



ACE Insurance Limited

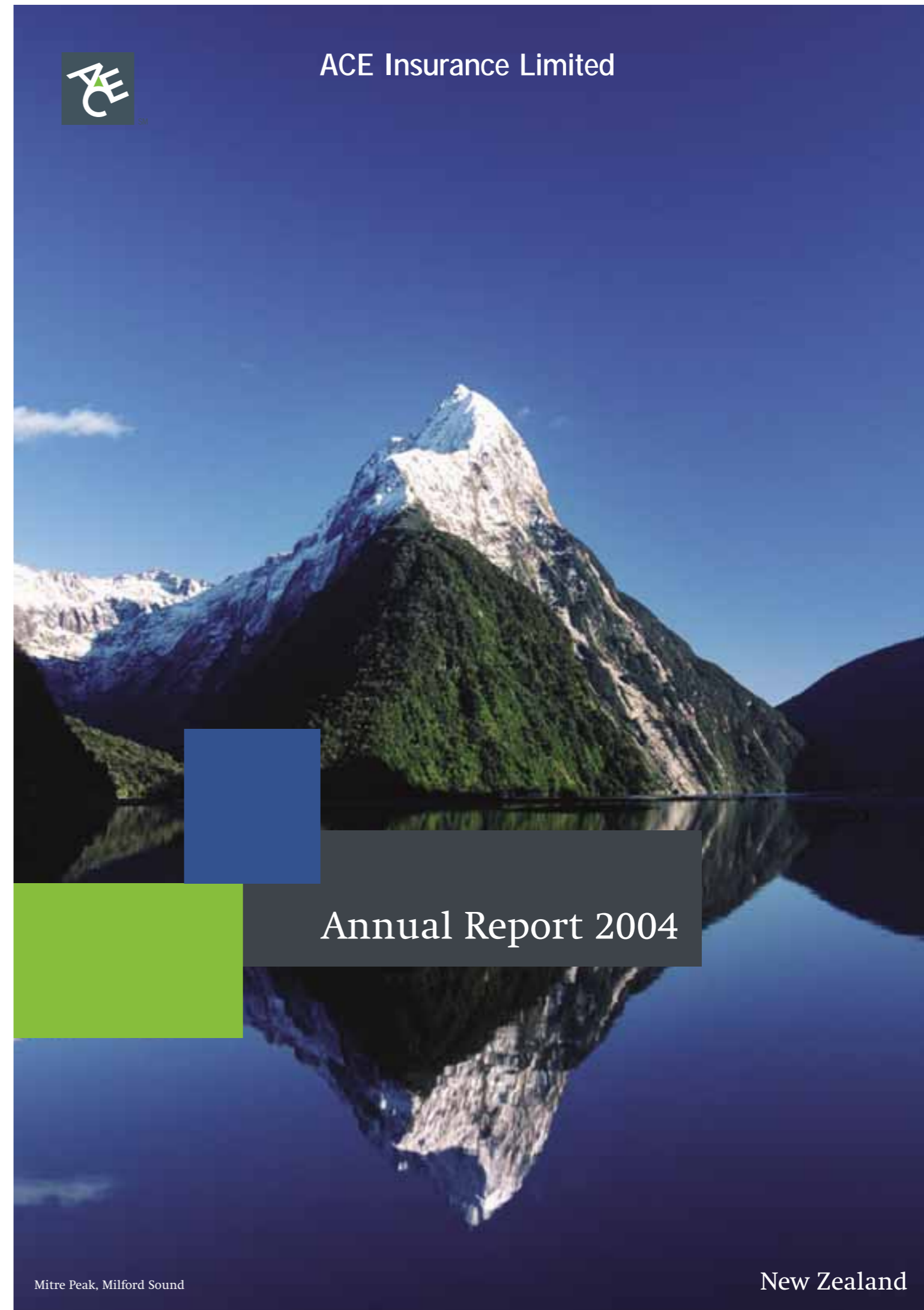


ace insurance limited

ACE Insurance Limited

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Annual Report 2004

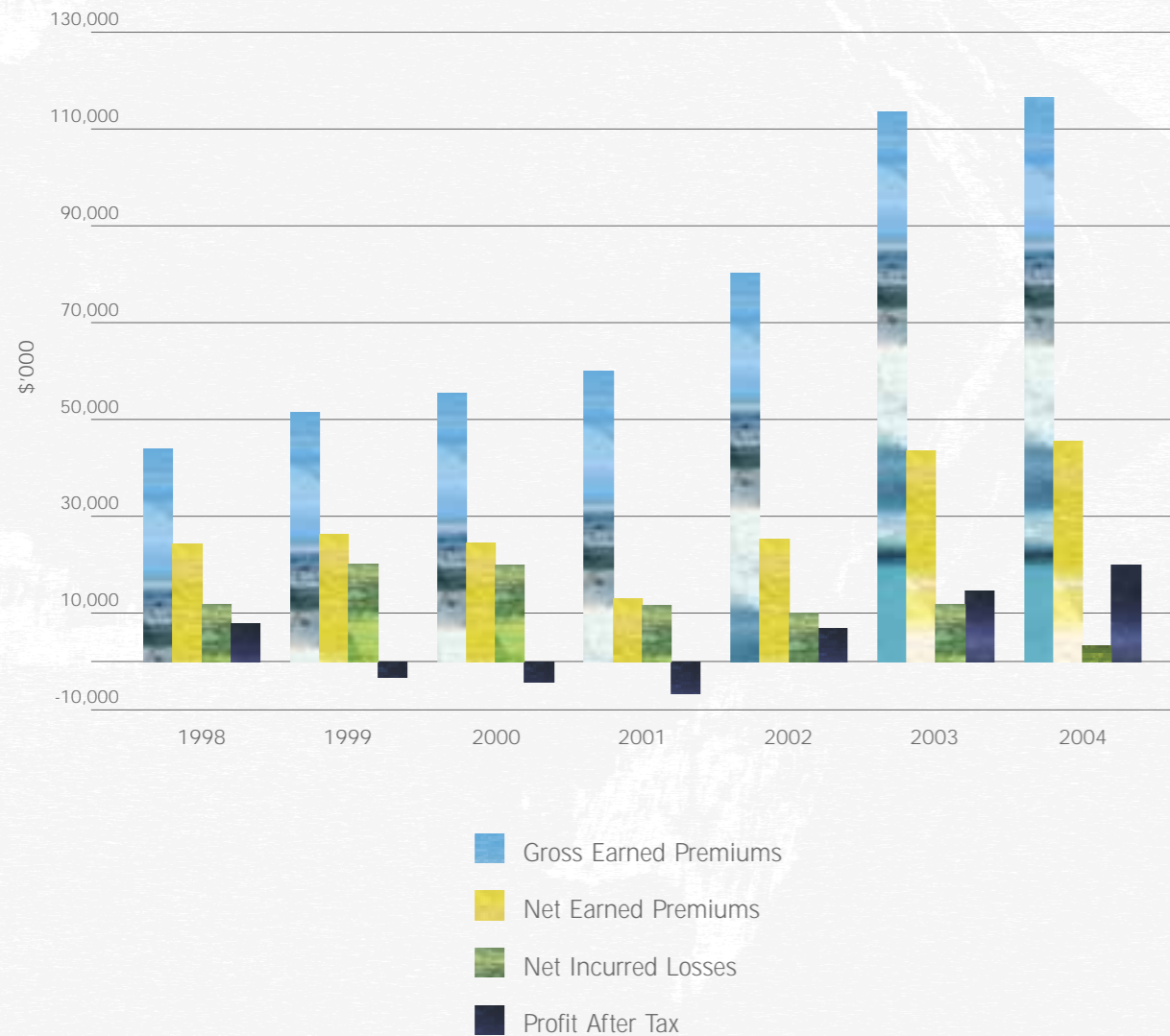
Mitre Peak, Milford Sound

New Zealand

## ACE Insurance Limited

ACE Insurance Limited is one of the ACE Group of Companies, a major global provider of insurance and reinsurance protection, with US\$56 billion in assets and gross premiums of US\$16.1 billion. In a wide range of traditional and specialty lines, ACE uses its strong analytical skills, breadth of resources and global reach to deliver quality products and exceptional service.

### ACE Insurance Limited Financial Highlights



## Contents

### FINANCIAL REPORT 2004

Directors' Responsibility Statement [Page 1](#)

Managing Director's Report [Page 2](#)

Auditors' Report [Page 3](#)

Statement of Financial Performance [Page 5](#)

Statement of Movements in Equity [Page 6](#)

Statement of Financial Position [Page 7](#)

Statement of Cash Flows [Page 8](#)

Notes to the Financial Statements [Page 9](#)

## Directors' Responsibility Statement

For The Year Ended 31 December 2004

The Directors are responsible for ensuring that the financial statements give a true and fair view of the financial position of the Company as at 31 December 2004 and its financial performance and cash flows for the year ended on that date.

The Directors consider that the financial statements of the Company have been prepared using appropriate accounting policies, consistently applied and supported by reasonable judgments and estimates and that all relevant financial reporting and accounting standards have been followed.

The Directors believe that proper accounting records have been kept which enable, with reasonable accuracy, the determination of the financial position of the Company and facilitate compliance of the financial statements with the Financial Reporting Act 1993.


