIBLE ASSETS (continued)

### SOFTWARE

Application software is recorded at cost less accumulated amortisation and impairment. Amortisation is charged on a straight line basis over the estimated useful life of the software.

Internally generated intangible assets are recorded at cost which includes all the directly attributable costs necessary to create, produce and prepare the asset capable of operating in the manner intended by management. Amortisation of internally generated intangible assets begins when the asset is available for use and is amortised on a straight line basis over the estimated useful life.

| | |
|---|---|
| General use computer software | 3-5 years |
| Core operating system software | 3-10 years |

The determination of estimated useful economic life is a key area of judgement.

### IMPAIRMENT OF SOFTWARE

The Group has reviewed the carrying value of software intangible assets (both internally developed and under development) for indicators of impairment as at 30 September 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.

The review was undertaken in light of expectations for future technology platforms required to support growth in the New Zealand and Pacific insurance businesses. The Directors concluded that no impairment of software intangible assets was required as at 30 September 2017.

An impairment charge of $19.65 million was recorded at 31 March 2016, and was recognised in the 30 September 2016 financial statements relating to Internally developed software and Software under development categories.

Following the impairment review in 2016, the Group reduced the estimated useful economic life and amortisation period of the core operating system software to 3 years from 1 April 2016. This increased the annual amortisation by $844,000.

### GOODWILL

Goodwill acquired in a business combination is initially measured at cost being the excess of the cost of the business combination over the Group's interest in the fair value of the identifiable assets, liabilities and contingent liabilities of the entity acquired, at the date of acquisition. Following initial recognition, goodwill on acquisition of a business combination is not amortised but is tested for impairment bi-annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired.

For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group’s cash generating units, or groups of cash generating units, that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units or groups of units.

Any impairment is recognised immediately in the income statement.

On disposal of an entity the carrying value of any associated goodwill is included in the calculation of the gain or loss on sale.

### IMPAIRMENT TESTING FOR GOODWILL

Goodwill is allocated to the New Zealand general insurance cash generating unit. The carrying amount of goodwill allocated to the cash generating unit is shown below:

| $ thousands | **2017** | 2016 |
|---|---|---|
| Carrying amount of goodwill | **17,744** | 17,744 |

Impairment of goodwill is a key area of judgement.

Goodwill is subject to impairment testing at the cash-generating unit level every six months. No impairment loss has been recognised in 2017 as a result of the impairment review (2016: Nil).

## 15 INTANGIBLE ASSETS (continued)

### IMPAIRMENT REVIEW METHOD

The recoverable amount of the general insurance business has been assessed with reference to its appraisal value to determine its value in use. A base discount rate of 14% was used in the calculation (2016: 14%). Other assumptions used are consistent with the actuarial assumptions in Note 27 in respect of Tower Insurance. The cash flows were projected over the expected life of the policies. The projected cash flows are determined based on past performance and management's expectations for market developments with a terminal growth rate of 2% (2016: 2%).

### SENSITIVITY TO CHANGES IN ASSUMPTIONS

Management considers that the recoverable amount from the general insurance business, as determined by the appraisal value, will exceed the carrying value under a reasonable range of adverse scenarios.

## 16 DEFERRED ACQUISITION COSTS

| $ thousands | Note | **2017** | 2016 |
|---|---|---|---|
| Balance at the beginning of year | | **19,973** | 20,277 |
| Acquisition costs during the year | | **20,961** | 19,973 |
| Current period amortisation | | **(19,973)** | (20,277) |
| **Total deferred acquisition costs** | | **20,961** | 19,973 |
| | | | |
| **Analysed as:** | | | |
| Current | | **20,961** | 19,973 |
| Non-current | | **-** | - |
| **Total deferred acquisition costs** | | **20,961** | 19,973 |

Acquisition costs incurred in obtaining general insurance contracts are deferred and recognised as assets where they can be reliably measured and where it is probable that they will give rise to premium revenue that will be recognised in subsequent reporting periods.

Deferred acquisition costs are amortised systematically in accordance with the expected pattern of the incidence of risk under the general insurance contracts to which they relate. This pattern of amortisation corresponds to the earning pattern of the corresponding premium revenue.

## NOTES TO THE FINANCIAL STATEMENTS

### 17 PROPERTY, PLANT AND EQUIPMENT

| $ thousands | Land and buildings | Office equipment and furniture | Motor vehicles | Computer equipment | Total |
|---|---|---|---|---|---|
| **For the Year Ended 30 September 2017** | | | | | |
| **Cost** | | | | | |
| Opening balance | **2,710** | **7,481** | **1,277** | **14,038** | **25,506** |
| Additions | **-** | **291** | **69** | **754** | **1,114** |
| Revaluations | **247** | **-** | **-** | **-** | **247** |
| Disposals | **(27)** | **(74)** | **(231)** | **(19)** | **(351)** |
| Foreign exchange movements | **29** | **17** | **7** | **(9)** | **44** |
| **Closing balance** | **2,959** | **7,715** | **1,122** | **14,764** | **26,560** |
| **Accumulated depreciation** | | | | | |
| Opening balance | **-** | **(2,004)** | **(930)** | **(13,061)** | **(15,995)** |
| Depreciation | **-** | **(928)** | **(93)** | **(1,011)** | **(2,032)** |
| Disposals | **-** | **57** | **188** | **16** | **261** |
| Foreign exchange movements | **-** | **(5)** | **(2)** | **(7)** | **(14)** |
| **Closing balance** | **-** | **(2,880)** | **(837)** | **(14,063)** | **(17,780)** |
| **Closing balance** | | | | | |
| Cost / revaluation | **2,959** | **7,715** | **1,122** | **14,764** | **26,560** |
| Accumulated depreciation | **-** | **(2,880)** | **(837)** | **(14,063)** | **(17,780)** |
| **Net book value** | **2,959** | **4,835** | **285** | **701** | **8,780** |
| For the Year Ended 30 September 2016 | | | | | |
| **Cost** | | | | | |
| Opening balance | 2,754 | 6,749 | 1,396 | 13,597 | 24,496 |
| Additions | - | 1,182 | 203 | 619 | 2,004 |
| Revaluations | 181 | - | - | - | 181 |
| Disposals | - | (85) | (122) | (33) | (240) |
| Foreign exchange movements | (225) | (365) | (200) | (145) | (935) |
| **Closing balance** | 2,710 | 7,481 | 1,277 | 14,038 | 25,506 |
| **Accumulated depreciation** | | | | | |
| Opening balance | - | (1,513) | (1,022) | (11,740) | (14,275) |
| Depreciation | - | (840) | (170) | (1,428) | (2,438) |
| Disposals | - | 82 | 124 | 7 | 213 |
| Foreign exchange movements | - | 267 | 138 | 100 | 505 |
| **Closing balance** | - | (2,004) | (930) | (13,061) | (15,995) |
| **Closing balance** | | | | | |
| Cost / revaluation | 2,710 | 7,481 | 1,277 | 14,038 | 25,506 |
| Accumulated depreciation | - | (2,004) | (930) | (13,061) | (15,995) |
| **Net book value** | 2,710 | 5,477 | 347 | 977 | 9,511 |

# NOTES TO THE FINANCIAL STATEMENTS

## 17 PROPERTY, PLANT AND EQUIPMENT (continued)

**Property, plant and equipment**

Property, plant and equipment is initially recorded at cost including transaction costs and subsequently measured at cost less any accumulated depreciation and impairment losses.

**Land and buildings**

Land and buildings are shown at fair value, based on periodic valuations by external independent appraisers less subsequent depreciation for buildings. Any accumulated depreciation at the date of revaluation is eliminated against the gross carrying amount of the asset and the net amount is restated to the revalued amount of the asset.

**Depreciation**

Depreciation is calculated using the straight line method to allocate the assets' cost or revalued amounts, net of any residual amounts, over their useful lives. The assets' useful lives are reviewed and adjusted if appropriate at each balance date. An asset's carrying amount is written down immediately to its recoverable amount if it is considered that the carrying amount is greater than its recoverable amount.

| | |
|---|---|
| Computer equipment | 3-5 years |
| Furniture & fittings | 5-9 years |
| Motor Vehicles | 5 years |
| Buildings | 50-100 years |
| Leasehold property improvements | 3-12 years |

Land and buildings are located in Fiji and are stated at fair value. Fair value is determined using an income approach whereby future rental streams are capitalised at a rate appropriate for the type of property and lease arrangement. This value is then adjusted to take into account recent market activity. Valuation was performed as at 30 August 2017 by Rolle Associates, registered valuers in Fiji. There has been no material movement in the valuation between 30 August 2017 and 30 September 2017. Inputs to the valuation of the Fiji property are considered to be based on non-observable market data, thus classified as level 3 in the fair value hierarchy. Inputs include gross rentals per square meter of similar property in the Suva area, recent comparable sales of commercial property in Suva and a capitalisation rate of 7.0% (2016: 7.0%).

Had land and buildings been recognised under the cost model the carrying amount would have been $1,145,000 (2016: $1,145,000). The revaluation surplus for the period is recorded in other comprehensive income and has no restrictions on the distribution of the balance to shareholders.

# NOTES TO THE FINANCIAL STATEMENTS

## 18 PAYABLES

| $ thousands | Note | 2017 | 2016 |
|---|---|---|---|
| Trade payables | | **16,479** | 16,125 |
| Reinsurance payables | | **4,063** | 4,445 |
| Payable to other insurers | | **2,590** | 2,798 |
| Other payables | | **27,992** | 26,132 |
| **Total payables** | | **51,124** | 49,500 |
| | | | |
| **Analysed as:** | | | |
| Current | | **51,124** | 49,500 |
| Non current | | **-** | - |
| **Total payables** | | **51,124** | 49,500 |

These amounts represent liabilities for goods and services provided to the Group prior to the end of the financial year which are unsettled. Payables are recognised initially at fair value less transaction costs and subsequently measured at amortised cost using the effective interest method.

Tower Insurance is a party to the Shared Property Process – Insurer Contract (SPP) which sets out obligations for insurers and appoints a lead insurer to act on behalf of other insurers with respect to the repair and rebuild of shared properties (known as multi-units). As lead insurer on multi-unit repairs or rebuilds, Tower Insurance receives cash from other insurance companies as settlement of their obligations under building contracts covered within the SPP. Tower Insurance has recorded amounts received from other insurers as a Payable, recognising these funds are restricted in use. Funds can only be applied to the rebuild or repair of properties within the SPP that Tower Insurance is lead insurer for. Tower Insurance holds this cash on behalf of other insurers in a segregated bank account.

At 30 September 2017 there was $2.6 million (2016: $2.8 million) recorded within Payables as funds held on behalf of other insurers in respect of SPP claims. Refer also to Note 12 for further details on cash held in respect of multi-unit claims as lead insurer.

## 19 PROVISIONS

| $ thousands | Note | 2017 | 2016 |
|---|---|---|---|
| Employee benefits | | **5,773** | 4,177 |
| **Total provisions** | | **5,773** | 4,177 |
| | | | |
| **Analysed as:** | | | |
| Current | | **5,592** | 4,037 |
| Non current | | **181** | 140 |
| **Total provisions** | | **5,773** | 4,177 |

Provisions are only recognised when the Group has a present legal or constructive obligation as a result of a past event or decision, and it is more likely than not that an outflow of resources will be required to settle the obligation. Provisions are recognised as the best estimate of future cash flows discounted to present value where the effect is material.

Provision is made for employee entitlements for services rendered up to the balance date. This includes salaries, wages, bonuses, annual leave and long service leave. Liabilities arising in respect of employee entitlements expected to be settled within 12 months of the reporting date are measured at their nominal amounts. All other employee entitlements are measured at the present value of the estimated future cash outflows to be made in respect of services provided up to the balance date. In determining the present value of future cash outflows, discount rates used are based on the interest rates attaching to government securities which have terms to maturity approximating the terms of the related liability.

## 20 INSURANCE LIABILITIES

| $ thousands | Note | 2017 | 2016 |
|---|---|---|---|
| Unearned premiums | | **154,848** | 150,807 |
| Outstanding claims | | **171,156** | 210,202 |
| Additional risk margin | | **10,000** | - |
| **Total insurance liabilities** | | **336,004** | 361,009 |
| | | | |
| **Analysed as** | | | |
| Current | | **297,190** | 291,845 |
| Non current | | **38,814** | 69,164 |
| **Total insurance liabilities** | | **336,004** | 361,009 |

The table below includes the reconciliation of the unearned premiums as at the reporting date:

| | | |
|---|---|---|
| **Opening balance** | **150,807** | 155,677 |
| Premiums written | **296,855** | 288,537 |
| Premiums earned | **(292,153)** | (293,911) |
| Foreign exchange movements | **(661)** | 504 |
| **Closing balance** | **154,848** | 150,807 |

Outstanding claims are measured at the central estimate of the present value of expected future payments after allowing for inflation and discounted at the risk free rate. In addition a risk margin is added to the claims provision to recognise the inherent uncertainty of the central estimate and to ensure provision is at least at 75% probability of sufficiency.

The expected future payments include those in relation to claims reported but not yet paid, claims incurred but not yet reported (IBNR), claims incurred but not enough reported (IBNER) and anticipated claims handling costs. Claims handling costs include costs that can be associated directly with individual claims, such as legal and other professional fees, and costs that can only be indirectly associated with individual claims, such as claims administration costs.

Provision has been made for the estimate of claim recoveries from third parties.

Liability adequacy testing is performed in order to recognise any deficiencies in the income statement arising from the carrying amount of the unearned premium liability less any related deferred acquisition costs and intangible assets not meeting the estimated future claims under current insurance conditions. Liability adequacy testing is performed at a portfolio level of contracts that are subject to broadly similar risks and are managed together as a single portfolio.

Refer to Note 8 for further details on the additional risk margin.

## 21 DISTRIBUTIONS TO SHAREHOLDERS

### DIVIDEND PAYMENTS

There were no Tower Limited dividend payments during the year ended 30 September 2017.

The final dividend for the 2015 financial year of 7.5 cents per share 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 Dividend Reinvestment Plan was not offered.

The interim dividend for the 2016 financial year of 8.5 cents per share was paid on 30 June 2016. The total amount paid was $14,336,340. There were no imputation credits attached to the dividend and the Dividend Reinvestment Plan was not offered.

### RETURN OF CAPITAL

There was no return of capital during the year ended 30 September 2017.

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 year ended 30 September 2017.

In 2015 the Company commenced 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.

# NOTES TO THE FINANCIAL STATEMENTS

## 22 BORROWINGS

| $ thousands | Currency | Interest Rate | Rollover Date (drawn) / Maturity Date (undrawn) | Face Value | Unamortised Costs | Carrying Value | Fair Value |
|---|---|---|---|---|---|---|---|
| **As at 30 September 2017** | | | | | | | |
| Bank facilities (drawn) | NZD | 4.505% | 13-Nov-17 | 30,000 | (79) | 29,921 | 29,921 |
| Bank facilities (undrawn) | NZD | Variable | 9-Sep-19 | 20,000 | - | - | - |
| **Total borrowings** | | | | | **(79)** | **29,921** | **29,921** |
| As at 30 September 2016 | | | | | | | |
| Bank facilities (undrawn) | NZD | Variable | 9-Sep-19 | 50,000 | - | - | - |
| **Total borrowings** | | | | | - | - | - |

Borrowings are recognised initially at fair value, net of transaction costs incurred. Subsequent to initial recognition, borrowings are measured at amortised cost with any difference between the initial recognised amount and the redemption value being recognised in the income statement over the period of the borrowings using the effective interest method.

Fees paid on the establishment of loan facilities are recognised as transaction costs of the loan to the extent that it is probable that some or all of the facility will be drawn down. The fee is capitalised as a pre-payment for liquidity services and amortised over the period of the facility to which it relates.

| $ thousands | Note | 2017 | 2016 |
|---|---|---|---|
| **Analysed as** | | | |
| Current | | **29,921** | - |
| Non current | | **-** | - |
| **Total borrowings** | | **29,921** | - |

### STANDBY CREDIT FACILITY

The Company entered into a cash advance facility with Bank of New Zealand on 7 September 2016. The facility provides for an amount of up to $50.0 million that can be drawn for general corporate purposes over a three year term and is subject to normal terms and conditions for a facility of this nature, including financial covenants.

In May 2017, the Company utilised the cash advance facility agreement. An amount of $30.0 million was drawn (from the available $50.0 million). Funds were used for new share capital within Tower Insurance Limited.

### COVENANTS

All borrowings are unsecured and are subject to various financial covenants. The Company has fully complied with all covenants during the year ended 30 September 2017.

# NOTES TO THE FINANCIAL STATEMENTS

## 23 CONTRIBUTED EQUITY

| $ thousands | 2017 | 2016 |
|---|---|---|
| Ordinary share capital (fully paid) | **382,172** | 382,172 |
| **Total contributed equity** | **382,172** | 382,172 |

**Represented by:**

| Number of shares | 2017 | 2016 |
|---|---|---|
| Ordinary shares (issued and fully paid) | **168,662,150** | 168,662,150 |
| **Movement in ordinary shares:** | | |
| **Opening balance** | **168,662,150** | 169,983,470 |
| Buyback of share capital | **-** | (1,321,320) |
| **Closing balance** | **168,662,150** | 168,662,150 |

Ordinary shares issued by the Group are classified as equity and are recognised at fair value less direct issue costs. All shares rank equally with one vote attached to each share. There is no par value for each share.

## 24 RESERVES

| $ thousands | Note | 2017 | 2016 |
|---|---|---|---|
| **Foreign currency translation reserve (FCTR)** | | | |
| Opening balance | | **(4,443)** | 791 |
| Currency translation differences arising during the year | | **100** | (5,234) |
| **Closing balance** | | **(4,343)** | (4,443) |
| | | | |
| **Separation Reserve** | | | |
| Opening balance | | **(113,000)** | (113,000) |
| **Closing balance** | | **(113,000)** | (113,000) |
| | | | |
| **Asset revaluation reserve** | | | |
| Opening balance | | **671** | 513 |
| Gain on revaluation, net of deferred tax | | **218** | 158 |
| **Closing balance** | | **889** | 671 |
| | | | |
| **Total reserves** | | **(116,454)** | (116,772) |

Exchange differences arising on translation of foreign controlled entities and net investment of a foreign entity are taken to the foreign currency translation reserve as described in Note 1. The reserve is recognised in profit and loss when the net investment is disposed.

