



Annual Report 2015

Te pūroko a tau a
Urupare ki te Tonga



Southern Response Earthquake Services Ltd

Fun with friends

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This annual report was produced and printed in Christchurch.

Chairman and Chief Executive's report

Introduction

This is the fourth annual report of Southern Response Earthquake Services Limited.

The third full year of operations has seen the maturing of the build phase. Including newly notified claims from EQC, 62% of house claims have been settled as at 30 June 2015.

Our newer over cap customers stem from EQC notifications, totalling more than 450 since June 2014. These customers are understandably apprehensive when beginning their claim settlement journey with us, after a long period of uncertainty. Their properties are receiving a full technical engineering evaluation prior to the customer being presented with settlement options, enabling informed decisions to be made by them earlier in the process. Vulnerable customers' claims are being handled with special concern for their circumstances.

Reflecting this flow of new over cap claims and adjustment of other actuarial assumptions to measure the actual claim

settlement experience during the year, the central estimate of the ultimate liability has increased to \$2,716.2 million, net of EQC contributions. It represents the estimate of the total amount which will be ultimately paid once all claims are settled (including payments already made but excluding claims handling expenses).

The 30 June 2015 actuarial valuation of the claims liability undertaken by Finity Consulting shows an outstanding net claims liability of \$1,108 million.

To meet our liabilities, we will be required to call on the Crown uncalled capital facility put in place in January 2013 with a total estimated drawdown of \$442 million. The Crown uncalled capital facility drawdowns are in addition to drawdowns of the Crown Receivable relating to the 2011 \$500 million preference share facility.

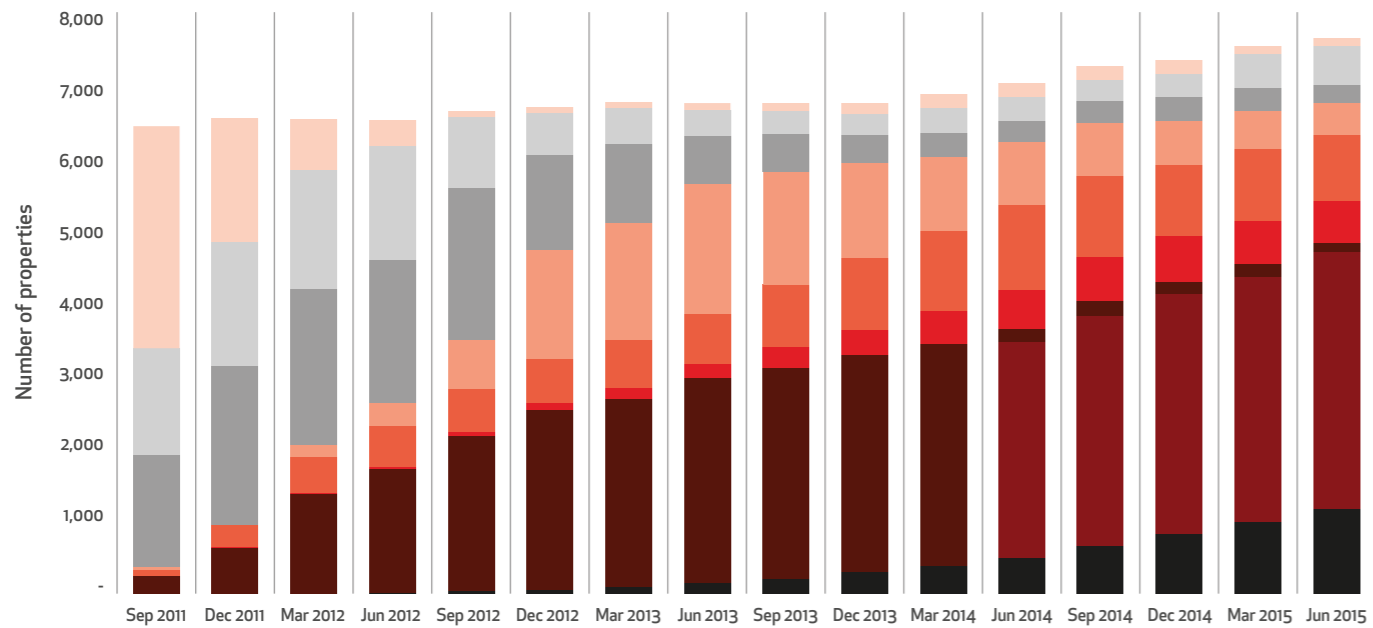
The Board will continue to keep the Company's funding position under review, particularly with respect to key assumptions underpinning the claims liability valuation.