The Directors have taken adequate steps to safeguard the assets of the Company and to prevent and detect fraud and other irregularities.

The Directors have pleasure in presenting the financial statements of ACE Insurance Limited for the year ended 31 December 2004.

### Shareholders' Resolution

In accordance with section 211(3) of the Companies Act 1993, the shareholders have passed a unanimous resolution that the annual report of the Company include only the signed financial statements for the accounting period completed and an Auditors' report.

For and on behalf of the Board of Directors



Director  
Scott Pickering  
31 March 2005



Director  
Stephen McConnell  
31 March 2005

## Managing Director's Report

For The Year Ended 31 December 2004

I am pleased to be able to present our annual report to shareholders and other interested parties.

2004 was another strong year for ACE Insurance Limited New Zealand with a record net profit after tax of \$22.2 million recorded, an increase of \$5.4 million over our 2003 results.

Our largest market segment, corporate, was impacted by rate reductions across most lines of business as the year progressed. Nonetheless, we were able to maintain a leading position in this segment by adherence to selective and disciplined underwriting coupled with a service oriented approach and continued utilisation of our internal risk management capabilities.

The Company was also able to pay a record dividend to shareholders of \$22.6 million at 31 December 2004, whilst maintaining comparable levels of equity over 2003. We also maintained capital adequacy of \$19.7 million in excess of the preferred capital requirement established by the Public Trustee in the Company's Trust Deed.