The separation reserve was created in 2007 at the time of the demerger of the New Zealand and Australian businesses in accordance with a ruling provided by the Australian Tax Office (ATO). It will be carried forward indefinitely as a non-equity reserve to meet the requirements of the ATO.

The asset revaluation reserve is used to recognise unrealised gains on the value of land and buildings above initial cost.

# NOTES TO THE FINANCIAL STATEMENTS

## 25 NET ASSETS PER SHARE

| $ dollars | **2017** | 2016 |
|---|---|---|
| Net assets per share | **1.28** | 1.33 |
| Net tangible assets per share | **0.90** | 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.

Reconciliation to net tangible assets is provided below:

| $ thousands | **2017** | 2016 |
|---|---|---|
| **Net assets** | **215,744** | 223,952 |
| Less: deferred tax | **(32,405)** | (29,370) |
| Less: intangible assets | **(31,334)** | (31,982) |
| **Net tangible assets** | **152,005** | 162,600 |

## 26 EARNINGS PER SHARE

Basic earnings per share is calculated by dividing the net profit attributed to shareholders of the Company, excluding any costs of servicing equity other than ordinary shares, by the weighted average number of ordinary shares outstanding during the year.

Diluted earnings per share is calculated by dividing the net profit attributed to shareholders of the Company by the weighted average number of ordinary shares on issue during the year adjusted for the weighted average number of ordinary shares that would be issued on the conversion of all the dilutive potential ordinary shares into ordinary shares.

There was no dilutive impact on basic earnings per share for 2017 (2016: nil).

| $ thousands | **2017** | 2016 |
|---|---|---|
| Loss attributable to shareholders | **(8,461)** | (22,328) |

| Number of shares | **2017** | 2016 |
|---|---|---|
| Weighted average number of ordinary shares for basic and diluted earnings per share | **168,662,150** | 169,069,382 |

| Cents | **2017** | 2016 |
|---|---|---|
| Basic and diluted (loss) earnings per share | **(5.02)** | (13.21) |

## 27 INSURANCE BUSINESS DISCLOSURE

### 27A NET CLAIMS EXPENSE

| | **2017** | | | 2016 | | |
|---|---|---|---|---|---|---|
| $ thousands | **Risks borne in current year** | **Risks borne in prior years** | **Total** | Risks borne in current year | Risks borne in prior years | Total |
| **Gross claims expense** | | | | | | |
| Direct claims - undiscounted | **171,160** | **46,316** | **217,476** | 148,710 | 91,358 | 240,068 |
| Movement in discount | **43** | **28** | **71** | 53 | 17 | 70 |
| **Total gross claims expense** | **171,203** | **46,344** | **217,547** | 148,763 | 91,375 | 240,138 |
| **Reinsurance and other recoveries** | | | | | | |
| Reinsurance and other recoveries - undiscounted | **(16,640)** | **(13,354)** | **(29,994)** | (12,094) | (42,428) | (54,522) |
| Movement in discount | **(1)** | **(1)** | **(2)** | (3) | (1) | (4) |
| **Total reinsurance recoveries** | **(16,641)** | **(13,355)** | **(29,996)** | (12,097) | (42,429) | (54,526) |
| **Net claims expense** | **154,562** | **32,989** | **187,551** | 136,666 | 48,946 | 185,612 |

Current year amounts relate to risks borne in the current financial year. Prior period amounts relate to a reassessment of the risks borne in all previous financial years including those arising due to the Canterbury earthquakes. Refer to Notes 7 and 8.

### 27B OUTSTANDING CLAIMS

**(a) Assumptions adopted in calculation of insurance liabilities**

The estimation of outstanding claims as at 30 September 2017 has been carried out by the following Actuaries:

Rick Shaw, B.Sc. (Hons), FIAA, Appointed Actuary; and

Peter Davies, B.Bus.Sc, FIA, FNZSA.

The New Zealand actuarial assessments are undertaken in accordance with the standards of the New Zealand Society of Actuaries, in particular Professional Standard No. 30 "Valuations of General Insurance Claims". The Actuaries were satisfied as to the nature, sufficiency and accuracy of the data used to determine the outstanding claims liability. The outstanding claims liability is set by the Actuaries at a level that is appropriate and sustainable to cover the Group's claims obligations after having regard to the prevailing market environment and prudent industry practice.

The following assumptions have been made in determining net outstanding claims liabilities:

| | **2017** | 2016 |
|---|---|---|
| Inflation rates varied from | 0.0% - 3.8% | 0.0% - 3.8% |
| Inflation rates for succeeding year | 0.0% - 3.8% | 0.0% - 3.8% |
| Inflation rates for following years | 0.0% - 3.8% | 0.0% - 3.8% |
| Discount rates varied from | 0.0% - 6.3% | 0.0% - 6.3% |
| Discount rates for succeeding year | 0.0% - 6.3% | 0.0% - 6.3% |
| Discount rates for following years | 0.0% - 6.3% | 0.0% - 6.3% |
| Claims handling expense ratio | 3.1% - 39.1% | 0.0% - 56.4% |
| Risk margin | 4.9% - 23.1% | 6.3% - 21.8% |

In addition to the risk margin range shown above, the total risk margin also includes $23,900,000, gross of reinsurance (2016: $17,700,000) associated with the Canterbury earthquakes.

## 27 INSURANCE BUSINESS DISCLOSURE (continued)

The weighted average expected term to settlement of outstanding claims (except for Canterbury earthquake claims) based on historical trends is:

| | **2017** | 2016 |
|---|---|---|
| Short tail claims within 1 year | within 1 year | within 1 year |
| Long tail claims in the Pacific Islands | 1.0 to 1.8 years | 0.9 to 1.8 years |
| Inwards reinsurance | greater than 10 years | greater than 10 years |

**Inflation rate**
Insurance costs are subject to inflationary pressures. Inflation assumptions for all classes of business are based on current economic indicators for the relevant country.

For motor and property classes, for example, claim costs are related to the inflationary pressures of the materials and goods insured as well as labour costs to effect repairs. These costs are expected to increase at a level between appropriate Consumer Price Index (CPI) indices and wage inflation.

**Discount rate**
Outstanding claim liabilities are discounted to present value using a risk free rate relevant to the term of the liability and the jurisdiction.

**EQC recoveries**
For each claim to which additional EQC recoveries relate, Tower has allocated recoverable amounts according to the quality of information and evidence available. Claims with primary evidence (e.g. independent expert documentation) have been assessed as having a strong position for recovery. Claims with non-primary evidence (e.g. general documentation like post code analysis or adjacent locations) will have a lower likelihood of recovery.

**Apportionment**

Tower assesses claims and apportions damage between Canterbury earthquake events on an individual property basis. The allocation process uses a hierarchical approach based on the relative quality and number of claim assessments completed after each of the four main earthquakes. Results from the hierarchical approach are used as an input to the actuarial valuations which estimate the ultimate claims costs.

**Claims handling expense**
The estimate of outstanding claim liabilities incorporates an allowance for the future cost of administering the claims. This allowance is determined after analysing historical claim related expenses incurred by the classes of business.

**Risk margin**
The outstanding claim liabilities also include a risk margin that relates to the inherent uncertainty in the central estimate of the future payments.

Risk margins are determined on a basis that reflects the business. Regard is given to the robustness of the valuation models, the reliability and volume of available data, past experience of the insurer and the industry, and the characteristics of the classes of business written.

Uncertainty in claims is represented as a volatility measure in relation to the central estimate. The volatility measure is derived after consideration of statistical modelling and benchmarking to industry analysis. The measure of the volatility is referred to as the coefficient of variation (CoV), defined as the standard deviation of the distribution of future cash flows divided by the mean.

Risk margins are calculated by jurisdiction. The risk margin for all classes when aggregated is less than the sum of the individual risk margins. This reflects the benefit of diversification. The measure of the parameter used to derive the diversification benefit is referred to as correlation, which is adopted with regard to industry analysis, historical experience and actuarial judgement.

The risk margins applied to future claims payments are determined with the objective of achieving 75% probability of sufficiency for both the outstanding claims liability and the unexpired risk liability.

## 27 INSURANCE BUSINESS DISCLOSURE (continued)

The following analysis is in respect of the insurance liabilities:

| $ thousands | Note | **2017** | 2016 |
|---|---|---|---|
| Central estimate of expected present value of future payments for claims incurred | | **133,898** | 129,058 |
| Risk margin | | **27,885** | 14,663 |
| Claims handling costs | | **3,914** | 4,177 |
| | | **165,697** | 147,898 |
| Discount | | **(270)** | (201) |
| **Net outstanding claims** | | **165,427** | 147,697 |

**Reconciliation of movements in discounted outstanding claim liabilities**

| | **2017** | | | 2016 | | |
|---|---|---|---|---|---|---|
| $ thousands | **Gross** | **Reinsurance** | **Net** | Gross | Reinsurance | Net |
| Balance brought forward | **210,202** | **(62,505)** | **147,697** | 220,200 | (65,914) | 154,286 |
| Effect of change in foreign exchange rates | **(553)** | **98** | **(455)** | 699 | 3 | 702 |
| Incurred claims recognised in the income statement | **217,547** | **(29,996)** | **187,551** | 240,138 | (54,526) | 185,612 |
| Claim (payment) recoveries during the year | **(246,040)** | **76,674** | **(169,366)** | (250,835) | 57,932 | (192,903) |
| **Total outstanding claims** | **181,156** | **(15,729)** | **165,427** | 210,202 | (62,505) | 147,697 |

**Reconciliation of movements in undiscounted claims to outstanding claim liabilities**

| | **2017** | | | 2016 | | |
|---|---|---|---|---|---|---|
| $ thousands | **Gross** | **Reinsurance** | **Net** | Gross | Reinsurance | Net |
| Outstanding claims undiscounted | **1,968** | **(367)** | **1,601** | 1,731 | (90) | 1,641 |
| Discount | **60** | **-** | **60** | (13) | 2 | (11) |
| Outstanding claims | **2,028** | **(367)** | **1,661** | 1,718 | (88) | 1,630 |
| Short tail outstanding claims | | | **163,766** | | | 146,067 |
| **Total outstanding claims** | | | **165,427** | | | 147,697 |

**(b) Sensitivity analysis**

The Group's insurance business is generally short tail in nature. Key sensitivities relate to the volume of claims, in particular for significant events such as earthquakes or extreme weather.

The Group has exposure to historical inwards reinsurance business which is in run off. While this business is not material, it is sensitive to claims experience, timing of claims and changes in assumptions. Movement in these variables does not have a material impact on the performance and equity of the Group.

# NOTES TO THE FINANCIAL STATEMENTS

## 27 INSURANCE BUSINESS DISCLOSURE (continued)

### (c) Future net cash out flows

The following table shows the expected run-off pattern of net outstanding claims:

| $ thousands | Note | **2017** | 2016 |
|---|---|---|---|
| **Expected claim payments** | | | |
| Within 3 months | | **50,622** | 39,580 |
| 3 to 6 months | | **32,137** | 22,255 |
| 6 to 12 months | | **43,064** | 19,234 |
| After 12 months | | **39,604** | 66,628 |
| **Total outstanding claim liabilities** | | **165,427** | 147,697 |

### 27C RISK MANAGEMENT POLICIES AND PROCEDURES

The financial condition and operations of the insurance business are affected by a number of key risks including insurance risk, interest rate risk, currency risk, market risk, financial risk, compliance risk, fiscal risk and operational risk, (refer to Note 29). Notes on the policies and procedures employed in managing these risks in the insurance business are set out below.

### (a) Objectives in managing risks arising from insurance contracts and policies for mitigating those risks

The risk management activities include prudent underwriting, pricing, and management of risk, together with claims management, reserving and investment management. The objective of these disciplines is to enhance the financial performance of the insurance operations and to ensure sound business practices are in place for underwriting risks and claims management.

The key policies in place to mitigate risks arising from writing insurance contracts include:

- comprehensive management information systems and actuarial models using historical information to calculate premiums and monitor claims;
- monitoring natural disasters such as earthquakes, floods, storms and other catastrophes using models; and
- the use of reinsurance to limit the Group's exposure to individual catastrophic risks.

### (b) Concentration of insurance risk

| Risk | Source of concentration | Risk management measures |
|---|---|---|
| An accumulation of risks arising from a natural peril | Insured property concentrations | Accumulation risk modelling, reinsurance protection |
| A large property loss | Fire or collapse affecting one building or a group of adjacent buildings | Maximum acceptance limits, property risk grading, reinsurance protection |

# NOTES TO THE FINANCIAL STATEMENTS

## 27 INSURANCE BUSINESS DISCLOSURE (continued)

### (c) Development of claims

The following table shows the development of net outstanding claims relative to the current estimate of ultimate claims costs for the five most recent years:

| | $ thousands | | | | | | |
|---|---|---|---|---|---|---|---|
| Ultimate claims cost estimate | **Prior** | **2013** | **2014** | **2015** | **2016** | **2017** | **Total** |
| At end of incident year | | 113,839 | 123,816 | 138,878 | 137,220 | 154,562 | |
| One year later | | 117,277 | 124,667 | 138,720 | 145,970 | | |
| Two years later | | 116,819 | 125,502 | 138,851 | | | |
| Three years later | | 117,862 | 125,408 | | | | |
| Four years later | | 142,015 | | | | | |
| Current estimate of ultimate claims cost | | 142,015 | 125,408 | 138,851 | 145,970 | 154,562 | |
| Cumulative payments | | (141,740) | (125,125) | (138,094) | (139,064) | (119,644) | |
| Undiscounted central estimate | 90,759 | 275 | 283 | 757 | 6,906 | 34,918 | 133,898 |
| Discount to present value | (3) | (3) | (11) | (8) | (19) | (226) | (270) |
| Discounted central estimate | 90,756 | 272 | 272 | 749 | 6,887 | 34,692 | 133,628 |
| Claims handling expense | | | | | | | 3,914 |
| Risk margin | | | | | | | 27,885 |
| Net outstanding claim liabilities | | | | | | | 165,427 |
| Reinsurance recoveries on outstanding claim liabilities and other recoveries | | | | | | | 15,729 |
| **Gross outstanding claim liabilities** | | | | | | | 181,156 |

### 27D LIABILITY ADEQUACY TEST

Liability adequacy tests are performed to determine whether the unearned premium liability is sufficient to cover the present value of the expected cash flows arising from rights and obligations under current insurance contracts, plus an additional risk margin to reflect the inherent uncertainty in the central estimate. The future cash flows are future claims, associated claims handling costs and other administration costs relating to the business.

If the unearned premium liability less related deferred acquisition costs exceeds the present value of expected future cash flows plus additional risk margin then the unearned premium liability is deemed to be adequate. The risk margins applied to future claims were determined with the objective of achieving at least 75% probability of sufficiency of the unexpired risk liability using the methodology described above. The unearned premium liabilities as at 30 September 2017 were sufficient (2016: sufficient).

| % | **2017** | 2016 |
|---|---|---|
| Central estimate claim % of premium | **41.2%** | 45.3% |
| Risk margin | **12.0%** | 9.3% |

## 27 INSURANCE BUSINESS DISCLOSURE (continued)

### 27E INSURER FINANCIAL STRENGTH RATING

Tower Insurance Limited has an insurer financial strength rating of ‘A-’ (Excellent) issued by international rating agency AM Best Company Inc. with an effective date of 16 August 2017.

### 27F REINSURANCE PROGRAMME

Reinsurance programmes are structured to adequately protect the solvency and capital positions of the insurance business. The adequacy of reinsurance cover is modelled by assessing Tower's exposure under a range of scenarios. The plausible scenario that has the most financial significance for Tower is a major Wellington earthquake. Each year, as part of setting the coming year's reinsurance cover, comprehensive modelling of the event probability and amount of the Group's exposure is undertaken.

### 27G SOLVENCY REQUIREMENTS

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.

The minimum solvency capital required to meet solvency requirements under the Insurance (Prudential Supervision) Act 2010 is shown below. Actual solvency capital exceeds the minimum solvency capital requirement for Tower Insurance Group by $96.3 million (2016: $73.8 million) and Tower Insurance parent by $87.9 million (2016: $64.3 million).

| | **Tower Insurance Limited** | | **Tower Insurance Limited Group** | |
|---|---|---|---|---|
| | **Unaudited** | Unaudited | **Audited** | Audited |
| $ thousands | **2017** | 2016 | **2017** | 2016 |
| Actual solvency capital | **149,317** | 120,684 | **166,823** | 140,827 |
| Minimum solvency capital | **61,387** | 56,350 | **70,545** | 67,047 |
| **Solvency margin** | **87,930** | 64,334 | **96,278** | 73,780 |
| **Solvency ratio** | **243%** | 214% | **236%** | 210% |

The Reserve Bank of New Zealand imposed a condition of license requirement for Tower Insurance Limited to maintain a minimum solvency margin of $50.0 million. This minimum solvency requirement continues to be a requirement for Tower Insurance Limited.

### 27H ASSETS BACKING INSURANCE BUSINESS

The Group has determined that all assets within its insurance companies are held to back insurance liabilities, with the exception of property, plant and equipment and investments in operating subsidiaries.

Assets backing insurance liabilities are managed in accordance with approved investment mandate agreements on a fair value basis and are reported to the Board on this basis.

# NOTES TO THE FINANCIAL STATEMENTS

## 28 FINANCIAL INSTRUMENTS

### 28A FINANCIAL INSTRUMENT CATEGORIES

The Group classifies its financial assets and liabilities in the following categories: at fair value through profit or loss; loans and receivables; and liabilities at amortised cost. The classification depends on the purpose for which the financial assets and liabilities were acquired. Management determines the classification of its financial assets and liabilities at initial recognition.