Progress

The graph below provides a summary of our settlement progress over time with a description against each of the over cap (repair or rebuild) property phases.

Status of properties over the past 4 years



Key	Sep 2011	Dec 2011	Mar 2012	Jun 2012	Sep 2012	Dec 2012	Mar 2013	Jun 2013	Sep 2013	Dec 2013	Mar 2014	Jun 2014	Sep 2014	Dec 2014	Mar 2015	Jun 2015
Scheduled for assessment	3063	1708	694	345	78	78	77	93	109	144	186	184	209	174	85	95
Assessment completed	1462	1711	1641	1579	967	586	508	360	316	292	351	326	266	346	474	509
Awaiting customer decision	1550	2181	2143	1976	2101	1310	1085	658	531	394	328	294	298	294	293	236
Construction with Southern Response - pre documentation	39	0	165	315	667	1497	1602	1792	1545	1310	1031	866	731	598	530	436
Construction design/documentation	81	312	499	563	596	605	672	683	861	988	1091	1167	1102	965	965	903
Under construction	3	6	10	27	66	98	143	202	294	348	459	540	599	603	603	543
Customers elected to cash settle ⁴	244	638	1379	1712	2135	2484	2606	2833	2906	2998	3066	192	210	184	158	156
Cash settlement completed ⁴	-	-	-	-	-	-	-	-	-	-	-	2966	3090	3231	3315	3443
Construction completed	1	1	2	10	33	50	83	139	203	291	376	493	648	819	965	1167

⁴ As of April 2014, cash settlements completed and cash settlements elected and in progress are recorded and reported separately.

Our statistics for major claim types are updated monthly and are available from www.southernresponse.co.nz/progress.

Good progress has been achieved in construction during the year, following a focus on progressing claims through documentation during 2013-14. Several significant milestones were reached during the year:

- To the end of May 2015, 1000 families were back in their homes after repairs and rebuilds managed as part of our programme (based on practical completion certificates issued). This number has since risen to 1,212
- To the end of May 2015, \$1.5 billion had been paid out in claims settlement (now \$1.67 billion).

Significant issues have affected the project completion estimate since the last report, including those claims more recently coming over cap, greater complexity with decision making and design for shared property, and an increasingly litigious environment, inevitably leading to the lengthening of the construction programme overall.

Our build programme, supported by project management company Arrow International (Arrow) and other key build partners, is maintaining momentum, although the progress rate in repairs has been slower than we have anticipated. This is mainly due to customers requiring independent advice regarding repair methodology to give them confidence that a satisfactory outcome will be achieved. We do not discourage this approach, and during the year have adapted our resourcing model for the repairs work stream to better support our customers through the process. The Claims Specialists are now out on site regularly, throughout both the documentation and construction phases. As a result, we are better able to identify issues, troubleshoot and look for appropriate solutions to help move a claim forward.

Ongoing operational integration between Arrow and Southern Response

With the closure of the Company's Auckland operation at the end of 2014 and transfer of the functions back to Christchurch, the opportunity to co-locate fully with Arrow was taken. In many respects the companies operate as one, enabling a united insurance and build response to be presented to customers with the objective of providing a seamless experience. The performance metrics and values for both companies are similar. This approach is unique in the recovery sector.

A project office environment was introduced in 2014, which has contributed to accountability and greater visibility across both companies, enabling a granular perspective of throughput targets and providing for solution-focused operations.

Building in difficult land conditions

The Company's TC3 strategy launched in September 2012 has provided an opportunity for customers on TC3 land to feel more confident about the future.

To date, the proportion of TC3 customers who have made a settlement election decision is comparable to those in any other land zones. Nearly 85% of customers whose properties are on land categories TC2 and TC3 who have notified a claim to us have made a settlement election decision and of those, 66% in each land category have built or are building with us.

A good rate of progress can also be observed in the technically complex areas of the Port Hills.