Our commercial segment, which focuses on the middle market business sector, is now in its third year and continued to show positive growth. This allowed us to offset some of the premium reductions seen in the corporate segment. We will continue to dedicate resources and investment to this segment as we see it as a key contributor to future growth. It also provides us with even greater balance to our overall business portfolio.

In June 2004, the Company received for the first time in its own right an A rating from Standard & Poors. A.M. Best also reaffirmed their A (Excellent) rating.

The Company is firmly committed to maintaining the highest levels of corporate governance and risk management processes, with the Board Audit Committee directing and monitoring our Business Risk Management Steering Committee in this area. During the course of the year a number of operational audits and peer reviews took place and the Company will continue to act promptly and proactively on any areas identified for improvement.

On behalf of the entire Board I would like to extend my thanks to our loyal and dedicated staff for their efforts in contributing to the overall success of the Company in 2004. Without you we would not be able to achieve the results we have.



Managing Director  
Scott Pickering  
31 March 2005

## Auditors' Report To The Shareholders Of ACE Insurance Limited

For The Year Ended 31 December 2004

PricewaterhouseCoopers  
188 Quay Street  
Private Bag 92162  
Auckland, New Zealand  
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Facsimile +64 9 355 8001  
www.pwc.com/nz

We have audited the financial statements on pages 5 to 23. The financial statements provide information about the past financial performance and cash flows of the Company for the year ended 31 December 2004 and its financial position as at that date. This information is stated in accordance with the accounting policies set out on pages 9 to 11.

### DIRECTORS' RESPONSIBILITIES

The Company's Directors are responsible for the preparation and presentation of the financial statements which give a true and fair view of the financial position of the Company as at 31 December 2004 and its financial performance and cash flow for the year ended on that date.

### AUDITORS' RESPONSIBILITIES

We are responsible for expressing an independent opinion on the financial statements presented by the Directors and reporting our opinion to you.

### BASIS OF OPINION

An audit includes examining, on a test basis, evidence relevant to the amounts and disclosures in the financial statements. It also includes assessing:

- (a) the significant estimates and judgements made by the Directors in the preparation of the financial statements; and
- (b) whether the accounting policies are appropriate to the circumstances of the Company, consistently applied and adequately disclosed.

We conducted our audit in accordance with generally accepted auditing standards in New Zealand. We planned and performed our audit so as to obtain all the information and explanations which we considered necessary to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatements, whether caused by fraud or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

We have no relationship with or interests in the Company other than in our capacity as auditors and tax advisers.

## Auditors' Report To The Shareholders Of ACE Insurance Limited

For The Year Ended 31 December 2004

### UNQUALIFIED OPINION

We have obtained all the information and explanations we have required.

In our opinion:

- (a) proper accounting records have been kept by the Company as far as appears from our examination of those records; and
- (b) the financial statements on pages 5 to 23:
  - (i) comply with generally accepted accounting practice in New Zealand; and
  - (ii) give a true and fair view of the financial position of the Company as at 31 December 2004 and its financial performance and cash flows for the year ended on that date.

Our audit was completed on 31 March 2005 and our unqualified opinion is expressed as at that date.

*PricewaterhouseCoopers*

Chartered Accountants  
Auckland

## Statement Of Financial Performance

For The Year Ended 31 December 2004

	NOTE	2004 \$'000	2003 \$'000
Premium revenue		116,685	112,008
Outwards reinsurance expense		69,988	67,013
Net premium income		46,697	44,995
Claims incurred		27,631	37,044
Reinsurance and other recoveries revenue	23	23,869	21,630
Net claims incurred	22	3,762	15,414
Net acquisition expenses		3,867	3,856
Other expenses		10,808	11,089
Total expenses		14,675	14,945
Other income		382	191
<b>UNDERWRITING RESULT</b>		<b>28,642</b>	<b>14,827</b>
Investment revenue	2	4,564	4,281
<b>OPERATING SURPLUS BEFORE TAX</b>	2	<b>33,206</b>	<b>19,108</b>
Income tax expense	3	11,016	2,331
<b>OPERATING SURPLUS AFTER TAX</b>		<b>22,190</b>	<b>16,777</b>
<b>NET SURPLUS ATTRIBUTABLE TO MEMBERS OF THE HOLDING COMPANY</b>		<b>22,190</b>	<b>16,777</b>

The attached notes form an integral part of these financial statements.

## Statement Of Movements In Equity

For The Year Ended 31 December 2004

	2004 \$'000	2003 \$'000
Equity at beginning of the year	33,363	16,299
	<b>33,363</b>	<b>16,299</b>
Net surplus for the year	22,190	16,777
Revaluation of land and building	121	287
<b>TOTAL RECOGNISED REVENUES AND EXPENSES FOR THE YEAR</b>	<b>22,311</b>	<b>17,064</b>
Dividends paid	(22,648)	-
<b>EQUITY AT END OF THE YEAR</b>	<b>33,026</b>	<b>33,363</b>

The attached notes form an integral part of these financial statements.