*(i) Loans and receivables*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted on an active market. The Group's loans and receivables comprise trade and other receivables and cash and cash equivalents in the balance sheet. Loans and receivables are measured initially at fair value plus transaction costs and subsequently at amortised cost using the effective interest method less any impairment.

*(ii) Financial liabilities at amortised cost*

Financial liabilities at amortised cost are non-derivative financial liabilities with fixed or determinable payments that are not quoted on an active market. The Group's financial liabilities comprise trade, reinsurance and other payables in the balance sheet. Financial liabilities are measured initially at fair value plus transaction costs and subsequently at amortised cost less any impairment.

*(iii) Financial assets and liabilities at fair value through profit or loss*

Financial assets and liabilities at fair value through profit or loss comprise of financial assets that are either held for trading or designated on initial recognition at fair value through profit or loss. A financial asset is classified in this category if acquired principally for the purpose of selling in the short-term or if so designated by management. Designation by management takes place when it is necessary to eliminate or significantly reduce measurement or recognition inconsistencies or if related financial assets or liabilities are managed and evaluated on a fair value basis.

Financial assets at fair value through profit or loss are stated at fair value, with any resultant gain or loss recognised in the income statements. The net gain or loss recognised in the income statements includes any dividend or interest earned on the financial assets.

Derivatives are categorised as held for trading unless they are designated as hedges. All derivatives entered into by the Group are classified as held for trading.

*(iv) Fair value*

Financial assets and liabilities are measured in the balance sheet at fair value with the exception of short term amounts which are held at a reasonable approximation of fair value.

*(v) Offsetting financial instruments*

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis or realise the asset and settle the liability simultaneously.

The Group does not hold financial assets and financial liabilities subject to offsetting arrangements other than cash and cash equivalents. Refer to Note 12.

*(vi) Derecognition*

Financial assets are derecognised when the rights to receive cash flows from the investments have expired or have been transferred and the Group has transferred substantially all risks and rewards of ownership.

# NOTES TO THE FINANCIAL STATEMENTS

## 28 FINANCIAL INSTRUMENTS (continued)

The analysis of financial assets and liabilities into their categories and classes is set out in the following tables:

| | | | At amortised cost | | At fair value through profit or loss | |
|---|---|---|---|---|---|---|
| $ thousands | Note | **Total** | **Loans and receivables** | **Financial liabilities** | **Designated** | **Held for trading** |
| **As at 30 September 2017** | | | | | | |
| **Assets** | | | | | | |
| Cash and cash equivalents | | **102,876** | **102,876** | **-** | **-** | **-** |
| Trade and other receivables | | **257,964** | **257,964** | **-** | **-** | **-** |
| Investments | | **167,702** | **-** | **-** | **167,702** | **-** |
| Derivative assets | | **231** | **-** | **-** | **231** | **-** |
| **Total financial assets** | | **528,773** | **360,840** | **-** | **167,933** | **-** |
| **Liabilities** | | | | | | |
| Trade and other payables | | **25,814** | **-** | **25,814** | **-** | **-** |
| Borrowings | | **29,921** | **-** | **29,921** | **-** | **-** |
| **Total financial liabilities** | | **55,735** | **-** | **55,735** | **-** | - |

| | | | At amortised cost | | At fair value through profit or loss | |
|---|---|---|---|---|---|---|
| $ thousands | Note | Total | Loans and receivables | Financial liabilities | Designated | Held for trading |
| As at 30 September 2016 | | | | | | |
| **Assets** | | | | | | |
| Cash and cash equivalents | | 92,228 | 92,228 | - | - | - |
| Trade and other receivables | | 253,115 | 253,115 | - | - | - |
| Investments | | 188,522 | - | - | 188,522 | - |
| Derivative assets | | 57 | - | - | 57 | - |
| **Total financial assets** | | 533,922 | 345,343 | - | 188,579 | - |
| **Liabilities** | | | | | | |
| Trade and other payables | | 26,532 | - | 26,532 | - | - |
| Derivative financial liabilities | | 735 | - | - | 735 | - |
| **Total financial liabilities** | | 27,267 | - | 26,532 | 735 | - |

# NOTES TO THE FINANCIAL STATEMENTS

## 28 FINANCIAL INSTRUMENTS (continued)

### 28B 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 30 September 2017, the Level 3 category included an investment in equity securities of $1,412,000 (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 valued by a third party independent valuer. The valuation has been calculated using the Income Capitalisation Approach and a sensitivity analysis has been performed later in this note.

*(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 FINANCIAL STATEMENTS

## 28 FINANCIAL INSTRUMENTS (continued)

The following tables present the Group's assets and liabilities categorised by fair value measurement hierarchy levels.

| $ thousands | Note | Total | Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|---|
| **As at 30 September 2017** | | | | | |
| **Assets** | | | | | |
| Investment in equity securities | | **1,412** | **-** | **-** | **1,412** |
| Investments in fixed interest securities | | **166,256** | **-** | **166,256** | **-** |
| Investments in property securities | | **34** | **-** | **34** | **-** |
| Investments | | **167,702** | **-** | **166,290** | **1,412** |
| Derivative financial assets | | **231** | **-** | **231** | **-** |
| **Total financial assets** | | **167,933** | **-** | **166,521** | **1,412** |
| **Liabilities** | | | | | |
| Borrowings | | **29,921** | **-** | **29,921** | **-** |
| **Total financial liabilities** | | **29,921** | **-** | **29,921** | **-** |
| As at 30 September 2016 | | | | | |
| **Assets** | | | | | |
| 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 | - |
| **Total financial assets** | | 188,579 | - | 187,173 | 1,406 |
| **Liabilities** | | | | | |
| Derivative financial liabilities | | 735 | - | 735 | - |
| **Total financial liabilities** | | 735 | - | 735 | - |

The following table represents the changes in Level 3 instruments:

| | Investment in equity securities | |
|---|---|---|
| $ thousands | **2017** | 2016 |
| **Opening balance** | **1,406** | 1,972 |
| Total gains and losses recognised in profit or loss | **(3)** | (163) |
| Foreign currency movement | **9** | (403) |
| **Closing balance** | **1,412** | 1,406 |

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

| $ thousands | Carrying Amount | Favourable changes of 10% | Unfavourable changes of 10% |
|---|---|---|---|
| **As at 30 September 2017** | | | |
| Investment in equity securities | **1,412** | **141** | **(141)** |
| As at 30 September 2016 | | | |
| Investment in equity securities | 1,406 | 141 | (141) |

## 28 FINANCIAL INSTRUMENTS (continued)

### 28C IMPAIRMENT OF FINANCIAL ASSETS

Financial assets, with the exception of those measured at fair value through profit or loss, are assessed for indicators of impairment at each reporting date. Financial assets are impaired when there is objective evidence that the estimated future cash flows of the asset have been impacted as a result of one or more events that occurred after the initial recognition of the financial asset.

For financial assets carried at amortised cost, the amount of the impairment is the difference between the carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate.

For all financial assets, other than trade receivables, the carrying amount is reduced by the impairment loss directly. For trade receivables the carrying amount is reduced via an allowance account, against which an uncollectible trade receivable is written off.

A trade receivable is deemed to be uncollectible upon receipt of evidence that the Group will be unable to collect the amount. Changes in the carrying amount of the allowance account are recognised in the income statement.

A previously recognised impairment loss is reversed when, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment loss was initially recognised.

In respect of financial assets carried at amortised cost, with the exception of trade receivables, the impairment loss is reversed through the income statement to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised. Subsequent recoveries of trade receivables previously written off are credited against the allowance account.

## 29 RISK MANAGEMENT

The financial condition and operating results of the Group are affected by a number of key financial and non-financial risks. Financial risks include market risk, credit risk, financing and liquidity risk. The non-financial risks include insurance risk, compliance risk and operational risk. The Group's objectives and policies in respect of insurance risks are disclosed in Note 27, while the managing of financial and other non financial risks are set out in the remainder of this note.

Tower Limited's objective is to satisfactorily manage these risks in line with the Board approved Group Risk and Compliance policy. Various procedures are put in place to control and mitigate the risks faced by the Group. Business managers are responsible for understanding and managing their risks including operational and compliance risk. The consolidated entity’s exposure to all high and critical risks is reported monthly to the Board and quarterly to the Audit and Risk Committee.

The Board has delegated to the Audit and Risk Committee the responsibility to review the effectiveness and efficiency of management processes, internal audit services, risk management and internal financial controls and systems as part of their duties. The Risk and Compliance team is in place in an oversight and advisory capacity and to manage the risk and compliance framework.

Financial risks are generally monitored and controlled by selecting appropriate assets to back policy liabilities. The assets are regularly monitored to ensure that there are no material asset and liability mismatching issues and other risks such as liquidity risk and credit risk are maintained within acceptable limits.

The Board has responsibility for:

- reviewing investment policies for Tower Limited funds;
- reviewing the risk management policy and statements in respect of investment management, including the derivative policy;
- considering the establishment, adjustment or deletion of limits and counter-party approvals, and the scope of financial instruments to be used in the management of Tower Limited's investments;
- reviewing the appointment of external investment managers;
- monitoring investment and fund manager performance; and
- monitoring compliance with investment policies and client mandates.

# NOTES TO THE FINANCIAL STATEMENTS

## 29 RISK MANAGEMENT (continued)

### 29A MARKET RISK

Market risk is the risk of change in the fair value of financial instruments from fluctuations in foreign exchange rates (currency risk), market interest rates (interest rate risk) and market prices (price risk), whether such change in price is caused by factors specific to an individual financial instrument, or its issuer or factors affecting all financial instruments traded in a market.

The impact of reasonably possible changes in market risk on the Group shareholders' profit and equity is included in Note 29F.

*(i) Currency risk*

Currency risk is the risk of loss resulting from changes in exchange rates when applied to assets and liabilities or future transactions denominated in a currency that is not the Group's functional currency. The exposure is not considered to be material.

Tower Limited's principal transactions are carried out in New Zealand dollars and its exposure to foreign exchange risk arises primarily with respect to the Pacific Island insurance business.

Tower Limited generally elects to not hedge the capital invested in overseas entities, thereby accepting the foreign currency translation risk on invested capital.

The Board sets limits for the management of currency risk arising from its investments based on prudent international asset management practice. Regular reviews are conducted to ensure that these limits are adhered to. In accordance with this policy, Tower Insurance does not hedge the currency risk arising from translation of the financial statements of foreign operations other than through net investment in foreign operations.

*(ii) Interest rate risk*

Interest rate risk is the risk that the value or future value cash flows of a financial instrument will fluctuate because of changes in interest rates.

Interest rate and other market risks are managed by the Group through a strategic asset allocation policy and an investment management policy that has regard to policyholder expectations and risks and to target surplus for solvency as advised by the Appointed Actuary.

Interest rate risk arises to the extent that there is a mismatch between the fixed interest portfolios used to back outstanding claim liabilities and those outstanding claims. Interest rate risk is managed by matching the duration profiles of investment assets and outstanding claim liabilities.

*(iii) Price risk*

Price risk is the risk of loss resulting from the decline in prices of equity securities or other assets. The exposure is not considered to be material. Refer to Note 29F.

## 29 RISK MANAGEMENT (continued)

### 29B CREDIT RISK

Credit risk is the risk of loss that arises from a counterparty failing to meet their contractual commitment in full and on time, or from losses arising from the change in value of a trading financial instrument as a result in changes in credit risk of that instrument.

The Group's exposure to credit risk is limited to deposits and investments held with banks and other financial institutions as well as credit exposure to trade customers or other counterparties. Credit exposure in respect of the Group’s cash deposit balances is limited to banks with minimum AA credit ratings. Investments held with banks and financial institutions that are managed by investment managers have a minimum credit rating accepted by the Group of 'A'. Independent ratings are used for customers that are rated by rating agencies. For customers with no external ratings, internally developed minimum credit quality requirements are applied, which take into account customers' financial position, past experience and other relevant factors. Overall exposure to credit risk is monitored on a Group basis in accordance with limits set by the Board. The Group has no significant exposure to credit risk.

*(i) Credit risk concentration*

Concentration of credit risk exists when the Group enters into contracts or financial instruments with a number of counterparties that are engaged in similar business activities or exposed to similar economic factors that might affect their ability to meet contractual obligations. Tower Limited manages concentration of credit risk by credit rating, industry type and individual counterparty.

The significant concentrations of credit risk are outlined by industry type below.

| | Carrying value | |
|---|---|---|
| $ thousands | **2017** | 2016 |
| New Zealand government | **8,184** | 3,744 |
| Other government agencies | **18,412** | 12,390 |
| Banks | **229,526** | 237,842 |
| Financial institutions | **13,241** | 25,770 |
| Other non-investment related receivables | **257,964** | 252,736 |
| **Total financial assets with credit exposure** | **527,327** | 532,482 |

*(ii) Maximum exposure to credit risk*

The Group's maximum exposure to credit risk without taking account of any collateral or any other credit enhancements, is as follows:

| | Carrying value | |
|---|---|---|
| $ thousands | **2017** | 2016 |
| Cash and cash equivalents | **102,876** | 92,228 |
| Loans and receivables | **257,964** | 253,115 |
| Financial assets at fair value through profit or loss | **166,256** | 187,082 |
| Derivative financial assets | **231** | 57 |
| **Total credit risk** | **527,327** | 532,482 |

## NOTES TO THE FINANCIAL STATEMENTS

### 29 RISK MANAGEMENT (continued)

*(iii) Credit quality of financial assets that are neither past due nor impaired*

The credit quality of financial assets that are neither past due nor impaired can be assessed by reference to external credit ratings (if applicable) or to historical information about counterparty default rates:

| $ thousands | Carrying value 2017 | Carrying value 2016 |
|---|---|---|
| **Credit exposure by credit rating** | | |
| AAA | **67,201** | 81,795 |
| AA | **184,233** | 180,515 |
| A | **527** | 412 |
| BBB | **-** | - |
| Below BBB | **15,706** | 12,437 |
| **Total counterparties with external credit ratings** | **267,667** | 275,159 |
| Group 1 | **205,601** | 234,274 |
| Group 2 | **-** | - |
| Group 3 | **1,696** | 6,026 |
| **Total counterparties with no external credit rating** | **207,297** | 240,300 |
| **Total financial assets neither past due nor impaired with credit exposure** | **474,964** | 515,459 |

Group 1 - trade debtors outstanding for less than 6 months

Group 2 - trade debtors outstanding for more than 6 months with no defaults in the past

Group 3 - unrated investments

Tower Insurance invests in Pacific regional investment markets through its Pacific Island operations to comply with local statutory requirements and in accordance with Tower Insurance investment policies. These investments generally have low credit ratings representing the majority of the value included in the 'Below BBB' and unrated categories in the table above.

*(iv) Financial assets that would otherwise be past due whose terms have been renegotiated*

No financial assets have been renegotiated in the past year (2016: nil).

*(v) Financial assets that are past due but not impaired*

The Group considers that financial assets are past due if payments have not been received when contractually due. At the reporting date, the total carrying value of past due but not impaired assets held are as follows:

| $ thousands | Less than 30 days | 31 to 60 days | 61 to 90 days | Over 90 days | Total |
|---|---|---|---|---|---|
| **As at 30 September 2017** | | | | | |
| Reinsurance recoveries receivable | **3,735** | **2,680** | **1,999** | **35,491** | **43,905** |
| Outstanding premiums and trade receivables | **5,026** | **1,754** | **1,268** | **410** | **8,458** |
| **Total** | **8,761** | **4,434** | **3,267** | **35,901** | **52,363** |

# NOTES TO THE FINANCIAL STATEMENTS

## 29 RISK MANAGEMENT (continued)

*(v) Financial assets that are past due but not impaired (continued)*

| $ thousands | Less than 30 days | 31 to 60 days | 61 to 90 days | Over 90 days | Total |
|---|---|---|---|---|---|
| As at 30 September 2016 | | | | | |
| Reinsurance recoveries receivable | 1,875 | 2,442 | 45 | 3 | 4,365 |
| Outstanding premiums and trade receivables | 3,150 | 7,978 | 1,244 | 285 | 12,657 |
| **Total** | 5,025 | 10,420 | 1,289 | 288 | 17,022 |

*(vi) Financial assets that are individually impaired*

| | Carrying value | |
|---|---|---|
| $ thousands | **2017** | 2016 |
| Outstanding premiums and trade receivables | **-** | - |
| **Total** | **-** | - |

### 29C FINANCING AND LIQUIDITY RISK

Financing and liquidity risk is the risk that the Group will not be able to meet its cash outflows or refinance debt obligations, as they fall due, because of lack of liquid assets or access to funding on acceptable terms. To mitigate financing and liquidity risk the Group maintains sufficient liquid assets to ensure that the Group can meet its debt obligations and other cash outflows on a timely basis.

*Financial liabilities and guarantees by contractual maturity*

The table below summarises the Group's financial liabilities and guarantees into relevant maturity groups based on the remaining period to the contractual maturity date at balance date. All amounts disclosed are contractual undiscounted cash flows that include interest payments and exclude the impact of netting agreements.

| $ thousands | **Carrying value** | **Total contractual cash flows** | **Less than one year** | **One to two years** | **Two to three years** | **Three to five years** |
|---|---|---|---|---|---|---|
| **As at 30 September 2017** | | | | | | |
| **Financial liabilities** | | | | | | |
| Trade payables | **19,069** | **19,069** | **19,069** | **-** | **-** | **-** |
| Reinsurance payables | **4,063** | **4,063** | **4,063** | **-** | **-** | **-** |
| Other payables | **2,682** | **2,682** | **2,682** | **-** | **-** | **-** |
| Derivative financial liabilities | **-** | **-** | **-** | **-** | **-** | **-** |
| Borrowings | **29,921** | **29,921** | **29,921** | **-** | **-** | **-** |
| **Total** | **55,735** | **55,735** | **55,735** | **-** | **-** | **-** |
| As at 30 September 2016 | | | | | | |
| **Financial liabilities** | | | | | | |
| Trade payables | 18,923 | 18,923 | 18,923 | - | - | - |
| Reinsurance payables | 4,445 | 4,445 | 4,445 | - | - | - |
| Other payables | 3,164 | 3,164 | 3,164 | - | - | - |
| Derivative financial liabilities | 735 | 735 | 735 | - | - | - |
| **Total** | 27,267 | 27,267 | 27,267 | - | - | - |

## 29 RISK MANAGEMENT (continued)

### 29D FAIR VALUE OF FINANCIAL ASSETS AND LIABILITIES

Refer to Note 28B, which discusses the fair value of financial assets and liabilities.