Health and safety

We continue to be vigilant and committed to health and safety. At a Board and management level within both Southern Response and Arrow, a health and safety framework has been established to

provide for an end-to-end supply chain response to the challenges of achieving an accident free environment. Whereas the builders and professionals associated with our programme are aligned in their objectives for safety, the extended supply chain (including sub-contractors and their sub-contractors) makes achieving uniform outcomes an ongoing challenge. We continue to strive for a zero harm environment where we contribute to a positive legacy, both within the project and across the wider residential rebuild. Our commitment to health and safety in the residential recovery includes:

- A Board sub-committee dedicated to health and safety and regular Board time on the many issues, including site inspections and feedback to the contractors
- Specific health and safety Key Performance Indicators (KPIs) for Arrow and statistical assessment of the safety performance of contractors
- Builder and building site audits conducted by Arrow and external providers, providing health and safety evaluations and better practice input to the contractors involved
- Leading best practice in the industry with contractor awareness training seminars and a zero tolerance to poor health and safety practices and performance on sites
- Progressive infiltration of health and safety awareness and good practice throughout the supply chain
- Health and Safety awards across various build contractor work streams
- Membership of the Canterbury Rebuild Safety Charter, which is also encouraged and promoted within our supply chain
- Establishing contractual responsibilities for all contractors, including engineers and designers, to adhere to good health and safety practice and adhere to their legislative obligations when working for us.

Managing complex situations for our customers

The combination of the unique open-ended insurance cover and the very complex environmental issues (poor quality land, flood-prone areas, contamination, uncontrolled fill) continues to challenge progress. With many decisions to be made and often heightened levels of frustration, these issues require careful management. We seek to keep all customers well informed through transparent communication and additional initiatives to support the claim settlement process.

Removing the roadblocks

A dedicated team (called the Solutions Team) which was set up in 2014 has delivered key benefits in reviewing and addressing claims. The claims typically notified to the Solutions Team are those which present technical challenges more complex than standard cases, or where differing expert opinions are presented and need to be reconciled.

In a move to improve the efficiency of such reviewing processes, a weekly claims clinic has been implemented. The claims clinic is a multi-disciplinary internal panel that builds on collective knowledge, experience and authority of its members to make key decisions and develop flexible responses to claim scenarios, where the standard approach or the conventional policy interpretation is not sufficient to resolve the issues hindering the claim's progress.

The aim of those initiatives is to develop agile, innovative solutions to address any issues which arise with individual claims or classes of claim. This allows the claim to progress, potentially avoiding a formal dispute situation.

Disputes and complaints

The strategy and operations in the management of disputes continue to evolve. During the year we continued with the qualitative easing initiatives which began in the previous year to bring about fair and reasonable resolution of claims.



The Technical Review and Resolution area of the business has been reorganised to separate litigated disputes which are subject to Court proceedings from the remaining disputes where resolution is being sought through a direct negotiation with the customer and their advocate.

To date, 58% of all disputes lodged with us have been resolved. The open dispute rate remains at approximately 4% of all claims. Customer disputes are primarily resolved through initial internal review and subsequent negotiation. Facilitated mediation is becoming a strong feature of claim resolution; through the Courts, the Residential Advisory Service and through the community group CanCERN's Breakthrough programme.

External resolution or mediation services

The Residential Advisory Service (RAS) continues to provide full representative services to customers who seek them. We actively promote RAS as a dispute resolution pathway which provides the necessary advocacy and technical advice to customers to address any disagreements.

We also encourage customers to use the Insurance and Savings Ombudsman service (ISO) to seek resolution prior to formal proceedings. The parties agree to utilise negotiation, conciliation,

or mediation. We voluntarily removed the \$200,000 cap to allow unfettered access for customers to the Insurance and Savings Ombudsman scheme, extended indefinitely after a successful 6-month trial.

We have begun using facilitated meetings and mediation services with mutually agreed mediators as an alternative to Court, and have reached successful resolution of 23 cases in this manner before they proceeded to trial. Our share of the High Court Earthquake List remains broadly in line with market share.

We have not discounted other services which provide active opportunities to bring about resolution, although there is still concern surrounding services that seek a contingency fee or a commission for outcome. Of significant risk to the recovery is the disproportionate number of disputed claims in which the customer is represented by advocates seeking highly inflated settlements and setting unrealistic expectations of the likely outcome. Such circumstances potentially place the customer in a disadvantaged position, both financially and in terms of the additional time to resolve their claim with finite mediation and Court resources available.

Policy changes

We continue to assess the currency of Company policies in light of previous experience. This is exemplified by the modification of the disputes management policy to consider customers' costings of individual items provided there is fair, reasonable and credible evidence to support their claim.

On 22 July 2015, the Supreme Court delivered its decision in *Avonside Holdings*¹, upholding the Court of Appeal's ruling with regard to professional fees and contingency costs payable to customers who elect to buy another house or to enter into a cash settlement for self-managed rebuilds and repairs.