## Statement Of Financial Position

As At 31 December 2004

	NOTE	2004 \$'000	2003 \$'000
<b>EQUITY</b>			
Share capital	4	16,900	16,900
Reserves	5	464	343
Retained earnings	5	15,662	16,120
<b>Total equity</b>		<b>33,026</b>	<b>33,363</b>
Represented by:			
<b>CURRENT ASSETS</b>			
Cash and bank deposits	14	11,984	21,862
Premiums receivable		35,198	32,061
Prepayments and other receivables		1,244	1,224
Deferred acquisition costs		5,047	4,386
		53,473	59,533
<b>NON CURRENT ASSETS</b>			
Investments	6	69,132	66,271
Fixed assets	7	3,588	3,413
		72,720	69,684
<b>Total assets</b>		<b>126,193</b>	<b>129,217</b>
<b>CURRENT LIABILITIES</b>			
Accounts payable	21	11,718	10,451
Intercompany payable	10	7,850	3,016
Income tax payable		585	1,398
Insurance provisions	8	58,415	64,738
		78,568	79,603
<b>NON CURRENT LIABILITIES</b>			
Accounts payable		1,844	1,734
Deferred income tax liability	3	753	848
Insurance provisions	8	12,002	13,669
		14,599	16,251
<b>Total liabilities</b>		<b>93,167</b>	<b>95,854</b>
<b>NET ASSETS</b>		<b>33,026</b>	<b>33,363</b>

The attached notes form an integral part of these financial statements.

## Statement Of Cash Flows

For The Year Ended 31 December 2004

	NOTE	2004 \$'000	2003 \$'000
<b>OPERATING ACTIVITIES</b>			
<b>Cash was provided from</b>			
Receipts of premium revenue		113,548	118,689
Receipts from reinsurance recoveries		22,087	9,720
Interest received		5,395	3,924
		141,030	132,333
<b>Cash was applied to</b>			
Payment of claims and claims expenses		(31,990)	(19,873)
Payment of outward reinsurance		(67,793)	(64,797)
Commission paid		(4,089)	(4,403)
Payment to suppliers and employees		(8,470)	(11,352)
Income tax paid		(11,924)	-
		(124,266)	(100,425)
<b>Net cash inflow from operating activities</b>	13	<b>16,764</b>	<b>31,908</b>
<b>INVESTMENT ACTIVITIES</b>			
<b>Cash was provided from</b>			
Proceeds from sale of investments		110,640	11,420
Proceeds from sale of fixed assets		24	21
		110,664	11,441
<b>Cash was applied to</b>			
Purchase of investments		114,278	32,681
Purchase of fixed assets		380	443
		114,658	33,124
<b>Net cash outflows from investing activities</b>		<b>(3,994)</b>	<b>(21,683)</b>
<b>FINANCING ACTIVITIES</b>			
<b>Cash was applied to</b>			
Dividends paid to parent company		22,648	-
Net cash outflows from financing activities		22,648	-
<b>Net (decrease)/increase in cash held</b>		<b>(9,878)</b>	<b>10,225</b>
<b>Cash at beginning of year</b>	14	<b>21,862</b>	<b>11,637</b>
<b>Cash at end of year</b>	14	<b>11,984</b>	<b>21,862</b>

## Notes To Financial Statements

For The Year Ended 31 December 2004

### 1. STATEMENT OF ACCOUNTING POLICIES

#### (i) Reporting entity and basis of reporting

The financial statements are for the reporting entity ACE Insurance Limited. The Company is registered under the Companies Act 1993.

The financial statements have been prepared in accordance with the Companies Act 1993 and the Financial Reporting Act 1993.

The financial statements have been prepared on the basis of historical cost with the exception of certain items for which specific accounting policies are identified.

#### (ii) Income recognition

##### General insurance

Premiums comprise of amounts charged to policyholders and brought into account from the date of attachment of risk. The earned portion of premiums received/receivable, including unclosed business, is recognised as revenue.

Unearned premiums have been determined from the date of attachment of risk based on the number of days of unexpired cover for each policy.

Outward reinsurance premiums are expensed in accordance with the pattern of benefits received. Accordingly, proportional reinsurance is expensed on a daily pro rated basis over the period of the underlying risk and excess of loss treaty reinsurance charges are expensed over the treaty period.

##### Investment income

Investment income is recognised on an accrual basis. Unrealised gains or losses on revaluation of investments are included in or charged against investment income in the Statement of Financial Performance.

#### (iii) Claims

Claims expense represents claims paid, cost of handling the claims and changes in amounts for provision for outstanding claims. Reinsurance and other recoveries are recognised in deriving the net claims expense.

Claims outstanding represent estimates of payments to be made on individual claims which have been incurred and reported, estimates of losses which have occurred but have not yet been reported and the anticipated direct and indirect costs of settling these claims. Reinsurance recoveries are included in these estimates, other recoveries are recognised when the amount to be recovered can be reliably measured. The provision for outstanding claims, reinsurance and other recoveries are discounted to the net present value.

#### (iv) Deferred acquisition costs

Costs directly associated with obtaining policies of general insurance business and which can be reliably measured, are deferred and recorded as assets where they give rise to premium revenue in subsequent periods. Deferred acquisition costs are measured at the lower of cost and recoverable amount and are amortised over the period expected to benefit from the expenditure.

## Notes To Financial Statements

For The Year Ended 31 December 2004

### 1. ACCOUNTING POLICIES (CONTINUED)

#### (v) Taxation

Income tax expense/(credit) recognises the current obligations and amounts arising from timing differences between the accounting results and assessable income for the year. This is the liability method applied on a comprehensive basis.