### 29E DERIVATIVE FINANCIAL INSTRUMENTS

The Group utilises derivative financial instruments to reduce investment risk. Specifically, derivatives are used to achieve cost effective short-term re-weightings of asset class, sector and security exposures and to hedge portfolios, as an economic hedge, when a market is subject to significant short-term risk.

Derivative financial instruments used by the Group are interest rate swaps. Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently remeasured at their fair value. The fair values of interest rate swaps are calculated by discounting estimated future cash flows based on the terms and maturity of each contract using market interest rates. The average interest rate is based on the outstanding balances at the start of the financial year.

The table below details the notional principal amounts (amounts used to calculate payments made on swap contracts), fair values and remaining terms of interest rate swap contracts outstanding as at the reporting date:

| | **Average contracted fixed interest** | | **Notional principal amount** | | **Fair value** | |
|---|---|---|---|---|---|---|
| | **2017** | 2016 | **2017** | 2016 | **2017** | 2016 |
| | % | | $ thousands | | $ thousands | |
| Less than 1 year | **0%** | 0% | **25,249** | 29,419 | **166** | (735) |
| 1 to 2 years | **0%** | 0% | **-** | - | **-** | - |
| 2 to 5 years | **2%** | 2% | **20,580** | 12,000 | **65** | 57 |
| Over 5 years | **0%** | 0% | **-** | - | **-** | - |
| | | | **45,829** | 41,419 | **231** | (678) |

### 29F SENSITIVITY ANALYSIS

The analysis below demonstrates the impact of changes in interest rates, exchange rates and equity prices on profit after tax and equity on continuing business. The analysis is based on changes in economic conditions that are considered reasonably possible at the reporting date. The potential impact is assumed as at the reporting date.

*(i) Interest rate*

The impact of a 50 basis point change in New Zealand and international interest rates as at the reporting date on profit after tax and equity is included in the tables below. The sensitivity analysis assumes changes in interest rates only. All other variables are held constant.

| | **2017** | | 2016 | |
|---|---|---|---|---|
| | **Impact on:** | | Impact on: | |
| $ thousands | **Profit after tax** | **Equity** | Profit after tax | Equity |
| **Change in variables** | | | | |
| + 50 basis points | **(511)** | **(511)** | (515) | (515) |
| - 50 basis points | **409** | **409** | 469 | 469 |

This analysis assumes that the sensitivity applies to the closing market yields of fixed interest investments. A parallel shift in the yield curve is assumed.

The risks assumed and methods used for deriving sensitivity information and significant variables have been applied consistently over the reporting period included in the analysis.

## 29 RISK MANAGEMENT (continued)

*(ii) Foreign currency*

The following tables demonstrate the impact of a 10% movement of currency rates against the New Zealand dollar on profit after tax and equity. The analysis assumes changes in foreign currency rates only, with all other variables held constant. The potential impact on the profit and equity of the Group is due to the changes in fair value of currency sensitive monetary assets and liabilities as at the reporting date.

| | **2017** | | 2016 | |
|---|---|---|---|---|
| | **Impact on:** | | Impact on: | |
| $ thousands | **Profit after tax** | **Equity** | Profit after tax | Equity |
| **Change in variables** | | | | |
| 10% appreciation of New Zealand dollar | **292** | **(2,380)** | 86 | (2,284) |
| 10% depreciation of New Zealand dollar | **(357)** | **2,909** | (105) | 2,791 |

The dollar impact of the change in currency movements is determined by applying the sensitivity to the value of the international assets.

The risks assumed and methods used for deriving sensitivity information and significant variables have been applied consistently over the reporting period included in the analysis.

*(iii) Equity price*

Equity price risk is the risk that the fair value of equities will decrease as a result of changes in levels of equity indices and the value of individual stocks. The Group does not hold any listed equities at fair value through profit or loss (2016: nil).

*(iv) Other price*

Other price sensitivity includes sensitivity to unit price fluctuations. Unit price risk is the risk that the fair value of investments in property fund units and international equities held in unit trusts will decrease as a result of changes in the value of these units.

The following tables demonstrate the impact of a 10% movement in the value of property funds and other unit trusts on the profit after tax and equity. The potential impact is assumed as at the reporting date.

| | **2017** | | 2016 | |
|---|---|---|---|---|
| | **Impact on:** | | Impact on: | |
| $ thousands | **Profit after tax** | **Equity** | Profit after tax | Equity |
| **Change in variables** | | | | |
| + 10% property funds and other unit trusts | **2** | **2** | 2 | 2 |
| - 10% property funds and other unit trusts | **(2)** | **(2)** | (2) | (2) |

The risks assumed and methods used for deriving sensitivity information and significant variables have been applied consistently over the two reporting periods included in the analysis.

# NOTES TO THE FINANCIAL STATEMENTS

## 30 CAPITAL RISK MANAGEMENT

The Group's objective when managing capital is to ensure that the level of capital is sufficient to meet the Group's statutory solvency obligations including on a look forward basis to enable it to continue as a going concern in order to meet the needs of its policyholders, to provide returns for shareholders, and to provide benefits for other stakeholders of the Group.

The Group's capital resources include shareholders' equity.

| $ thousands | Note | **2017** | 2016 |
|---|---|---|---|
| Tower shareholder equity | | **214,419** | 222,578 |
| Standby credit facility (undrawn) | 22 | **20,000** | 50,000 |
| **Total capital resources** | | **234,419** | 272,578 |

The Group measures adequacy of capital against the Solvency Standards for Non-life Insurance Business (the solvency standards) published by the Reserve Bank of New Zealand (RBNZ) alongside additional capital held to meet RBNZ minimum requirements and any further capital as determined by the Board.

The Group is required by RBNZ to maintain a minimum solvency margin of no less than $50.0 million (2016: $50.0 million) in Tower Insurance Limited. The actual solvency capital as determined under the solvency standards is required to exceed the minimum solvency capital level by at least this amount.

During the year ended 30 September 2017 the Group complied with all externally imposed capital requirements.

The Group holds assets in excess of the levels specified by the various solvency requirements to ensure that it continues to meet the minimum requirements under a reasonable range of adverse scenarios. The Group’s capital management strategy forms part of the Group’s broader strategic planning process overseen by the Audit and Risk Committee of the Board.

## 31 OPERATING LEASES

| $ thousands | **2017** | 2016 |
|---|---|---|
| **As lessee** | | |
| Rent payable to the end of the lease terms are: | | |
| Not later than one year | **2,806** | 3,044 |
| Later than one year and not later than five years | **7,444** | 7,763 |
| Later than five years | **2,010** | 3,733 |
| | **12,260** | 14,540 |

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Operating lease payments are recognised as an expense in the periods the services are received over the period of the lease. Operating lease payments represent future rentals payable for office space under current leases. Initial leases were for an average of four years with rental rates reviewed every two to six years.

# NOTES TO THE FINANCIAL STATEMENTS

## 32 SUBSIDIARIES

The table below lists Tower Limited subsidiary companies and controlled entities. All entities have a balance date of 30 September.

| Name of company | Country Incorporated in | Holdings 2017 | Holdings 2016 | Nature of business |
|---|---|---|---|---|
| **Incorporated in New Zealand** | | | | |
| Tower Financial Services Group Limited | NZ | **100%** | 100% | Holding company |
| Tower Insurance Limited | NZ | **100%** | 100% | General insurance |
| Tower New Zealand Limited | NZ | **100%** | 100% | Management services |
| **Incorporated Overseas** | | | | |
| Tower Insurance (Cook Islands) Limited | Cook Islands | **100%** | 100% | General insurance |
| Tower Insurance (Fiji) Limited | Fiji | **100%** | 100% | General insurance |
| Tower Insurance (PNG) Limited | PNG | **100%** | 100% | General insurance |
| National Pacific Insurance Limited | Samoa | **71%** | 71% | General insurance |
| Tower Insurance (Vanuatu) Limited | Vanuatu | **100%** | 100% | General insurance |

## 33 TRANSACTIONS WITH RELATED PARTIES

### 33A KEY MANAGEMENT PERSONNEL COMPENSATION

The remuneration of key management personnel during the year was as follows:

| $ thousands | Note | 2017 | 2016 |
|---|---|---|---|
| Salaries and other short term employee benefits paid | | **4,244** | 4,219 |
| Independent director fees | | **509** | 565 |
| | | **4,753** | 4,784 |

Information regarding individual director and executive compensation is provided in the Corporate Governance section of the annual report.

### 33B LOANS TO KEY MANAGEMENT PERSONNEL

There have been no loans made to directors of the Company and other key management personnel of the Group, including their personally related parties (2016: nil).

### 33C OTHER TRANSACTIONS WITH KEY MANAGEMENT PERSONNEL

Key management hold various policies and accounts with Tower Group companies. These are operated in the normal course of business on normal customer terms.

# NOTES TO THE FINANCIAL STATEMENTS

## 34 CONTINGENT LIABILITIES

The Group is occasionally subject to claims and disputes as a commercial outcome of conducting insurance business. Provisions are recorded for these claims or disputes when it is probable that an outflow of resources will be required to settle any obligations. Best estimates are included within claims reserves for any litigation that has arisen in the usual course of business.

Under the Fairfax mutual termination agreement, a break fee of $1.57 million is payable to Fairfax if another party completes an acquisition of Tower by 31 August 2018.

The Group has no other contingent liabilities (2016: nil).

## 35 CAPITAL COMMITMENTS

The Group has no capital commitments at reporting date (2016: nil).

## 36 SUBSEQUENT EVENTS

**Capital raise process**

The Tower Board has announced it will undertake a capital raising process commencing 14 November 2017. The capital raise will be by way of a fully underwritten, renounceable rights issue. An amount of $70.8 million gross of fees will be raised, with rights offered at a ratio of 1 for every 1 ordinary shares held on the record date of 22 November 2017. It is expected new shares will be allotted and quoted on NZX and ASX in December 2017. Capital will be utilised to repay the BNZ banking facility partially drawn in May 2017 and to allow accelerated growth in Tower's strategy.

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

On 7 November 2017, Tower advised that the SIA with Suncorp had passed its end date and had been terminated. Suncorp subsequently announced that as a result, it would no longer be proceeding with its appeal of the Commerce Commission's decision to decline its application to acquire Tower.

Following Suncorp's announcement, the Tower Board withdrew its cross appeal against the Commerce Commission's decision.

# *Independent auditor's report*

To the shareholders of Tower Limited

The financial statements comprise:

- the consolidated balance sheet as at 30 September 2017;
- the consolidated income statement for the year then ended;
- the consolidated statement of comprehensive income for the year then ended;
- the consolidated statement of changes in equity for the year then ended;
- the consolidated statement of cash flows for the year then ended; and
- the notes to the financial statements, which include a summary of general accounting policies.

## *Our opinion*

In our opinion, the financial statements of Tower Limited (the Company), including its subsidiaries (the Group), present fairly, in all material respects, the financial position of the Group as at 30 September 2017, its financial performance and its cash flows for the year then ended in accordance with New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS) and International Financial Reporting Standards (IFRS).

## *Basis for opinion*

We conducted our audit in accordance with International Standards on Auditing (New Zealand) (ISAs NZ) and International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the financial statements* section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

We are independent of the Group in accordance with Professional and Ethical Standard 1 (Revised) *Code of Ethics for Assurance Practitioners* (PES 1) issued by the New Zealand Auditing and Assurance Standards Board and the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with these requirements.

Our firm carries out other services for the Group in the areas of solvency return assurance and agreed upon procedures. The provision of these other services has not impaired our independence as auditor of the Group. In addition, certain partners and employees of our firm may deal with Tower Limited and the Group on normal terms within the ordinary course of trading activities of Tower Limited and the Group. These matters have not impaired our independence. We have no other interests in Tower Limited or the Group.

## *Our audit approach*

### Overview


An audit is designed to obtain reasonable assurance whether the financial statements are free from material misstatement.

Overall group materiality: $3,068 thousand, which represents approximately 1% of premium revenue.

We chose premium revenue as the benchmark because, in our view, it is a key financial statement metric used in assessing the performance of the Group and is not as volatile as other profit and loss measures, and is a generally accepted benchmark. The 1% is based on our professional judgement, noting that it is also within the range of commonly accepted revenue related thresholds.

The following have been determined as key audit matters:

- Outstanding claims and related reinsurance and other recoveries
- Recoverability of the deferred tax asset

### Materiality

The scope of our audit was influenced by our application of materiality.

Based on our professional judgement, we determined certain quantitative thresholds for materiality, including the overall Group materiality for the financial statements as a whole as set out above. These, together with qualitative considerations, helped us to determine the scope of our audit, the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and in aggregate on the financial statements as a whole.

### Audit scope

We designed our audit by assessing the risks of material misstatement in the financial statements and our application of materiality. As in all of our audits, we also addressed the risk of management override of internal controls including among other matters, consideration of whether there was evidence of bias that represented a risk of material misstatement due to fraud.

We tailored the scope of our audit in order to perform sufficient work to enable us to provide an opinion on the financial statements as a whole, taking into account the structure of the Group, the accounting processes and controls, and the industry in which the Group operates.

Our Group audit scope focused on the most financially significant subsidiary, which contributes 80% of the Group's premium revenue. We performed further audit procedures over the balances and transactions of the non-significant subsidiaries and the consolidation of the Group's subsidiaries.

## *Key audit matters*

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current year. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

| Key audit matter | How our audit addressed the key audit matter |
|---|---|

**1) Outstanding claims and related reinsurance and other recoveries from the Earthquake Commission (EQC) and Peak Re**

This is a key audit matter because of the complexity involved in the estimation process and the significant judgements that management make in determining the balances.

Notes 8, 20 and 27 to the financial statements describe the elements of the outstanding claims, related reinsurance and other recoveries and assumptions used in the calculation.

***(a) Outstanding claims ($181,156 thousand)***

***Central estimate of expected present value of future payments for claims incurred***

The valuation of outstanding claims involves significant judgement given the inherent uncertainty in the calculation of the central estimate of the expected present value of future payments for claims incurred (central estimate).

In particular, judgement arises over the estimation of payments for claims that have been incurred at the reporting date but have not yet been reported to the Group, or claims that have been reported but there is uncertainty over the amount which will be settled.

This estimate relies on the quality of underlying data, including historical claims data, and the application of complex and subjective actuarial models and methodologies, judgements and assumptions about future events.

Our audit procedures included the following:

- Re-performing key actuarial data reconciliations by agreeing claims data to the general ledger.
- Inspecting a sample of claims paid during the year to check that they were supported by appropriate documentation and approved within delegated authority limits.
- Testing the historical claims data by:
  - evaluating the design and effectiveness of controls over the processing of claims,
  - for a sample of claims outstanding at year end, agreeing to supporting documents.
- We utilised our actuarial specialists to assist us with:
  - evaluating the actuarial models and methodologies by comparing with generally accepted models and methodologies applied in the sector and with the prior year,
  - assessing key actuarial judgements and assumptions by comparing with our expectations based on the Group's experience, our own sector knowledge and independently observable trends, and
  - considering the work and findings of the external independent actuaries engaged by the Group.

***Risk margin***

Outstanding claims include a risk margin that allows for the inherent uncertainty in the central estimate of the future claim payments. In determining the risk margin, the Group makes judgements about the volatility of each class of business written and the correlation between each division and between different geographical locations.

With the assistance of our actuarial specialists we assessed the Group's approach to determining the risk margin by comparing to known industry practices and the Actuaries Institute recommended framework. In particular we focused on the assessed level of uncertainty in the central estimate.

We have no matters to report from the procedures performed.

***(b) Reinsurance and other recoveries from EQC ($65,100 thousand) and Peak Re ($43,750 thousand)***

Significant management judgement is required to value:

- expected recoveries from EQC in respect of land damage and building costs, as these recoveries are subject to agreement with EQC, and
- reinsurance recoveries from Peak Re, as these are dependent upon the outcome of a legal arbitration process.

The expected recoveries from EQC are related to the Canterbury earthquakes, and require judgement and actuarial expertise to evaluate the attribution of claims cost between the major earthquake events, in particular the September 2010 and February 2011 events.

We assessed management's approach to estimate the recoveries from EQC. We reviewed correspondence with EQC and held discussions with management, lawyers and external independent actuaries to understand assumptions, including the attribution of losses to the different Canterbury earthquake events, used to establish the right to recovery. We compared these assumptions with sector peers and sought evidence for any significant variances.

For reinsurance recoveries from Peak Re, we discussed with management the status of the arbitration process. We reviewed the legal correspondence between the Group and Peak Re lawyers and held discussions with the lawyers advising the Group.

We have no matters to report from the procedures performed.

***2) Recoverability of the deferred tax asset***

The Group has a deferred tax asset balance of $32,745 thousand, of which $26,958 thousand relates to deferred tax assets arising from past tax losses. We focused on the deferred tax asset from tax losses as its recoverability is sensitive to the Group's expected future profitability and its entitlement to offset these losses against future profits. Significant management judgement is involved in forecasting future taxable profits which are inherently uncertain.

Refer to note 10 to the financial statements.

We evaluated the progress made by management in improving the profitability of the business in recent periods, which includes the remediation of the causes of past losses through, amongst other things, assessment of the Canterbury earthquakes claims and related reinsurance and other recoveries (assessment of the recoverability of the receivables from EQC and Peak Re) and other expense reduction and income initiatives. We noted that progress has been made in relation to each of these matters.