Pursuant to the Supreme Court ruling, the Board endorsed a policy decision that a full 10% contingency allowance and a full allowance for actual or estimated professional fees² will apply to all settlements from 1 October 2014 for costs not already incurred.

We previously stated that for any settlement agreement entered into after the Court of Appeal's decision on 1 October 2014, contingencies and professional fees would be addressed once the result of the appeal was known (to the extent not already provided for). Accordingly, we are working with customers who entered into settlement agreements on or after 1 October 2014 to identify the appropriate amounts payable in light of the Supreme Court's decision.

Vulnerable customers

Our Customer Support team is a fully dedicated team continuing to provide end-to-end services for the growing portfolio of vulnerable customers, who need additional support throughout the claims process. The team includes four Customer Liaison Advisors with backgrounds in social and health services who are able to provide specialist assistance to those affected customers. Working alongside families and organisations such as Canterbury Earthquake Temporary Accommodation Service (CETAS), Canterbury Communities' Earthquake Recovery Network (CanCERN) and other external support agencies, the Customer Support team endeavours to find the most appropriate



outcome for each of their customers, providing support every step of the way.

Due to increasing demand we continue to strengthen the team's capacity and capabilities, including the employment of additional specialists who are all well equipped to assist this particular group of customers.

Customers with shared title properties

Many of our customers are part of a shared property³.

These are often complex situations, with multiple repair/rebuild methodologies, multiple insurers and multiple owners. We have an established Shared Property team that specialises in this multifaceted area, working with all parties including owners, other insurers, loss adjusters, project managers and contractors to progress these claims. An agreed process has been implemented between insurers for managing this work as smoothly and efficiently as possible. The agreed process includes working with external loss adjusters, use of a standardised construction contract, and the insurer with the majority of the properties in the complex taking the lead on joint projects.

¹ SC 118/2014

² Although in *Avonside*, which was an architectural build, professional fees of 10% were allowed, the extent of professional fees to be calculated for each of the affected customers will vary depending on both the costs incurred (that were effective and useful to date) and the nature of the insured house's construction (for example, group home or architectural home).

³ Shared property involves customer dwellings that are adjoined to one another or otherwise have shared titles.

Enhanced customer communications

We maintain our commitment to achieving the right claim settlement outcomes for customers by communicating with them directly. To date, almost 4,700 customers who chose to work with us have settled their house claims directly with us.

During the year, we increased our focus on improving communication and direct interactions with customers. This will continue to evolve as we support our customers in moving forward.

Claims Specialist assignment

Each over cap customer has been assigned a dedicated Claims Specialist, rather than a team approach. The Claims Specialist acts as the key point of contact for the customer, keeping them informed and fielding any questions or concerns from the customer with regard to the policy, claim, or the repair or rebuild process. The Claims Specialists are supported by Project Managers from Arrow whose job is to guide the customer through the design, consenting and construction phases, working alongside the builder and other experts involved.

Improvements in face-to-face communication

We continue to invest in resources to ensure that customers' questions and concerns about the next steps can be answered in face-to-face meetings. Sitting down with the right people can be valuable in terms of helping to get the claim moving.

Customer e-newsletters

A new communication channel has been introduced to deliver direct and timely group email communication. These e-newsletters help us to inform over cap customers, providing monthly information, news and initiatives to support them through the process.

Enhanced Southern Response website

A redesign of the website and refresh of content occurred during the year to improve the functionality, responsiveness and engagement for customers. New additions have included a



document library, where all documents can be easily found in one place, and informative videos, including customer stories and process videos.

Customer portal

Soon after the start of the financial year, we introduced the online 'customer portal', a simplified version of Arrow's project management and monitoring tool. The aim of this feature is to provide Arrow-managed over cap repair and rebuild customers with a view of the status and progress of their builds or repairs, with web-based access protected by a secure sign-in process. The system is real-time and is a very positive step forward in communicating with customers throughout the build process, providing them with visibility of their own individual build progress.

Customer-focused supportive material

The diverse range of channels used for communications has seen the introduction of a number of new initiatives to support customers through the process and with their decision making.

These include:

- **'From Here To Home' book**

An informative guide to the claim settlement process to help prepare and support customers from beginning to end, providing clarity each step of the way. A similar book, tailored specifically for shared property, has also been developed. Both are available on our website

- **Repair packs**

An informative pack for repair customers, also serving as a document storage system. The pack outlines the repair process in detail through a repair map, and explains the significance of relevant reports that customers can expect to receive during their repair process

- **Factsheets**

Informative factsheets for customers, detailing different foundation repair methodologies and processes, designed to provide customers with more clarity and confidence regarding their claim.