A deferred tax asset or the effect of losses carried forward that exceed the deferred tax liability, is recognised in the financial statements only where there is virtual certainty that the benefit of timing differences, or losses, will be utilised.

#### (vi) Fixed assets

All fixed assets are initially recorded at cost. Freehold land and buildings are subsequently revalued to net market value by an independent valuer on an annual basis.

Depreciation of fixed assets, other than freehold land, is calculated using straight line basis, so as to allocate the cost of the assets or the revalued amounts less their residual value over their useful lives. The rates are as follows:

Computer equipment	13.5% to 36.0%
Furniture and fittings	6.5% to 48.0%
Motor vehicles	18.0% to 21.6%

Gains and losses on disposal of fixed assets are taken into account in determining the operating surplus for the year.

#### (vii) Goods and services tax (GST)

The Statement of Financial Performance and Statement of Cash Flows have been prepared so that all components are stated exclusive of GST. All items in the Statement of Financial Position are stated net of GST, with the exception of receivables and payables, which include GST, invoiced.

#### (viii) Investments

Investments are recorded on the following basis:

- debentures, local authority and government stock and offshore fixed interest securities are valued at market or yield to maturity.
- a statutory deposit, comprising of government stock, is held in accordance with the Insurance Companies Deposit Act 1953 and is recorded at market value.

## Notes To Financial Statements

For The Year Ended 31 December 2004

### 1. ACCOUNTING POLICIES (CONTINUED)

#### (ix) Operating leases

Leases under which all the risks and benefits of ownership are effectively retained by the lessor are classified as operating leases. Operating lease payments are recognised as an expense in the periods the amounts are payable.

#### (x) Statement of Cash Flows

The following are the definitions of the terms used in the Statement of Cash Flows:

- (a) Operating activities include all transactions and other events that are not investing or financing activities.
- (b) Investing activities are those activities relating to the acquisition, holding and disposal of property, plant and equipment and of investments. Investments include securities not falling within the definition of cash.
- (c) Financing activities are those activities that result in changes in size and composition of the capital structure. This includes both equity and debt not falling within the definition of cash. Dividends paid in relation to capital structure are included in financing activities.
- (d) Cash is considered to be cash on hand, current accounts in banks, and deposits on call, net of bank overdrafts.

#### (xi) Financial instruments

##### Recognised

Financial instruments carried on the Statement of Financial Position include cash and bank balances, investments, receivables, trade creditors and borrowings. The particular recognition methods adopted are disclosed in the individual policy statements associated with each item.

##### Unrecognised

There were no unrecognised financial instruments at the balance date.

#### (xii) Foreign currency transactions

Transactions denominated in a foreign currency are converted to New Zealand dollars at the exchange rates effective at the date of the transaction. Monetary assets and liabilities arising from trading transactions or overseas borrowings are translated at closing rates. Gains and losses due to currency fluctuations on these items are included in the Statement of Financial Performance.

#### (xiii) Changes in Accounting Policy

There have been no changes in accounting policy during the current year.

## Notes To Financial Statements

For The Year Ended 31 December 2004

### 2. OPERATING SURPLUS

	2004 \$'000	2003 \$'000
The operating surplus for the year is after charging/(crediting):		
Interest received	(5,415)	(4,308)
Decrease/(increase) in valuation of investments	646	(31)
Loss on sale of investments	205	58
Investment Revenue	(4,564)	(4,281)
Loss on foreign exchange translation	346	1,127
Depreciation		
– Furniture and equipment	177	160
– Motor vehicles	61	52
Audit fees	89	88
Other fees paid to auditors	47	74
Rent and lease expenses	64	61
Profit on sale of fixed assets	(9)	(2)

## Notes To Financial Statements

For The Year Ended 31 December 2004

### 3. TAXATION

INCOME TAX EXPENSE	2004 \$'000	2003 \$'000
Operating surplus before income tax	33,206	19,108
<b>Permanent differences</b>		
Prior year adjustment	39	-
Expenditure not deductible for tax	137	(100)
	33,382	19,008
Surplus subject to tax	33,382	19,008
Tax at 33%	11,016	6,273
Recognition of prior year tax losses	-	(4,883)
Recognition of prior year timing differences	-	941
<b>Income tax recognised in Statement of Financial Performance</b>	<b>11,016</b>	<b>2,331</b>
<b>Comprising</b>		
Estimated current year tax assessment	11,111	1,390
Recognition of prior year timing differences	-	941
Deferred tax liability	(95)	-
	<b>11,016</b>	<b>2,331</b>
<b>DEFERRED TAX BALANCES</b>	<b>2004 \$'000</b>	<b>2003 \$'000</b>
Opening Balance	848	-
On surplus for year	(95)	848
	<b>753</b>	<b>848</b>

## Notes To Financial Statements

For The Year Ended 31 December 2004

### 3. TAXATION (CONTINUED)

IMPUTATION BALANCES	2004 \$'000	2003 \$'000
Balance at the beginning of the year	-	-
Tax Payment	7,936	-
Imputation credits attached to dividends paid	(7,158)	-
Balance at the end of the year	778	-

### 4. SHARE CAPITAL

	2004 \$'000	2003 \$'000
Balance at beginning of year	16,900	16,900
Balance at end of year – 16,899,558 ordinary fully paid	16,900	16,900

All ordinary shares rank equally with one vote attached to each fully paid ordinary share.