We assessed the operational plan used in the deferred tax asset recoverability assessment by comparing previous business plans with actual results and assessed the appropriateness of the assumptions used in the operational plan.

We used our tax specialist to assess whether the Group is entitled to offset the tax losses against future profits.

We have no matters to report from the procedures performed.

## *Information other than the financial statements and auditor's report*

The Directors are responsible for the annual report. Our opinion on the financial statements does not cover the other information included in the annual report and we do not express any form of assurance conclusion on the other information.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed on the other information that we obtained prior to the date of this auditor's report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

## *Responsibilities of the Directors for the financial statements*

The Directors are responsible, on behalf of the Company, for the preparation and fair presentation of the financial statements in accordance with NZ IFRS and IFRS, and for such internal control as the Directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Directors are responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Directors either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

## *Auditor's responsibilities for the audit of the financial statements*

Our objectives are to obtain reasonable assurance about whether the financial statements, as a whole, are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs NZ and ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located at the External Reporting Board's website at:
https://www.xrb.govt.nz/standards-for-assurance-practitioners/auditors-responsibilities/audit-report-1/

This description forms part of our auditor's report.

*Who we report to*

This report is made solely to the Company's shareholders, as a body. Our audit work has been undertaken so that we might state those matters which we are required to state to them in an auditor's 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 Company and the Company's shareholders, as a body, for our audit work, for this report or for the opinions we have formed.

The engagement partner on the audit resulting in this independent auditor's report is Karl Deutschle.

For and on behalf of:

PricewaterhouseCoopers

Chartered Accountants
14 November 2017

Auckland

# 2017 full year results and announcement of entitlement offer

## Tower Limited investor presentation

14 November 2017

# Disclaimer

**Disclaimer**
This presentation has been prepared by Tower Limited (the "Company"). This presentation has been prepared to provide information on Tower's business and in relation to the proposed rights offer of fully paid ordinary shares (the "New Shares") in the Company to eligible shareholders under clause 19 of Schedule 1 of the Financial Markets Conduct Act 2013 and ASIC Instrument 16-0218 (the "Offer").

**Information**
This presentation contains summary information about the Company and its activities which is current as at the date of this presentation. The information in this presentation is of a general nature and does not purport to be complete nor does it contain all the information which a prospective investor may require in evaluating a possible investment in the Company or that would be required in a product disclosure statement for the purposes of the Financial Markets Conduct Act 2013. The historical information in this presentation is, or is based upon, information that has been released to NZX Limited ("NZX"). This presentation should be read in conjunction with the Company's other periodic and continuous disclosure announcements, which are available at www.nzx.com.

**NZX and ASX**
The new Shares have been accepted for quotation by NZX and will be quoted on the NZX Main Board upon completion of allotment procedures. The NZX Main Board is a licensed market under the Financial Markets Conduct Act 2013. However, NZX accepts no responsibility for any statement in this presentation. Application will be made to quote the new shares on ASX and Tower expects the new Shares will be quoted upon completion of allotment procedures. However, ASX accepts no responsibility for any statement in this presentation.

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This presentation is for information purposes only and is not financial or investment advice or a recommendation to acquire the Company's securities, and has been prepared without taking into account the objectives, financial situation or needs of individuals. Before making an investment decision, prospective investors should consider the appropriateness of the information having regard to their own objectives, financial situation and needs and consult an NZX Participant, or solicitor, accountant or other professional adviser if necessary.

**Past performance**
Any past performance information given in this presentation is given for illustrative purposes only and should not be relied upon as (and is not) an indication of future performance.

**Future performance**
This presentation may contain certain "forward-looking statements" such as indications of, and guidance on, future earnings and financial position and performance. Forward-looking information is inherently uncertain and no assurance can be given that actual outcomes will not materially differ from the forward looking statements.

Disclaimer: To the maximum extent permitted by law, the Company and its officers, advisers and affiliates will not be liable (whether in tort (including negligence) or otherwise) to you or any other person in relation to this presentation.

# Executive summary

**Michael Stiassny**
Chairman

# Executive summary

**Vero strategic discussions**

- After considering various structural options in late 2016, Tower received two unsolicited offers for 100% of the company's shares
- Tower's Board accepted Vero's offer, however, the Commerce Commission declined approval
- The Scheme Implementation Agreement (SIA) has passed its end date and was terminated by Tower on 6 November 2017
- Vero and Tower have since withdrawn their Commerce Commission appeals

**Validated balance sheet and capital structure**

- An extensive, independent review of Tower's solvency capital has been conducted
- Tower's Board has determined that an additional $70.8 million capital is required to enable investment in the business and manage inherent balance sheet risks
- Tower's Board has elected to create an additional risk margin for Canterbury claims of $10m over and above the provision of the Appointed Actuary. This is currently equivalent to a probability of sufficiency between the 80-85th percentile and will be released as Canterbury outstanding claims run off

**Equity raise**

- $70.8 million capital to be raised via pro-rata renounceable entitlement offer
- Issue price of NZ$0.42 representing a 29% discount to the theoretical ex-rights price
- Ratio of 1 New share for every 1 Existing share held
- Vero has committed to take up its full entitlement under the Offer

# Positive trends continue in FY17

**Momentum picks up pace in FY17**

- Significant improvements achieved in core metrics, including policy and premium growth, claims control and expense reduction, however, an unprecedented number of large natural events have affected underlying result
- Tower has reported a full year loss of $8m, a $13.5m improvement on the prior year

**Solid progress in finalising Canterbury earthquake claims**

- The number of open Canterbury Earthquake claims reduced by 241 in FY17
- Tower's Board has elected to create an additional risk margin for Canterbury claims of $10m.

**Positive short-term and medium-term outlook**

- Investment in digital and IT required to accelerate the solid progress made in transforming into a challenger brand

**Committed to efficient capital management and payment of dividend**

- Tower's Board and management team are strongly committed to paying dividends and to the efficient management of capital
- Tower's Board will review the dividend policy and look to recommence dividends in FY18


# Overview of Tower

**Richard Harding**
Chief Executive Officer

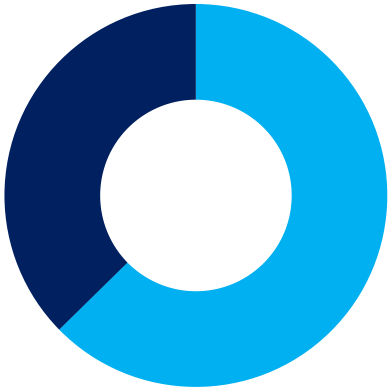
# A New Zealand and Pacific general insurer

TOWER

## Powerful platform for future growth as the #3 general insurer in New Zealand and one of the leading insurers in the Pacific

**$18 m**

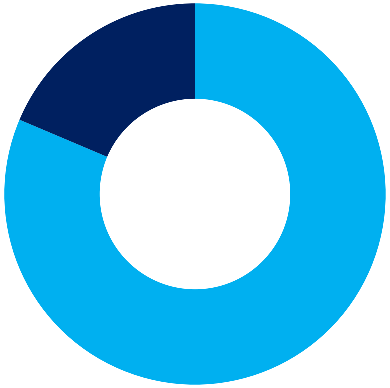
UNDERLYING **NPAT**[1]



- New Zealand 63%[2]
- Pacific Islands 37%[2]

**$312.4m**

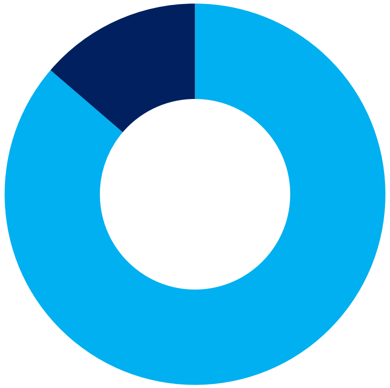
**GWP**



- New Zealand 81%
- Pacific Islands 19%

**479k**

**INFORCE POLICIES**



- New Zealand 86%
- Pacific Islands 14%

**Personal lines**

**GWP breakdown**

- House 38%
- Contents 16%
- Motor 31%
- Other 15%

Notes:
1. Excludes impact of the Canterbury and Kaikoura earthquakes, foreign tax credits lost and corporate transaction costs
2. Represents percentage of General Insurance underlying profit, excluding Corporate

# Clear strategic plan to grow Tower as the leading digital challenger brand

TOWER

## Traditional insurance

- Product and price transparency
- Simplification of policies and processes
- Underwriting refinement and capability build
- Claims process efficiency
- IT refresh, security, and regulatory requirements

## Digital distribution

- Digital self-service and engagement tools
- Partnerships through extended ecosystem
- Pacific operating model & growth plan
- Product and underwriting experimentation
- Data-driven insights for risk and decision-making

## Customer experience

- Setting it right at the moment of truth
- Predictive modelling and data analytics
- Simple and easy underwriting and claims experiences
- Automation and technology to accelerate claims
- Sophisticated pricing and risk understanding

## Challenger brand

- Personalised price, cover, and service
- Power to choose when and how to pay
- Community of loyalists and vocal advocates
- Innovative leadership (i.e. instant claims)
- Challenger culture, capability, and leadership

Solid foundations in place

**To achieve high performance, investment is required**

# Transformation will deliver step change in results

TOWER

## SIGNIFICANT BENEFITS

- ✓ Simple, customer focussed products
- ✓ Easy product experimentation and development
- ✓ Granular, automated pricing and underwriting
- ✓ Improved access and use of internal and external data
- ✓ Improved claims management
- ✓ Significant operational efficiencies and reduced costs
- ✓ Highly engaged employee group

## MEDIUM TERM TARGETS

**Challenger brand delivering:**

- **GWP growth of 4 – 6%**
- **Expense ratio <35%**
- **ROE of 12 – 14% through the cycle**

# Improving business performance

## Positive momentum in GWP growth with effective claims management and ongoing expense reduction

### ACHIEVEMENTS

- ✓ GWP growth of 5.8% achieved in core NZ portfolio
- ✓ Maintained claims discipline despite challenging environment
- ✓ $3.9m improvement in management expenses
- ✓ Solid progress being made in Canterbury with a further reduction of 241 open claims

| Key metrics | FY17 | FY16 |
|---|---|---|
| Total GWP | **$312.4m** | $303.2m |
| GWP growth in core NZ portfolio[1] | **5.8%** | 1.9% |
| Growth in policies in core NZ portfolio[1] | **12,441** | 2,509 |
| Claims expenses | **$131.6m** | $127.7m |
| Management and sales expenses | **$102.4m** | $106.3m |
| Underlying profit[2] | **$18m** | $20.1m |
| Reported loss after tax[3] | **$8m** | $21.5m |
| Open Canterbury earthquake claims | **323** | 564 |

1. Core portfolio is the NZ business and excludes ANZ legacy portfolio
2. "Underlying profit" does not have a standardised meaning prescribed by Generally Accepted Accounting Practice (GAAP) and may not be comparable to similar measures presented by other entities. While Tower has applied a consistent approach to measuring underlying profit in the current and comparative periods, it is not subject to audit or independent review. Tower uses underlying profit as an internal reporting measure as management believes it provides a better measure of Tower's underlying performance than reported profit, as it excludes large or non-recurring items that may obscure trends in the underlying performance of the Tower group. Tower considers that underlying profit is useful to investors as it makes it easier to compare the underlying financial performance of Tower between periods.
3. "Reported loss after tax" is calculated and presented in accordance with GAAP and is taken from Tower Limited's audited financial statements for the year ended 30 September 2017.

# Focus on customers delivers growth

TOWER

## Core book growing as a result of digital growth and strong retention

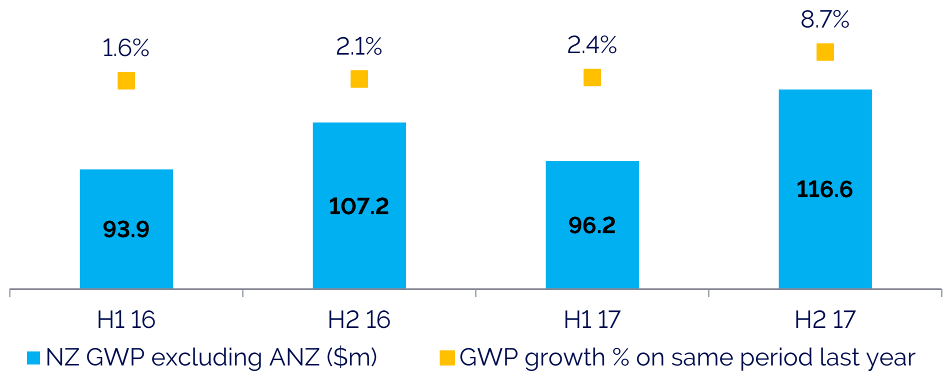
### ACHIEVEMENTS

- ✓ New digital program supporting core GWP growth in second half of 8.7% on prior year
- ✓ Tower Direct retention improved 2.0% points on prior year[2]
- ✓ New, simple and easy products improving lead conversion – currently 4% points above target

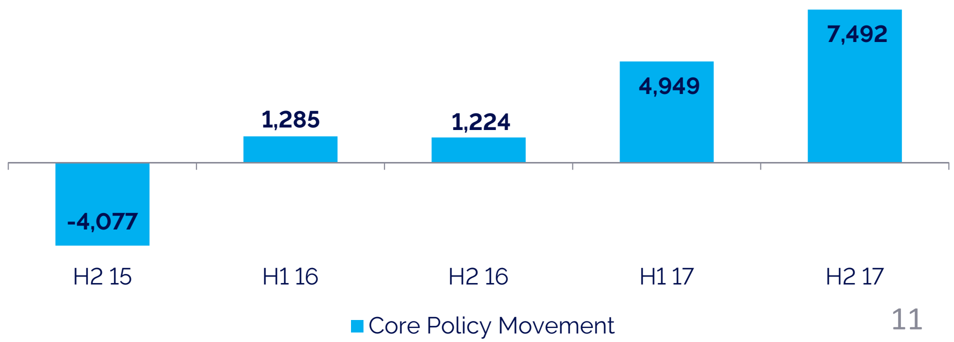
### INVESTMENT WILL ACCELERATE TRAJECTORY

- Unique customer experience
- Leverage new and existing partnerships to drive retention
- Innovative new offerings delivered through partners

### CORE[1] NEW ZEALAND GWP GROWTH




### POLICY GROWTH IN CORE[1] NEW ZEALAND PORTFOLIO




1. Core portfolio is the NZ business and excludes ANZ legacy portfolio
2. During 2017, Tower has changed its methodology for calculating retention rates. Using the previous methodology, retention for Tower Direct would be 81.7%, up 1.0% point on prior year.

# Digital continues to deliver

## Continued focus on digital capability and partnership delivers more customers

**ACHIEVEMENTS**

✓ Online sales increased from 9% of new business transactions in March 2016, to 30% in September 2017

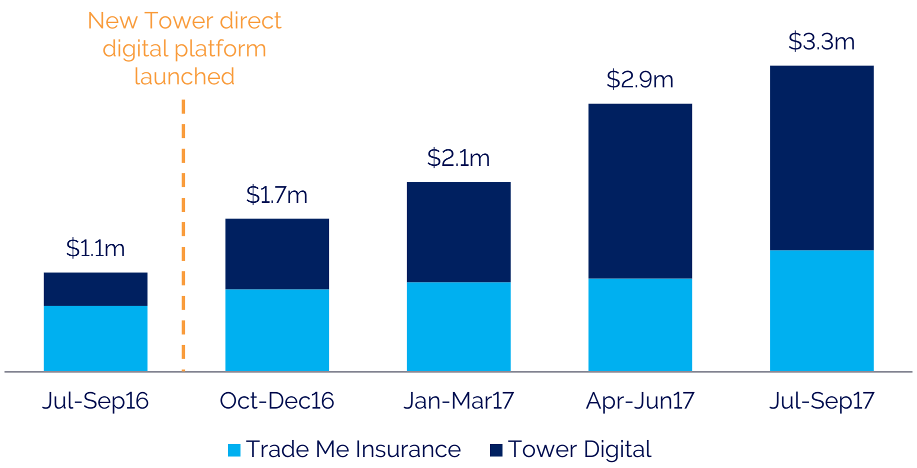
✓ Relaunch of new Trade Me Insurance platform, more than tripling net earned premium on prior year

✓ Tailored, targeted insurance offers available for customers using digital channels

**INVESTMENT WILL ACCELERATE TRAJECTORY**

- Online conversion rate optimisation and improvement
- Digital self-service, policy management and claims lodgement

**QUARTERLY NEW BUSINESS GWP ACROSS DIGITAL CHANNELS**



# Claims and underwriting update

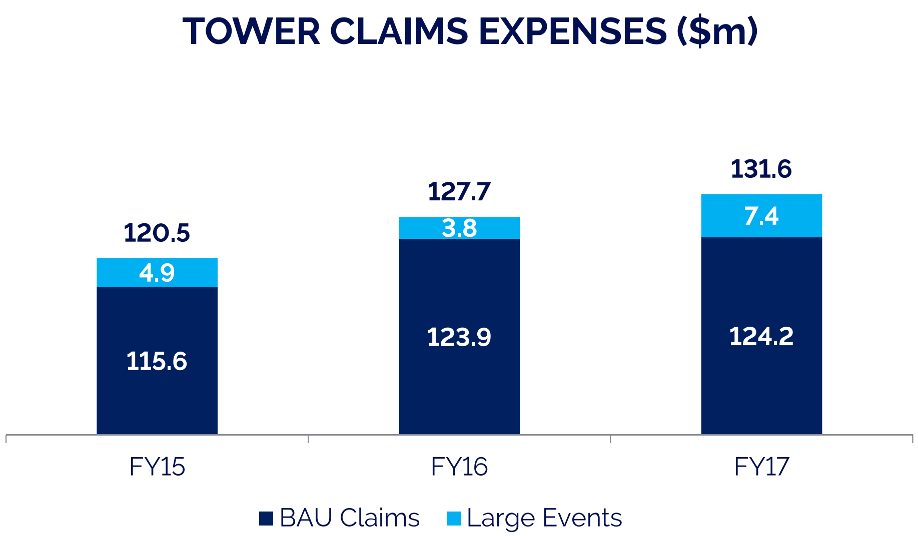
## Improvements in pricing, underwriting controlling claims costs despite industry wide inflation