### 5. RESERVES

	2004 \$'000	2003 \$'000
<b>Revaluation reserve:</b>		
Balance at beginning of year	343	56
Revaluation of land and building	121	287
<b>Balance at end of year</b>	<b>464</b>	<b>343</b>
<b>Retained earnings:</b>		
Balance at beginning of year	16,120	(657)
Net surplus for the year	22,190	16,777
Dividends paid	(22,648)	-
<b>Balance at end of year</b>	<b>15,662</b>	<b>16,120</b>

## Notes To Financial Statements

For The Year Ended 31 December 2004

### 6. INVESTMENTS

	2004 \$'000	2003 \$'000
Statutory deposit	516	530
Government and local authority securities	65,338	62,041
Offshore fixed interest securities	3,278	3,700
	<b>69,132</b>	<b>66,271</b>

### 7. FIXED ASSETS

	Cost/ valuation \$'000	Accumulated depreciation \$'000	Net book value \$'000
<b>2004</b>			
Land – valuation	1,200	-	1,200
Buildings – valuation	1,486	-	1,486
Furniture & equipment – cost	1,528	852	676
Motor vehicles – cost	375	149	226
	<b>4,589</b>	<b>1,001</b>	<b>3,588</b>
<b>2003</b>			
Land – valuation	1,200	-	1,200
Buildings – valuation	1,365	-	1,365
Furniture & equipment – cost	1,431	735	696
Motor vehicles – cost	285	133	152
	<b>4,281</b>	<b>868</b>	<b>3,413</b>

An independent valuation of freehold land and buildings was made as at 18 November 2004 by an independent registered valuer, Colliers International New Zealand Limited. The total net market valuation is \$2,686,000 (2003: \$2,565,000). The valuation reflects the building being fully leased.

### 8. INSURANCE PROVISIONS

	2004 \$'000	2003 \$'000
Claims outstanding	24,968	31,109
Unearned premiums	45,449	47,298
	<b>70,417</b>	<b>78,407</b>

## Notes To Financial Statements

For The Year Ended 31 December 2004

### 8A. OUTSTANDING CLAIMS

	2004 \$'000	2003 \$'000
Gross outstanding claims reserve	58,297	64,957
Discount to present value	(4,517)	(6,817)
	<b>53,780</b>	<b>58,140</b>
Gross reinsurance and other recoveries on outstanding claims	(30,982)	(29,947)
Discount to present value	2,170	2,916
	<b>(28,812)</b>	<b>(27,031)</b>
Outstanding claims	24,968	31,109

#### NET OUTSTANDING CLAIMS RESERVE

The following discount rates were used in the measurement of outstanding claims, reinsurance and other recoveries:

	2004
<b>The discount rates are determined from the government bond yield curve. Rates used are:</b>	
2004	6.40%
2005	6.20%
2006	6.10%
2007	6.10%
Thereafter	6.00%

The weighted average term to settlement is 1.50 years (2003: 1.70 years).

### 8B. UNEARNED PREMIUMS

	2004 \$'000	2003 \$'000
Gross unearned premium reserve	60,938	61,631
Reinsurance on unearned premium reserve	(15,489)	(14,333)
Total unearned premium reserve	45,449	47,298

## Notes To Financial Statements

For The Year Ended 31 December 2004

### 9. ULTIMATE HOLDING COMPANY

ACE Insurance Limited is a wholly owned subsidiary of ACE INA International Holdings, Ltd registered in Delaware, United States of America. The ultimate holding company is ACE Limited, whose principal office is located in Hamilton, Bermuda.

### 10. RELATED PARTY TRANSACTIONS

The Company has transactions in the normal course of business with fellow subsidiaries. These comprise of insurance and reinsurance transactions, management and support services. The significant transactions are as follows:

Related party	Relationship	Type of transaction	2004 Transaction \$'000	2004 Balances \$'000	2003 Transaction \$'000	2003 Balances \$'000
Tempest Reinsurance Company Limited, Bermuda	Fellow Subsidiary	Reinsurance placements/claims	51,683	(7,376)	47,497	(2,988)
Other ACE entities	Fellow Subsidiary	Reinsurance placements/claims	9,206	(841)	4,881	(97)
Other ACE entities	Fellow Subsidiary	Premiums & other recharges	186	18	227	65
Safire Pte Ltd, Singapore	Fellow Subsidiary	Management charges	842	-	494	-
Cover Direct Ltd, USA	Fellow Subsidiary	Management charges	1028	-	607	-
ACE UK Services Ltd, UK	Fellow Subsidiary	EDP support service charges	458	-	431	-
ACE Insurance Limited, Australia	Fellow Subsidiary	Management/IT service charges	880	349	863	4
			64,283	(7,850)	55,000	(3,016)

Other ACE entities comprise transactions with fellow subsidiary entities which are not individually material to disclose separately.

No related party balances have been written off or forgiven during the year. (2003: Nil)

## Notes To Financial Statements

For The Year Ended 31 December 2004

### 11. SEGMENT INFORMATION

Throughout the year the Company operated predominantly in general insurance business in New Zealand. The Company was registered as an insurer under Section 201 of the Accident Insurance Act 1998 on 2 June 1999.

#### Re-nationalisation of accident insurance

In accordance with the Accident Insurance (Transitional Provisions) Act 2000 and Accident Insurance Amendment Act 2000, the Company ceased to underwrite new accident insurance business effective 1 April 2000 and all policies in existence as at 1 July 2000 were not renewed.

	General Insurance		Accident Insurance (Run off)		Total	
	2004 \$'000	2003 \$'000	2004 \$'000	2003 \$'000	2004 \$'000	2003 \$'000
Net premium income	46,697	44,995	-	-	46,697	44,995
Net claims incurred	3,824	15,525	(62)	(111)	3,762	15,414
Net acquisition expenses	3,867	3,856	-	-	3,867	3,856
Other expenses	10,792	11,065	16	24	10,808	11,089
Other income	382	191	-	-	382	191
<b>Underwriting result</b>	<b>28,596</b>	<b>14,740</b>	<b>46</b>	<b>87</b>	<b>28,642</b>	<b>14,827</b>
Investment income	4,529	4,238	35	43	4,564	4,281
<b>Operating surplus before tax</b>	<b>33,125</b>	<b>18,978</b>	<b>81</b>	<b>130</b>	<b>33,206</b>	<b>19,108</b>
Income tax expense	11,016	2,288	-	43	11,016	2,331
<b>Operating surplus after tax</b>	<b>22,109</b>	<b>16,690</b>	<b>81</b>	<b>87</b>	<b>22,190</b>	<b>16,777</b>
<b>Total assets</b>	<b>117,274</b>	<b>120,293</b>	<b>8,919</b>	<b>8,924</b>	<b>126,193</b>	<b>129,217</b>

## Notes To Financial Statements

For The Year Ended 31 December 2004

### 12. FINANCIAL INSTRUMENTS

The Company has financial instruments comprising cash at bank and on hand, cash on deposit, premiums receivable, intercompany receivables, other receivables, fixed interest securities, trade and other payables, and lease liabilities.

#### a) Interest Rate Risk

The following table identifies the years in which interest rates are subject to review on interest bearing assets and provides the current weighted average interest rate of each item.

	Repricing Analysis:					
	Weighted Average Interest rate	Current \$'000	1 year or less \$'000	Over 1 to 5 years \$'000	More than 5 years \$'000	Total \$'000
<b>2004 FINANCIAL ASSETS</b>						
Cash & Deposits	5.17%	11,984	-	-	-	11,984
Fixed Interest Securities	6.59%	-	7,109	27,958	34,065	69,132
		11,984	7,109	27,958	34,065	81,116
<b>2003 FINANCIAL ASSETS</b>						
Cash & Deposits	4.76%	21,862	-	-	-	21,862
Fixed Interest Securities	6.71%	-	3,794	28,939	33,538	66,271
		21,862	3,794	28,939	33,538	88,133

#### b) Credit risk

The Company incurs credit risk from transactions with reinsurers, trade receivables and financial institutions in the normal course of its business. The Company has a credit policy, which restricts the exposure to individual trade receivables, which are reviewed on a regular basis. The Company places a majority of its reinsurance placements with ACE group entities. The credit risk on financial assets, which have been recognised in the financial statements, is generally the carrying amount of the assets net of any provision for doubtful debts. The Company does not have any significant concentrations of credit risk, except for reinsurance placements with ACE group entities.

#### c) Fair values

The carrying value of financial assets and liabilities of the Company are representative of their fair values as at balance date. The carrying amounts of all financial assets and liabilities are reviewed to ensure they equal or approximate their fair market values.

#### d) Currency risk

During the normal course of business the Company transacts insurance and other business with amounts denominated in foreign currencies, primarily certain reinsurance transactions are arranged in United States Dollars. As a result of these transactions exposures to fluctuations in foreign currency exchange rates arise. These foreign exchange transactions are settled on a quarterly basis to minimise foreign exchange risk exposure.

## Notes To Financial Statements

For The Year Ended 31 December 2004

### 13. RECONCILIATION OF NET OPERATING CASH FLOWS

	2004 \$'000	2003 \$'000
Operating surplus after income tax	22,190	16,777
<b>Items not involving cash flows</b>		
(Decrease)/increase in unearned premium reserve	(1,849)	5,760
(Decrease)/increase in outstanding claims	(6,141)	5,261
Increase in deferred acquisition costs	(661)	(392)
Changes in net market value of investments	646	(31)
Depreciation expense	238	212
	(7,767)	10,810
<b>Impact of changes in working capital items</b>		
Increase in other receivables	(20)	(384)
(Increase)/decrease in policyholder debtors	(3,137)	3,137
Increase/(decrease) in accounts payable	1,376	(735)
Increase/(decrease) in intercompany payables	4,834	(84)
(Decrease)/increase in tax payable	(908)	2,331
	2,145	4,265
<b>Items classified as investing activities</b>		
Loss on disposal of investments	205	58
Gain on disposal of assets	(9)	(2)
	196	56
<b>Net cash flows from operating activities</b>	<b>16,764</b>	<b>31,908</b>

### 14. RECONCILIATION OF CASH

	2004 \$'000	2003 \$'000
Cash on hand and at bank	274	19,212
Deposits at call	11,710	2,650
	<b>11,984</b>	<b>21,862</b>

## Notes To Financial Statements

For The Year Ended 31 December 2004

### 15. CHARGE

Under the Trust Deed, which governs the operation and management of the accident insurance business, the Public Trustee maintains a floating first charge over the assets of the Company.