### ACHIEVEMENTS

- ✓ Over 30 product updates, pricing reviews and targeted rate changes across all New Zealand portfolios
- ✓ Supply chain and preferred supplier initiatives delivered material savings
- ✓ New vehicle risk ratings further reducing claims frequency
- ✓ Excess changes significantly improved average claims costs

### INVESTMENT WILL ACCELERATE TRAJECTORY

- Sophisticated pricing and underwriting to offset claims inflation and improve long-term profitability
- Advanced rating algorithms and address based pricing
- Improved supply chain management and focus on fraud and claims leakage




Note: Claims costs includes BAU and large storm events, but excludes Christchurch and Kaikoura movements

# Kaikoura earthquake and storm events

## Highest number of natural event losses in over 25 years for Tower, excluding the Canterbury quakes

### IMPROVEMENTS IN FINANCIAL OUTCOMES

- ✓ Aggregate reinsurance cover helping to absorb large storm volatility
- ✓ $3.1m reduction of after tax impact of Kaikoura earthquakes from H1, from $7.2m to $4.1m
- ✓ $1.5m reduction of after tax impact of Ex-Cyclone Debbie and associated flooding in Edgecumbe since April 2017, from $3.6m to $2.1m

### KAIKOURA EARTHQUAKE

- ✓ 100% of Tower motor claims, 97% of contents and 79% of over-cap and other house claims finalised
- ✓ 99% of EQC contents claims and 82% of EQC home claims that relate to Tower's Kaikoura customers closed

Tower has experienced five large loss events during the year and has set up dedicated teams to help affected customers

| Event | Date | Incurred to Date | Ultimate Estimate + Risk Margin | Net of Reinsurance (before tax) | # of claims | Percentage finalised |
|---|---|---|---|---|---|---|
| Port Hills fire[1] | Feb-17 | $1.0m | $1.2m | $1.2m | 19 | 89% |
| Tasman Tempest | Mar-17 | $3.9m | $4.2m | $3.8m | 721 | 88% |
| Ex-Cyclone Debbie[2] | Apr-17 | $5.7m | $7.4m | $2.4m | 412 | 78% |
| Winter storm | Jul-17 | $1.3m | $1.6m | - | 232 | 49% |
| **Total storms and other** | | **$11.9m** | **$14.4m** | **$7.4m** | **1,384** | |
| Kaikoura earthquake | Nov-16 | $3.1m | $5.7m | $5.7m | 347 | 81% |

Notes:
1. All claims have had settlement offers presented to customers
2. There are 15 open claims in Edgecumbe. Whakatane Council is aiming for 90% of all people to be back in their properties by Christmas, and Tower is well on track to achieve this.

# Focus on costs

## Cost saving initiatives continue to deliver a reduction in expense base

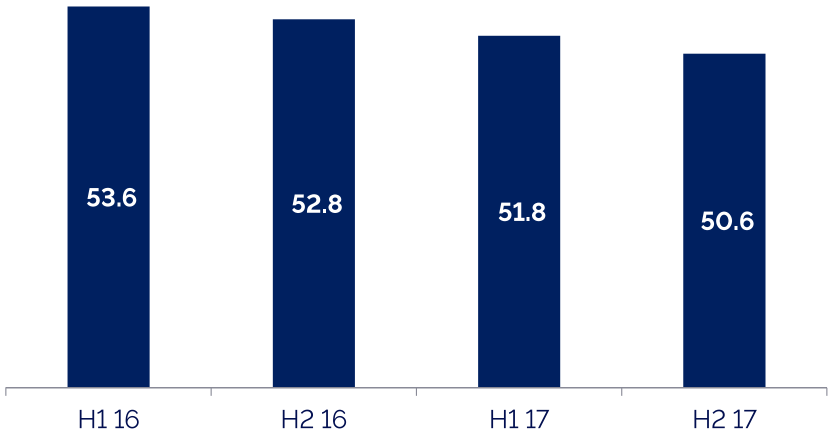
### ACHIEVEMENTS

- ✓ Increased focus on efficiency and productivity
- ✓ Significant saving through in-housing IT service desk and other key support functions
- ✓ Whole of business procurement review and close management of contract negotiations
- ✓ Some costs deferred as a result of acquisition and separation activity

### INVESTMENT WILL ACCELERATE TRAJECTORY

- IT simplification will deliver significant productivity gains and step-change in expense reduction
- Savings expected in FY18 to be reinvested in stabilising legacy systems and meeting compliance requirements

### MANAGEMENT EXPENSES




Note: Management expenses include commission cost, depreciation and amortisation and excludes corporate transaction costs.

# IT simplification

## Following the pause due to ownership, focus is now on delivery of IT simplification to drive growth and productivity

**ACHIEVEMENTS**

- ✓ Delivery of Tower digital solution
- ✓ Enhanced Trade Me Insurance platform
- ✓ Legacy IT systems stabilised

**INVESTMENT WILL ACCELERATE TRAJECTORY**

- Full digital and self service functionality
- Flexibility to update products and enable targeted, granular pricing
- Improved access and use of internal and external data
- Improved claims management and operational efficiencies

**NEXT STEPS**

- ✓ Selection of EIS to complete formal scoping and costing following comprehensive tender process
- ✓ Staged execution planned to enable Board to protect shareholder value
- ✓ EIS offer a modern insurance system that will improve productivity and customer experience
- ✓ Scoping and costing phase has commenced
- ✓ Board approval for appointment of EIS to undertake project will be sought once costs and timeline confirmed

# Financial performance

**Jeff Wright**
Chief Financial Officer

# FY17 Financial update

## Business performance remains in line with expectations. Results impacted by larger than usual number of natural events

### GROUP PROFIT SUMMARY (NZ$m)

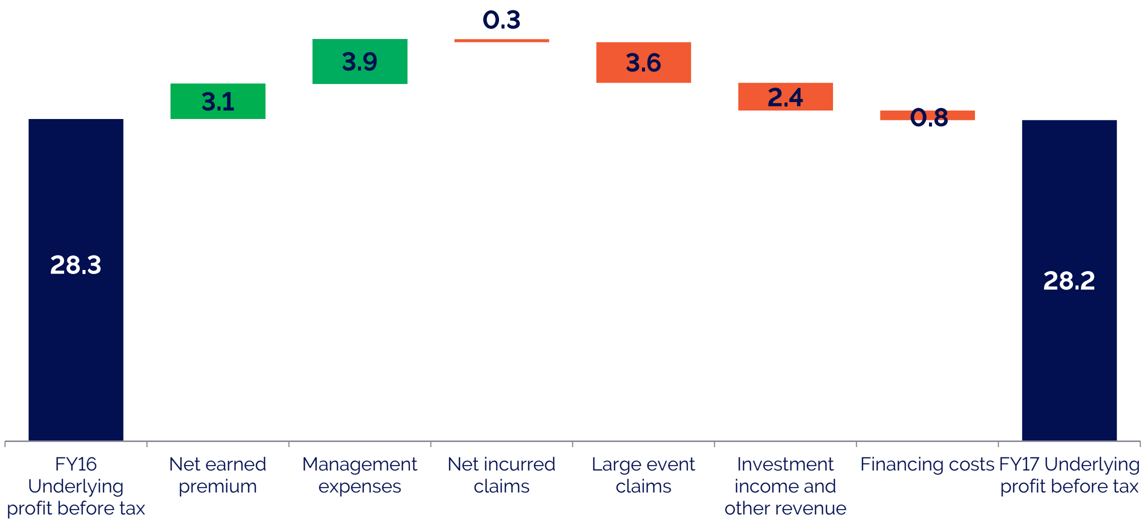
| $ million | | FY17 | FY16 |
|---|---|---|---|
| Gross written premium | | 312.4 | 303.2 |
| Gross earned premium | | 306.8 | 302.9 |
| Reinsurance costs | | (49.8) | (49.1) |
| **Net earned premium** | | **256.9** | **253.8** |
| Net claims expense | | (131.6) | (127.7) |
| Management and sales expenses | | (102.4) | (106.3) |
| **Underwriting profit** | | **22.9** | **19.8** |
| Investment revenue and other revenue | | 6.1 | 8.5 |
| Financing costs | | (0.8) | - |
| Underlying profit before tax | | 28.2 | 28.3 |
| Income tax expense | | (10.2) | (8.2) |
| **Underlying profit after tax** | | **18.0** | **20.1** |
| Canterbury impact | - Increase in outstanding claims | (11.4) | (25.3) |
| | - Additional risk margin | (7.2) | - |
| Kaikoura impact | | (4.1) | - |
| Impairment of intangibles | | - | (14.1) |
| Business in runoff | | 1.7 | - |
| Corporate transaction costs | | (3.1) | - |
| Foreign tax credits written off | | (1.9) | (2.2) |
| **Reported loss after tax** | | **(8.0)** | **(21.5)** |
| | | | |
| **Key ratios** | | | |
| Loss ratio | | 51.2% | 50.3% |
| Expense ratio | | 39.9% | 41.9% |
| Combined ratio | | 91.1% | 92.2% |

- Reported loss after tax reflects:
  - $11.4m impact from movement in Canterbury provisions
    - $9.8m increase in March
    - $1.6m increase in September
  - $7.2m impact from additional risk margin for Canterbury
  - $4.1m impact from Kaikoura earthquake
  - $3.1m impact from corporate transaction activity
- Underlying profit after tax of $18m affected by storm activity vs FY16 underlying profit after tax of $20.1m
  - $0.9m impact from Port Hills Fires
  - $2.7m impact from Tasman Tempest
  - $1.8m impact from Ex-Cyclone Debbie
- Pacific NPAT stable and in line with prior periods, excluding impact of Cyclone Winston in FY16
  - Reported profit in Pacific of $7.2m, compared to $5.5m for the prior year
- 2018 reinsurance program has been finalised on favourable premium terms, with limit of $790m and aggregate excess increased from $5m to $7m

# Movement in underlying profit

## Growth in premiums and lower management expenses offset by large events and lower investment income

**MOVEMENT IN UNDERLYING PROFIT BEFORE TAX** (NZ$m)




- Net earned premium higher due to growth in core book and improved retention
- Focus on costs has reduced management expenses
- Net incurred claims were flat, as initiatives to manage cost inflation have largely offset increasing claims frequency
- More large events this year compared to last year resulting in higher large events claims expense
- Reduced balances and lower interest rate environment has reduced investment income

# Pacific business remains steady

## The Pacific offers a solid platform with significant potential for Tower

**PACIFIC PROFIT SUMMARY** (NZ$m)

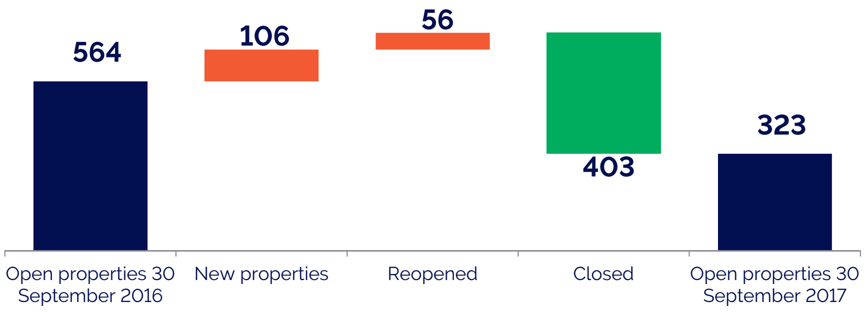
| $ million | FY17 | FY16 |
|---|---|---|
| Gross written premium | 58.2 | 59.3 |
| Gross earned premium | 57.6 | 58.6 |
| Reinsurance costs | (15.5) | (15.6) |
| **Net earned premium** | **42.1** | **43.1** |
| Net claims expense | (15.3) | (20.1) |
| Management and sales expenses | (15.6) | (15.0) |
| **Underwriting profit** | **11.3** | **8.0** |
| Investment revenue and other revenue | 0.9 | 1.2 |
| Underlying profit before tax | 12.2 | 9.2 |
| Income tax expense | (5.0) | (3.7) |
| **Underlying profit after tax** | **7.2** | **5.5** |

- YTD NPAT stable and in line with prior periods, excluding impact of Cyclone Winston in FY16
- Growth in Fiji, Vanuatu and Samoa offset by softening market and tightened approach to risk in Papua New Guinea
- Repricing of portfolios underway and enhanced underwriting capability in local teams

# Canterbury update

## Open claims and numbers of new over-cap claims are reducing, but uncertainty still remains

### MOVEMENT IN PROPERTIES (since Sep 2016)




- Reduction in new and reopened claims
  - 56 claims currently under litigation
  - 56 "Protocol 1" claims[3]
  - 211 claims moving towards settlement
- Additional claims continue to be received due to:
  - New EQC over-cap claims
  - Additional DFPP and accommodation claims as EQC finalise under-cap properties
- Reopened claims for additional payments and litigation

### RESERVING UPDATE

| (NZ$m) | Sep-17 | % of case estimates[2] | Mar-17 | % of case estimates[2] | Sep-16 | % of case estimates[2] |
|---|---|---|---|---|---|---|
| Case estimates | 58.9 | | 73.9 | | 93.2 | |
| IBNR/IBNER[1] | 34.4 | | 47.4 | | 44.0 | |
| Risk margin | 13.9 | | 18.2 | | 11.9 | |
| Additional risk margin | 10.0 | | - | | - | |
| Combined IBNR/IBNER/risk margin | 58.3 | 99% | 65.6 | 89% | 55.9 | 60% |
| **Gross outstanding claims** | **117.2** | | **139.5** | | **149.1** | |

- Challenging environment remains, with New Zealand insurers continuing to face ongoing risks as a result of Canterbury earthquakes
- Appointed Actuary recommended a further $1.6m after-tax strengthening in second half, bringing the full after tax impact to $11.4 million for the year
- Since March, case estimates have fallen as a result of closing claims. IBNR/IBNER/risk margin have also reduced as we obtain more certainty about outstanding claims

Notes:
1. IBNR / IBNER includes claims handling expenses
2. Ratio of IBNR / IBNER plus risk margin to case estimates
3. Protocol 1 claims are where EQC are managing repairs yet the total cost is over the EQC cap.

# Update on Peak Re and EQC

## Tower remains confident of recovery from Peak Re and EQC

### PEAK RE DISPUTE

- Tower is party to an arbitration process with Peak Re regarding an adverse development cover policy entered into in 2015 valued at $43.75m.
- Currently Tower anticipates the arbitration will take place in March 2018 with a decision by mid-2018.
- Tower remains confident that it will be successful but both the process and the hearing hold risk and collection of the owed amount is not certain. An adverse outcome could lead to a nil recovery due to the binary nature of the process.

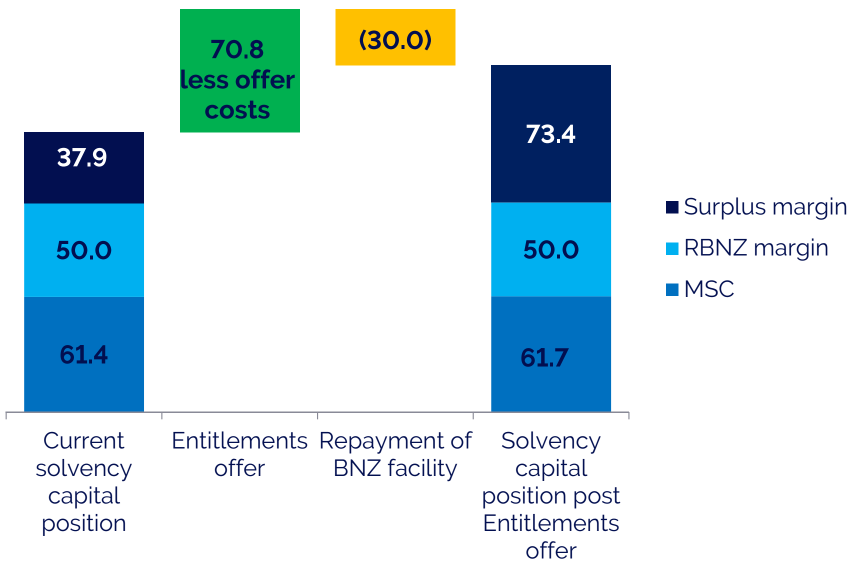
### EQC RECOVERIES

- Tower in consultation with its reinsurers is progressing its recovery program against the Earthquake Commission (EQC) in relation to the costs incurred due to building and land work following the 2010 and 2011 Canterbury earthquakes.
- Tower estimates the gross amount receivable due from EQC is significantly higher than $65.1 million ($13.5m for land and $51.6m for buildings), but has adopted this amount, which is the actuarial valuation of the Appointed Actuary. The method by which the actuarial valuation is completed recognises the inherent risk and uncertainty with recovery of the full gross amount. If the amount of $65.1m is received from EQC, an amount of $17.7 million (2016: $20.7 million) will be payable to reinsurers.
- To date, Tower along with IAG, have issued proceedings against the EQC seeking compensation for remediation of land damage with a court hearing expected in late 2018. Further litigation in regards to land is expected. Tower is also applying significant resources to the EQC building recovery program. Based on legal advice to date Tower is confident in its position in regards to its recovery program.
- Due to the nature of the claims and the potential for litigation or an alternate dispute resolution process, the actual recoveries may be higher or lower than anticipated.