### 16. CREDIT RATING

On 15 December 2004, the Company's financial strength rating of 'A Excellent' was reaffirmed by rating agency A.M. Best in accordance with the Insurance Companies Rating and Inspections Act 1994. A.M. Best's A rating is assigned to companies, which in their opinion have demonstrated excellence in overall performance and have a strong ability to meet their obligation to policyholders over a long period of time. The NZ operation has also obtained a Standard and Poors (S & P) rating on 17 June 2004. S & P assigned a rating of "A".

### 17. ACTUARIAL INFORMATION

The actuary who carried out the valuation of the Outstanding Claims Liability is Andrew Bendall BSc., FIAA of ACE Insurance Limited (Australia). The Outstanding Claims liability has been determined in accordance with the standards of the New Zealand Society of Actuaries and the actuary is satisfied as to the nature, sufficiency and accuracy of the data used in the determination.

	2004	2003
Discount rate	6.4%	5.6%
Volatility adjustment	25.0%	25.0%

### 18. CAPITAL COMMITMENTS

As at 31 December 2004 there were no capital commitments (2003: Nil).

### 19. CONTINGENT LIABILITIES

As at 31 December 2004 there were no contingent liabilities outstanding (2003: Nil).

### 20. LEASE COMMITMENTS

The Company has future rental commitments on property leases as follows:

	2004 \$'000	2003 \$'000
Operating lease commitments		
Within one year	88	76
One to two years	52	76
Two to five years	2	38
Beyond five years	-	-
	<b>142</b>	<b>190</b>

## Notes To Financial Statements

For The Year Ended 31 December 2004

### 21. ACCOUNTS PAYABLE

Included in the accounts payable are the following employee entitlements:

	2004 \$'000	2003 \$'000
Employee Entitlements:		
Holiday pay provisions	266	291
Bonus provisions	286	262
Restricted stock grants in the parent company	55	-
Long service leave provisions	19	-
	<b>626</b>	<b>553</b>

### 22. CLAIMS INCURRED

	2004			2003		
	Current \$000	Previous years \$000	Total \$000	Current \$000	Previous years \$000	Total \$000
Gross claims incurred	24,245	5,686	29,931	42,780	(4,724)	38,056
Discounted movement	(96)	(2,204)	(2,300)	(2,553)	1,003	(1,550)
Discounted gross claims incurred	24,149	3,482	27,631	40,227	(3,721)	36,506
Reinsurance and other recoveries	(16,075)	(7,048)	(23,123)	(21,347)	(1,838)	(23,185)
Discounted movement	131	(877)	(746)	1,068	1,025	2,093
Discounted reinsurance and other recoveries	(15,944)	(7,925)	(23,869)	(20,279)	(813)	(21,092)
Net claims incurred	8,205	(4,443)	3,762	19,948	(4,534)	15,414

## Notes To Financial Statements

For The Year Ended 31 December 2004

### 23. REINSURANCE AND OTHER RECOVERIES

	2004 \$'000	2003 \$'000
Reinsurance recoveries	22,673	21,103
Other recoveries	1,196	527
	23,869	21,630

### 24. REINSURANCE PROGRAMME PRINCIPLES

Reinsurance is purchased to make the Company's results more predictable by reducing the effect that individual large claims, and catastrophic events that lead to multiple claims, have on results. The majority of reinsurance will be arranged on a non proportional excess of loss treaty basis.

Reinsurance is purchased by the ACE Group on a centralised basis to ensure tight control over reinsurer security, underwriting discipline and maximising economies of scale. The majority of ACE's reinsurance is on a treaty basis via Quota Share and Excess of Loss contracts. Facultative reinsurance is used on a limited basis to protect net exposures.

### 25. CAPITAL ADEQUACY

The basis that has been used for capital adequacy is the Preferred Capital Requirement established by the Public Trustee in the Trust Deed entered into with the Company on 1 June 1999. The Preferred Capital Requirement is the greatest of \$2,000,000, 30% of Net Written Premiums or 25% of Net Outstanding Claims.

The amount of equity retained for the purpose of capital adequacy as at 31 December 2004 is \$13,454,476 (2003: \$15,226,411) based on the Net Written Premiums requirement. The Company has more than met the Preferred Capital Requirements as at 31 December 2004. The total amount of equity retained in the Company as at 31 December 2004 is \$33,026,000 (2003: \$33,363,000).

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WELLINGTON

#### Christchurch

Level 3  
180 Manchester Street  
CHRISTCHURCH

#### Immediate Parent

**ACE INA International Holdings, Ltd**  
One Beaver Valley Road  
Wilmington, Delaware  
UNITED STATES OF AMERICA

#### Ultimate Parent

**ACE Limited**  
The ACE Building  
30 Woodbourne Avenue  
Hamilton HM08  
BERMUDA

#### Auditors

**PricewaterhouseCoopers**  
188 Quay Street  
AUCKLAND

#### Legal Advisors

**Bell Gully Barristers and Solicitors**  
Vero Centre  
48 Shortland Street  
AUCKLAND

#### Bankers

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Citibank Centre  
23 Customs Street East  
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#### Westpac Banking Corporation

79 Queen Street  
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#### Actuary

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#### Investment Custodian

**State Street Investment Services**  
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#### Company Secretary

**Mark Eggleton**  
ACE Insurance Limited  
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