# Capital requirement review

## Entitlement offer will strengthen solvency position to a long-term sustainable level

**TOWER INSURANCE LIMITED SOLVENCY POSITION** ($m)




Note: Solvency capital calculation based on $70.8m entitlement offer less offer costs

**MEDIUM-TERM CAPITAL REQUIREMENT**

- Tower's Board and management have confidently determined to invest in a sustainable future while recognising the inherent uncertainty faced by the industry relating to the Canterbury earthquakes
- Tower has undertaken a detailed review to determine the amount of capital required to strengthen its solvency capital position and enable investment for the future
- Tower has determined that additional capital of $70.8m is required, to address the inherent uncertainty faced by the business and to permit the signaled and ongoing reinvestment in Tower's NZ business
- In reaching this conclusion, the Board has engaged with Tower's Appointed Actuary, and independent, external advisers

**LONG-TERM CAPITAL VIEW**

- Historically, Tower has paid consistent dividends, reflecting the strength of Tower's underlying business and its inherently strong cash flow
- Tower's Board recognise the need for capital in the medium-term
  - Tower's Board and management team are strongly committed to paying dividends and to the efficient management of capital
  - Tower's Board will review the dividend policy and look to recommence dividends in FY18

# FY18 outlook

**Richard Harding**
Chief Executive Officer

# Tower outlook for FY18

| | |
|---|---|
| **Expect continuing gross written premium growth in NZ core book** | • Improving retention rates and current marketing campaign resulting in strong lead enquiry<br>• Positive momentum in digital distribution channel<br>• Continued pricing and product refinement to offset claims inflation and improve profitability |
| **Pacific offers significant potential** | • New operating model to improve risk management and underwriting discipline in key Pacific markets<br>• Repricing of portfolios to improve profitability |
| **Management expenses maintained** | • Maintain current expense level, with all savings expected in FY18 to be reinvested in stabilising legacy systems and meeting compliance requirements<br>• Step-change in expense reduction and productivity gains to be realised following implementation of new technology systems which is expected to yield benefits from FY19 |
| **Claims management improvements expected** | • Industry wide claims inflation expected to be offset by product updates, targeted rate/pricing changes and supply chain initiatives |
| **Investment in simplification will accelerate improvements in FY19 and beyond** | • Significant management focus will go into IT simplification and EIS implementation in FY18<br>• Expected to yield benefits from FY19 |
| **Intention to review dividend policy following capital raise** | • Tower's Board and management team are strongly committed to paying dividends and to the efficient management of capital<br>• Tower's Board will review the dividend policy and look to recommence dividends in FY18 |
| **Enhanced capital position** | • Completion of capital raise, along with continuing resolution of other legacy issues (Peak arbitration, EQC receivable and finalisation of Canterbury earthquake claims), will enable management to focus on execution of business plan |

# Entitlement offer

**Richard Harding**
Chief Executive Officer

# Equity raising terms and shareholder options

## Equity raising terms

| | |
|---|---|
| **Entitlement ratio** | • 1 New Share for every 1 Existing Share held |
| **Offer size** | • $70.8m |
| **Maximum New Shares to be issued** | • 168,662,150 |
| **Issue price** | • NZ$0.42 |
| **Offer discount** | • 29% to TERP[1] |
| **Eligibility** | • Available to persons recorded on Tower's share register at 7:00pm on 22 November 2017, with a registered address in New Zealand or Australia |
| **Ranking** | • New shares issued on completion of the Rights Offer will rank equally with Existing shares and will be quoted on the NZX and ASX |
| **Structure** | • Pro rata renounceable Rights Offer provides all Eligible Shareholders with the opportunity to participate |
| **Underwriting** | • The Offer is underwritten by Goldman Sachs New Zealand Limited |

## Shareholder options

| | |
|---|---|
| **Take up all or some Rights** | • You will be able to acquire Shares at the Issue Price of NZ$0.42 which is at a discount to the market price immediately prior to the announcement of the Rights Offer.<br>• If you take up all your rights you will maintain your proportional ownership of Tower after the Rights Offer |
| **Sell all or some Rights** | • If you wish to sell your Rights, you should contact an NZX Broker<br>• You will receive value for any Rights sold on-market<br>• You may be required to pay brokerage on the sale of your Rights |
| **Let Rights lapse** | • If you do nothing, your Rights will lapse and you will not be able to subscribe for any New Shares |

**If you do nothing, your Rights will lapse and you will not be able to subscribe for any New Shares or realise any other value for your Rights.**

**The Tower Board encourages you to either take up your Rights in full or sell your Rights on market**

Notes:
1. TERP is the theoretical ex rights price of $0.59 which is equal to the average price of 1 New Share at the Issue Price of $0.42 and 1 Existing Share at $0.76 being the last traded price as at 13 November 2017.

# Key risks to Tower

- Tower is subject to risk factors that are specific to its business activities and those of a more general nature. Any, or a combination, of these risk factors may have a material impact on Tower's business, operating and financial performance. These impacts can be negative or positive. This page describes some of the potential risks associated with Tower's business and an investment in its Shares. It does not purport to list every risk that may be associated with an investment in Shares now or in the future, and the occurrence of consequences of some of the risks described on this page are partially or completely outside the control of Tower, its Directors and management team.
- The selection of risks has been based on an assessment of a combination of the probability of the risk occurring and impact of the risk if it did occur. The assessment is based on the knowledge of the Directors as at the date of this document, but there is no guarantee or assurance that the importance of different risks will not change or other risks will not emerge.
- Before applying for Shares, you should satisfy yourself that you have a sufficient understanding of these matters and should consider whether Shares are a suitable investment for you, having regard to your own investment objectives, financial situation and particular needs (including financial and taxation issues). If you do not understand any part of this presentation or are in any doubt as to whether to invest in Shares, it is recommended that you seek professional guidance from your accountant, share broker, financial adviser, lawyer or other professional adviser before deciding whether to invest.

| *Risk* | *Description* |
|---|---|
| **Tower business performance** | • The insurance industry that Tower operates within involves the assumption of risk. Changes in frequency and severity of customer claims, which may result from inflation, natural disasters or other events, can affect Tower's capital position, consistency of earnings and the achievement of targets.<br>• The insurance industry is competitive, which may impact Tower's ability to acquire and retain business. Concentrations of risk occur due to relationships with partners, who may choose to put their business with other insurers. Kiwibank domestic general insurance business will transition into runoff in April 2018. ASB conducted a tender process for their credit card and retail travel insurance portfolios that Tower were not successful in retaining, this relationship will cease in April 2018. Tower is currently participating in a competitive RFI process with TSB to retain their domestic general insurance business and secure their retail travel insurance program.<br>• Risks exist around the implementation of Tower's IT simplification plan which, if not successful, may result in failure to achieve desired operational performance improvements and medium term financial targets. |
| **Canterbury earthquake claims** | • The scale and impact of the Canterbury Earthquakes is unprecedented for all affected general insurers in New Zealand and has led to Tower alone receiving over 16,000 claims.<br>• Tower has increased its ultimate incurred claims liabilities in respect of the four main Canterbury earthquakes that occurred on 4 September 2010; 22 February 2011; 13 June 2011 and 23 December 2011 from $792.0 million in September 2015 to $897.4 million in September 2017.<br>• Whilst Tower and its appointed actuary have conducted a comprehensive review in order to assess its Canterbury claims liabilities as accurately as possible, to a conservative statistical standard, the impact of further Canterbury claims, and the cost to close existing claims or re-opening of claims, remain a risk for the Tower business.<br>• Reinsurance relating to September 2010 and February 2011 Canterbury earthquakes has been exhausted, meaning Tower could be directly exposed to further developments. Reinsurance for the June 2011 and December 2011 events is unlikely to be fully utilised. |



- *Continued on next page*

# Key risks to Tower

- *Continued from prior page*

| *Risk* | *Description* |
|---|---|
| **PeakRe arbitration outcome** | • Tower is party to an arbitration process with Peak Re regarding an adverse development cover policy entered into in 2015 valued at $43.75m.<br>• Currently Tower anticipates the arbitration will take place in March 2018 with a decision by mid-2018. Tower remains confident that it will be successful but both the process and the hearing hold risk and collection of the owed amount is not certain. An adverse outcome could lead to a nil recovery due to the binary nature of the process. |
| **EQC Recoveries Program** | • Tower in consultation with its reinsurers is progressing its recovery program against the Earthquake Commission (EQC) in relation to the costs incurred due to building and land work following the 2010 and 2011 Canterbury earthquakes. Tower estimates the gross amount receivable due from EQC is significantly higher than $65.1 million ($13.5m for land and $51.6m for buildings), but has adopted this amount, which is the actuarial valuation of the Appointed Actuary. The method by which the actuarial valuation is completed recognises the inherent risk and uncertainty with recovery of the full gross amount. If the amount of $65.1m is received from EQC, an amount of $17.7 million (2016: $20.7 million) will be payable to reinsurers.<br>• To date, Tower along with IAG, have issued proceedings against the EQC seeking compensation for remediation of land damage with a court hearing expected in late 2018. Further litigation in regards to land is expected. Tower is also applying significant resources to the EQC building recovery program. Based on legal advice to date Tower is confident in its position in regards to its recovery program. Due to the nature of the claims and the potential for litigation or an alternate dispute resolution process, the actual recoveries may be higher or lower than anticipated. |
| **Potential strategic discussions** | • Tower and Vero Insurance New Zealand Limited entered into a scheme implementation agreement in June 2017 for the purchase by Vero of all Tower shares it did not already hold. In July 2017, the Commerce Commission declined Vero's clearance application. Vero and Tower each separately appealed that decision. Vero and Tower have since withdrawn their Commerce Commission appeals<br>• In addition, the Commerce Commission has made public comments in relation to its potential investigation under Section 47 of the New Zealand Commerce Act to review potential competition issues caused by Vero's acquisition of a 19.9% stake in Tower.<br>• The scheme implementation agreement (SIA) has passed its end date and was terminated by Tower on 6 November 2017.<br>• Shareholders should be aware that Tower may remain as a standalone listed NZ insurer or that Tower may be acquired by a third party.<br>• Vero has committed to take up its full entitlement under the Offer. In the event Vero sells its shares, it has agreed to procure any person acquiring its shareholding to take up its rights issue participation commitment |

# Offer timetable

## Key dates[1] for the rights offer are outlined below

| | |
|---|---|
| **Shares quoted "ex-rights" and Rights Trading commences on the NZX Main Board** | Tuesday 21 November |
| **Record date** | Wednesday 22 November |
| **Offer documents sent by** | Monday 27 November |
| **Right trading ceases** | Thursday 7 December |
| **Rights offer closes (and last date for receipt of renunciations)** | Wednesday 13 December |
| **New Shares allotted and commence trading** | Wednesday 20 December |

Notes:
1. These dates are subject to change. Tower reserves the right to amend the dates and times without prior notice, subject to applicable legal and regulatory requirements.

# Appendices

# New Zealand business improving

## Improvements in key focus areas offset by storm activity and large events

**NEW ZEALAND PROFIT SUMMARY** (NZ$m)

| $ million | FY17 | FY16 |
|---|---|---|
| Gross written premium | 254.2 | 243.9 |
| Gross earned premium | 249.1 | 244.3 |
| Reinsurance costs | (34.3) | (33.6) |
| **Net earned premium** | **214.8** | **210.8** |
| Net claims expense | (116.3) | (107.6) |
| Management and sales expenses | (85.2) | (88.5) |
| **Underwriting profit** | **13.2** | **14.7** |
| Investment revenue and other revenue | 4.6 | 5.7 |
| Underlying profit before tax | 17.8 | 20.4 |
| Income tax expense | (5.7) | (4.9) |
| **Underlying profit after tax** | **12.1** | **15.6** |

- Improvements in underlying business offset by natural events
- Increase in GWP on back of better growth in digital and retention initiatives
- Claims costs remain flat despite industry wide inflation
- Savings in management expenses

# Balance sheet
# Tower Group

| $ million | 30 September 17 | 30 September 16 | Movement $ | Movement % |
|---|---|---|---|---|
| Cash & call deposits | 102.9 | 92.2 | 10.6 | 11.5% |
| Investment assets | 167.9 | 188.6 | (20.6) | (10.9%) |
| Deferred acquisition costs | 21.0 | 20.0 | 1.0 | 4.9% |
| Intangible assets | 31.3 | 32.0 | (0.6) | (2.0%) |
| Other operational assets | 316.4 | 307.5 | 8.8 | 2.9% |
| **Total assets** | **639.5** | **640.3** | **(0.8)** | **(0.1%)** |
| Policy liabilities & insurance provisions | (336.0) | (361.0) | 25.0 | (6.9%) |
| External debt | (29.9) | 0.0 | (29.9) | 100.0% |
| Other operational liabilities | (57.8) | (55.3) | (2.5) | 4.5% |
| **Total liabilities** | **(423.7)** | **(416.3)** | **(7.4)** | **1.8%** |
| **Total equity** | **215.7** | **224.0** | **(8.2)** | **(3.7%)** |

# Reconciliation between underlying profit after tax and net profit after tax

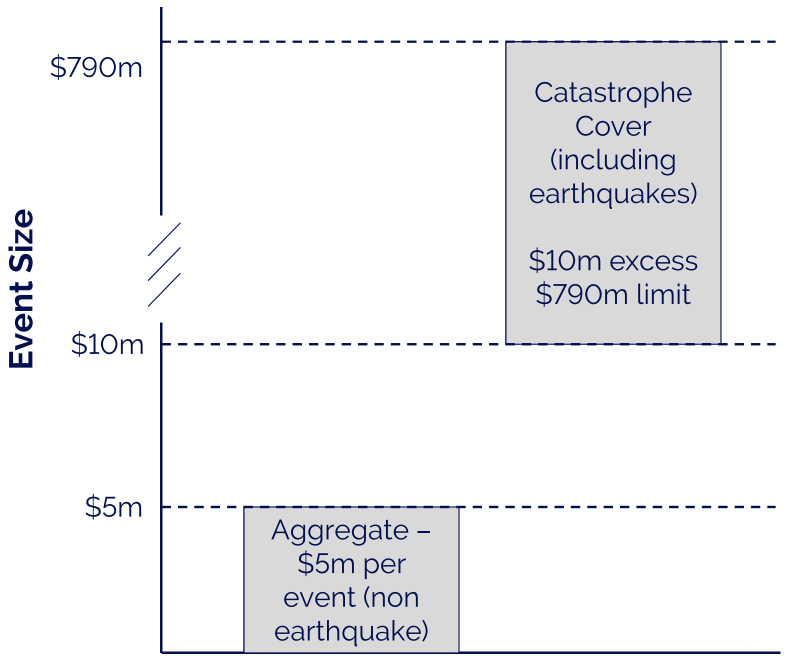
| $ million | FY17 underlying profit | Non-underlying items (1) | Claims handling expenses (2) | Other items (3) | FY17 reported profit |
|---|---|---|---|---|---|
| Gross written premium | 312.4 | | | | 312.4 |
| Gross earned premium | 306.8 | | | | 306.8 |
| Reinsurance costs | (49.8) | | | | (49.8) |
| **Net earned premium** | **256.9** | **0.0** | **0.0** | **0.0** | **256.9** |
| Net claims expense | (131.6) | (30.0) | (26.0) | | (187.6) |
| Management and sales expenses | (102.4) | (4.3) | 26.0 | (4.5) | (85.2) |
| **Underwriting profit** | **22.9** | **(34.2)** | **0.0** | **(4.5)** | **(15.8)** |
| Investment revenue and other revenue | 6.1 | | | 4.5 | 10.7 |
| Financing costs | (0.8) | | | | (0.8) |
| Underlying profit before tax | 28.2 | (34.2) | 0.0 | 0.0 | (6.0) |
| Income tax expense | (10.2) | 8.2 | | | (2.0) |
| **Underlying profit after tax** | **18.0** | **(26.0)** | **0.0** | **0.0** | |
| Canterbury impact - Increase in outstanding claims | (11.4) | 11.4 | | | |
| - Additional risk margin | (7.2) | 7.2 | | | |
| Kaikoura impact | (4.1) | 4.1 | | | |
| Business in runoff | 1.7 | (1.7) | | | |
| Corporate transaction costs | (3.1) | 3.1 | | | |
| Foreign tax credits written off | (1.9) | 1.9 | | | |
| **Reported loss after tax** | **(8.0)** | **0.0** | **0.0** | **0.0** | **(8.0)** |

1. Non-underlying items are shown separately in Tower's management reporting, yet included within 'net claims expense', 'management and sales expenses' and 'tax expense' (depending on the nature of the item) in the financial statements.
2. In Tower's management reporting, claims handling expenses are reported within 'management and sales expenses'. In the financial statements, claims handling expenses are reclassified to 'net claims expense'.
3. Certain items of revenue are netted off 'management and sales expenses' in Tower's management reporting, and are reclassified to 'other revenue' in the financial statements. This primarily relates to commission received by Tower.

# Reinsurance structure overview

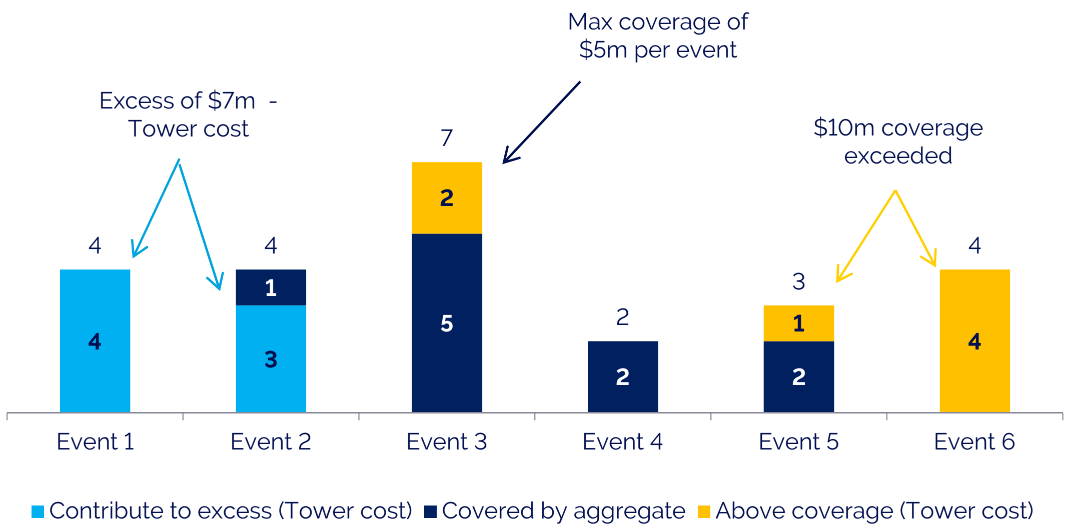
## The excess on the aggregate cover has increased to $7m and the limit on catastrophe cover increased to $790m

**STRUCTURE OVERVIEW (per event)**




**AGGREGATE COVER OVERVIEW FOR FY18**

- Minimum event size of $1m to qualify, max of $5m per event coverage
- $10m cover once $7m excess filled
- No coverage for earthquake in New Zealand



APPENDIX 7 – NZSX Listing Rules

**EMAIL: announce@nzx.com**

*Number of pages including this one (Please provide any other relevant details on additional pages)* **1**

# Notice of event affecting securities

*NZSX Listing Rule 7.12.2. For rights, NZSX Listing Rules 7.10.9 and 7.10.10.*
*For change to allotment, NZSX Listing Rule 7.12.1, a separate advice is required.*

| | |
|---|---|
| *Full name of Issuer* | **Tower Limited** |
| *Name of officer authorised to make this notice* | **David Callanan** |
| *Authority for event, e.g. Directors' resolution* | **Directors' resolution** |
| *Contact phone number* | **09 369 2235** |
| *Contact fax number* | **N/A** |
| *Date* | **14 / 11 / 2017** |

**Nature of event**
*Tick as appropriate*

| | |
|---|---|
| *Bonus Issue* | ☐ |
| *If ticked, state whether: Taxable* | ☐ |
| */ Non Taxable* | ☐ |
| *Conversion* | ☐ |
| *Interest* | ☐ |
| *Rights Issue Renouncable* | ☑ |
| *Rights Issue non-renouncable* | ☐ |
| Capital change | ☐ |
| Call | ☐ |
| Dividend | ☐ |
| If ticked, state whether: Interim | ☐ |
| Full Year | ☐ |
| Special | ☐ |
| DRP Applies | ☐ |

**EXISTING securities affected by this**

*If more than one security is affected by the event, use a separate form.*

| | |
|---|---|
| *Description of the class of securities* | **Ordinary shares** |
| *ISIN* | **NZTWRE0011S2** *If unknown, contact NZX* |

**Details of securities issued pursuant to this event**

*If more than one class of security is to be issued, use a separate form for each class.*

| | |
|---|---|
| *Description of the class of securities* | **Ordinary shares** |
| *ISIN* | **NZTWRE0011S2** *If unknown, contact NZX* |
| *Number of Securities to be issued following event* | **168,662,150** |
| *Minimum Entitlement* | **N/A** |
| *Ratio, e.g 1 for 2* | **1** *for* **1** |
| *Conversion, Maturity, Call Payable or Exercise Date* | N/A *Enter N/A if not applicable* |
| *Treatment of Fractions* | **N/A** |
| *Tick if pari passu* | ✓ |
| *OR provide an explanation of the ranking* | |
| *Strike price per security for any issue in lieu or date Strike Price available.* | N/A |

***Monies Associated with Event***

*Dividend payable, Call payable, Exercise price, Conversion price, Redemption price, Application money.*

*In dollars and cents*

| | |
|---|---|
| *Amount per security (does not include any excluded income)* | **$0.420** |
| Source of Payment | N/A |
| *Excluded income per security (only applicable to listed PIEs)* | |
| *Currency* | **NZD** |
| *Total monies* | **$70.8 million** |

Supplementary dividend details - NZSX Listing Rule 7.12.7

| | |
|---|---|
| *Amount per security in dollars and cents* | N/A |
| ***Date Payable*** | N/A |

***Taxation***

*Amount per Security in Dollars and cents to six decimal places*

| | |
|---|---|
| *In the case of a taxable bonus issue state strike price* | N/A |
| Resident Withholding Tax | N/A |
| Imputation Credits (Give details) | N/A |
| Foreign Withholding Tax | N/A |
| FDP Credits (Give details) | N/A |

***Timing*** (Refer Appendix 8 in the NZSX Listing Rules)

| | |
|---|---|
| ***Record Date 7pm*** *For calculation of entitlements -* | **22 November 2017** |
| ***Application Date*** *Also, Call Payable, Dividend / Interest Payable, Exercise Date, Conversion Date.* | **13 December 2017** |
| ***Notice Date*** *Entitlement letters, call notices, conversion notices mailed* | **By 27 November 2017** |
| ***Allotment Date*** *For the issue of new securities. Must be within 5 business days of application closing date.* | **20 December 2017** |

**OFFICE USE ONLY**
Ex Date:
Commence Quoting Rights:
Cease Quoting Rights 5pm:
Commence Quoting New Securities:
Cease Quoting Old Security 5pm:

Security Code:

Security Code:

*Rule 2.7, 3.10.3, 3.10.4, 3.10.5*

# Appendix 3B

## New issue announcement, application for quotation of additional securities and agreement

*Information or documents not available now must be given to ASX as soon as available. Information and documents given to ASX become ASX's property and may be made public.*

Introduced 01/07/96 Origin: Appendix 5 Amended 01/07/98, 01/09/99, 01/07/00, 30/09/01, 11/03/02, 01/01/03, 24/10/05, 01/08/12, 04/03/13

Name of entity

Tower Limited (**Tower**)

ARBN

088 481 234

We (the entity) give ASX the following information.

## Part 1 - All issues

*You must complete the relevant sections (attach sheets if there is not enough space).*

| | | |
|---|---|---|
| 1 | +Class of +securities issued or to be issued | Fully paid ordinary shares (**New Shares**). |
| 2 | Number of +securities issued or to be issued (if known) or maximum number which may be issued | 168,662,150 New Shares, to be issued pursuant to the terms of an underwritten renounceable pro rata entitlement offer (**Entitlement Offer**) announced on ASX on 14 November 2017. |
| 3 | Principal terms of the +securities (e.g. if options, exercise price and expiry date; if partly paid +securities, the amount outstanding and due dates for payment; if +convertible securities, the conversion price and dates for conversion) | The New Shares will have the same terms as the existing quoted fully paid ordinary shares in Tower. |

+ See chapter 19 for defined terms.

| | | |
|---|---|---|
| 4 | Do the +securities rank equally in all respects from the +issue date with an existing +class of quoted +securities?<br><br>If the additional +securities do not rank equally, please state:<br>• the date from which they do<br>• the extent to which they participate for the next dividend, (in the case of a trust, distribution) or interest payment<br>• the extent to which they do not rank equally, other than in relation to the next dividend, distribution or interest payment | Yes. The New Shares will rank equally with existing ordinary shares from the date of issue of the New Shares. |
| 5 | Issue price or consideration | NZ$0.42 per New Share for eligible New Zealand shareholders, and A$0.39 per New Share for eligible Australian shareholders. |
| 6 | Purpose of the issue<br>(If issued as consideration for the acquisition of assets, clearly identify those assets) | To provide further capital for Tower's subsidiary, Tower Insurance Limited, and for general corporate purposes. |
| 6a | Is the entity an +eligible entity that has obtained security holder approval under rule 7.1A?<br><br>If Yes, complete sections 6b – 6h *in relation to the +securities the subject of this Appendix 3B*, and comply with section 6i | N/A |
| 6b | The date the security holder resolution under rule 7.1A was passed | N/A |
| 6c | Number of +securities issued without security holder approval under rule 7.1 | N/A |

+ See chapter 19 for defined terms.

| | | |
|---|---|---|
| 6d | Number of +securities issued with security holder approval under rule 7.1A | N/A |
| 6e | Number of +securities issued with security holder approval under rule 7.3, or another specific security holder approval (specify date of meeting) | N/A |
| 6f | Number of +securities issued under an exception in rule 7.2 | N/A |
| 6g | If +securities issued under rule 7.1A, was issue price at least 75% of 15 day VWAP as calculated under rule 7.1A.3? Include the +issue date and both values. Include the source of the VWAP calculation. | N/A |
| 6h | If +securities were issued under rule 7.1A for non-cash consideration, state date on which valuation of consideration was released to ASX Market Announcements | N/A |
| 6i | Calculate the entity's remaining issue capacity under rule 7.1 and rule 7.1A – complete Annexure 1 and release to ASX Market Announcements | N/A |
| 7 | +Issue dates<br>Note: The issue date may be prescribed by ASX (refer to the definition of issue date in rule 19.12). For example, the issue date for a pro rata entitlement issue must comply with the applicable timetable in Appendix 7A.<br>Cross reference: item 33 of Appendix 3B. | 20 December 2017 |

| | | Number | +Class |
|---|---|---|---|
| 8 | Number and +class of all +securities quoted on ASX (*including* the +securities in section 2 if applicable) | After completion of the Entitlement Offer, there will be up to 337,324,300 fully paid ordinary shares quoted on ASX. | Fully paid ordinary shares |

+ See chapter 19 for defined terms.

| | | Number | +Class |
|---|---|---|---|
| 9 | Number and +class of all +securities not quoted on ASX (*including* the +securities in section 2 if applicable) | N/A | N/A |

| | | |
|---|---|---|
| 10 | Dividend policy (in the case of a trust, distribution policy) on the increased capital (interests) | Tower has presently suspended dividend payments. Tower's Board and management team are strongly committed to paying dividends and to the efficient management of capital. Tower's Board will review the dividend policy and look to recommence dividends in FY18. |

## Part 2 - Pro rata issue

| | | |
|---|---|---|
| 11 | Is security holder approval required? | No. |
| 12 | Is the issue renounceable or non-renounceable? | Renounceable. |
| 13 | Ratio in which the +securities will be offered | 1 New Share for every 1 fully paid ordinary share held by each eligible shareholder as at the record date for the Entitlement Offer. |
| 14 | +Class of +securities to which the offer relates | Fully paid ordinary shares. |
| 15 | +Record date to determine entitlements | 7:00 PM (New Zealand time) on 22 November 2017. |
| 16 | Will holdings on different registers (or subregisters) be aggregated for calculating entitlements? | No. |
| 17 | Policy for deciding entitlements in relation to fractions | N/A |

+ See chapter 19 for defined terms.

| | | |
|---|---|---|
| 18 | Names of countries in which the entity has security holders who will not be sent new offer documents<br>Note: Security holders must be told how their entitlements are to be dealt with.<br>Cross reference: rule 7.7. | All countries other than Australia and New Zealand. |
| 19 | Closing date for receipt of acceptances or renunciations | 7.00pm (New Zealand Time) on 13 December 2017 |
| 20 | Names of any underwriters | Goldman Sachs New Zealand Limited (**Goldman Sachs**) |
| 21 | Amount of any underwriting fee or commission | An underwriting fee of 1.9% of the proceeds of the Entitlement Offer will be paid to Goldman Sachs. |
| 22 | Names of any brokers to the issue | N/A |
| 23 | Fee or commission payable to the broker to the issue | N/A |
| 24 | Amount of any handling fee payable to brokers who lodge acceptances or renunciations on behalf of security holders | N/A |
| 25 | If the issue is contingent on security holders' approval, the date of the meeting | N/A |
| 26 | Date entitlement and acceptance form and offer documents will be sent to persons entitled | No disclosure document is being prepared. The Offer Booklet will be released to the market on or around 16 November 2017. An Offer Booklet and personalised entitlement and acceptance form will be sent to eligible shareholders by 27 November 2017. |
| 27 | If the entity has issued options, and the terms entitle option holders to participate on exercise, the date on which notices will be sent to option holders | N/A |
| 28 | Date rights trading will begin (if | 21 November 2017 on the NZX Main Board |

+ See chapter 19 for defined terms.

| | | |
|---|---|---|
| | applicable) | |
| 29 | Date rights trading will end (if applicable) | 7 December 2017 |
| 30 | How do security holders sell their entitlements *in full* through a broker? | Entitlements will not be quoted on ASX and cannot be traded on ASX. Eligible shareholders may sell some or all of their entitlements on the NZX Main Board in accordance with the listing rules of the NZX and in accordance with the details set out in the Offer Booklet and entitlement and acceptance form. |
| 31 | How do security holders sell *part* of their entitlements through a broker and accept for the balance? | Entitlements will not be quoted on ASX and cannot be traded on ASX. Eligible shareholders may sell some or all of their rights on the NZX Main Board in accordance with the rules of the NZX and in accordance with the details set out in the Offer Booklet and entitlement and acceptance form. |
| 32 | How do security holders dispose of their entitlements (except by sale through a broker)? | Entitlements will not be quoted on ASX and cannot be traded on ASX. Eligible shareholders may sell some or all of their rights on the NZX Main Board in accordance with the rules of the NZX and in accordance with the details set out in the Offer Booklet and entitlement and acceptance form. |
| 33 | +Issue date | 20 December 2017. |

## Part 3 - Quotation of securities

*You need only complete this section if you are applying for quotation of securities*

34 Type of +securities
(*tick one*)

+ See chapter 19 for defined terms.

(a) ☒ +Securities described in Part 1

(b) ☐ All other +securities

Example: restricted securities at the end of the escrowed period, partly paid securities that become fully paid, employee incentive share securities when restriction ends, securities issued on expiry or conversion of convertible securities

## Entities that have ticked box 34(a)

### Additional securities forming a new class of securities

*Tick to indicate you are providing the information or documents*

35 ☐ If the +securities are +equity securities, the names of the 20 largest holders of the additional +securities, and the number and percentage of additional +securities held by those holders

36 ☐ If the +securities are +equity securities, a distribution schedule of the additional +securities setting out the number of holders in the categories
1 - 1,000
1,001 - 5,000
5,001 - 10,000
10,001 - 100,000
100,001 and over

37 ☐ A copy of any trust deed for the additional +securities

## Entities that have ticked box 34(b)

| | | |
|---|---|---|
| 38 | Number of +securities for which +quotation is sought | |
| 39 | +Class of +securities for which quotation is sought | |

+ See chapter 19 for defined terms.

| | | |
|---|---|---|
| 40 | Do the +securities rank equally in all respects from the +issue date with an existing +class of quoted +securities?<br><br>If the additional +securities do not rank equally, please state:<br>• the date from which they do<br>• the extent to which they participate for the next dividend, (in the case of a trust, distribution) or interest payment<br>• the extent to which they do not rank equally, other than in relation to the next dividend, distribution or interest payment | |
| 41 | Reason for request for quotation now<br><br>Example: In the case of restricted securities, end of restriction period<br><br>(if issued upon conversion of another +security, clearly identify that other +security) | |

42 Number and +class of all +securities quoted on ASX (*including* the +securities in clause 38)

| Number | +Class |
|---|---|
| | |

## Quotation agreement

1 +Quotation of our additional +securities is in ASX's absolute discretion. ASX may quote the +securities on any conditions it decides.

2 We warrant the following to ASX.

- The issue of the +securities to be quoted complies with the law and is not for an illegal purpose.

- There is no reason why those +securities should not be granted +quotation.

- An offer of the +securities for sale within 12 months after their issue will not require disclosure under section 707(3) or section 1012C(6) of the Corporations Act.

  Note: An entity may need to obtain appropriate warranties from subscribers for the securities in order to be able to give this warranty

- Section 724 or section 1016E of the Corporations Act does not apply to any applications received by us in relation to any +securities to be quoted and that no-one has any right to return any +securities to be quoted under sections 737, 738 or 1016F of the Corporations Act at the time that we request that the +securities be quoted.

- If we are a trust, we warrant that no person has the right to return the +securities to be quoted under section 1019B of the Corporations Act at the time that we request that the +securities be quoted.

3 We will indemnify ASX to the fullest extent permitted by law in respect of any claim, action or expense arising from or connected with any breach of the warranties in this agreement.

4 We give ASX the information and documents required by this form. If any information or document is not available now, we will give it to ASX before +quotation of the +securities begins. We acknowledge that ASX is relying on the information and documents. We warrant that they are (will be) true and complete.

Sign here: (Company secretary) Date: 14 November 2017

Print name: David Callanan

+ See chapter 19 for defined terms.

14 November 2017

NZX Limited
Level 1, NZX Centre
11 Cable Street
Wellington

ASX Limited
20 Bridge Street
Sydney NSW 2000

**TOWER RIGHTS ISSUE CLEANSING NOTICE**

1 Tower Limited (*Tower*) has announced that it will undertake a pro rata 1 for 1 renounceable rights offer of fully paid ordinary shares of the same class as already quoted on the NZX Main Board of NZX Limited and the Australian Securities Exchange, underwritten by Goldman Sachs New Zealand Limited.

2 Pursuant to clause 20(1)(a) of Schedule 8 to the Financial Markets Conduct Regulations 2014 (*FMC Regulations*), and the Financial Markets Conduct Act 2015 (*FMCA*), Tower states that:

2.1 Tower is making the offer in reliance upon the exclusion in clause 19 of Schedule 1 to the FMCA and is giving this notice under clause 20(1)(a) of Schedule 8 to the FMC Regulations.

2.2 As at the date of this notice, Tower is in compliance with the continuous disclosure obligations that apply to it in relation to ordinary shares in Tower and there is no information that is "excluded information" as defined in clause 20(5) of Schedule 8 to the FMC Regulations.

2.3 As at the date of this notice, Tower is in compliance with its financial reporting obligations.

3 This notice is also given in accordance with 708AA of the Corporations Act 2001 (Cth), as modified by Australian Securities and Investments Commission (**ASIC**) Instrument 16-0218 and in reliance on ASIC Corporations (Non-Traditional Rights Issues) Instrument 2016/84.

4 The offer is not expected to have any material effect or consequence on the control of Tower.

TOWER

Michael Stiassny
Chairman
Tower Limited
ARBN 088 481 234 Incorporated in New Zealand

*For media queries, please contact:*

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