Initiatives

The Cantabrian

The Cantabrian TC3 concept home came about after we ran a design competition in association with the New Zealand Institute of Architects in 2013, and was opened to the public in 2014.

After more than 4,000 visitors came through the doors over a 12 month period seeking ideas and inspiration, the concept home



closed at the end of March 2015. It is now transitioning into the next phase of becoming a home, one of the Housing New Zealand stock.

ROVER

ROVER is the all-terrain miniature under-floor camera survey robot, which was developed and implemented as part of our ongoing commitment to the repair programme.

The quality assurance that a ROVER-assisted repair provides is very valuable for us and our contractors, as well as homeowners, who can feel confident that their repair will be completed to a compliant standard. The successful outcome for us from an industry survey conducted by the Ministry of Business, Innovation and Employment into earthquake repairs is testament to the scrutiny we apply to our programme.

To date, ROVER has been involved in well over 1,000 repair inspections.



Global resource consent for contaminated land

In essence, through our own global resource consent, we engage directly with geotechnical consultants to test the soil, develop the plan and undertake monitoring of the processes.

This consent, granted during the financial year, leads to greater efficiencies in consenting and in elapsed time throughout the identification, testing and remediation work. We provide consistent expectations to contractors on how they manage contaminants that pose a risk to human health with control measures around managing health and safety of workers, controlling risk to the environment and correctly disposing of contaminated material.

Preferred repairer and builder arrangements

The volume group repairers' and builders' panel arrangements, originally entered into in 2013, expired during the year. In their place, relationship agreements have been developed under which guaranteed volume arrangements will not apply to either group going forward. Instead, quarterly allocations will be based on performance of the individual panel members.

There have been changes to both panels due to the length and extent of the build pipelines and the experience with the contractors over the previous two years.

Financial summary

Key aspects of Southern Response's financial results are outlined below.

	2015 \$000	2014 \$000
Continuing operations		
Net earthquake claims incurred	(339,826)	(148,229)
Other costs	(350)	431
Investment income	15,898	23,531
Unrealised gain on fair value of Crown receivable	14,846	8,514
Loss for the year from continuing operations	(309,432)	(115,753)
Other comprehensive income	0	0
Total comprehensive loss for the year	(309,432)	(115,753)
Claims liability		
Discounted central estimate (including claims handling expenses)	1,106,626	1,305,730
Risk margin	108,907	127,114
Gross outstanding claims liabilities	1,215,533	1,432,844
Reinsurance receivables	(100,754)	(183,483)
Net outstanding claims liability	1,114,779	1,249,361

The following table shows the movement in the central estimate of the claims liability since the 30 June 2011 year end reflecting increasing claims numbers and the expanding technical challenge of the rebuild.

\$000	2011	2012	2013	2014	2015
Central estimate	1,819,180	2,157,415	2,254,417	2,364,388	2,716,207



We're back, and this
is our forever home



Appreciation

We acknowledge the continued commitment and contribution of our dedicated staff, Arrow International staff, our build panel and technical consultants. Based in Christchurch, staff are living in the same environment as customers, one which is often challenging, and they remain loyal and committed in difficult, sometimes strained circumstances.

We appreciate the support and willingness of community support groups, local government, professional bodies, sector groups, local MPs and their electorate staff, iwi and customers (in meetings, seminars and focus groups) to serve as communication conduits to the community. The feedback, support and suggestions provided

continue to assist with developing and refining our position on a range of issues.

We are thankful for the relationships with the Insurance Council and government agencies which are key to the earthquake recovery. These connections are beneficial in seeking the best outcomes for customers and the community at large. We appreciate the presence of CERA and EQC as close partners; Housing New Zealand for continuing collegueship and support for initiatives such as the Cantabrian concept house; and the Ministry of Business, Innovation and Employment for advanced technical guidance. We are also grateful for the support received from the Treasury's Commercial Operations group as the Crown's monitoring agent.

Governance

We acknowledge the dedication of our Board, which brings a collective sense of commitment, sensitivity, and technical knowledge to the governance table. Since the change of ownership to the Crown on 5 April 2012 and the commencement of annual reporting as a Crown-owned entity, our Board and management have continued to enhance the governance framework around the Company, to ensure optimum accountability and integrity for the substantial financial commitment that the Crown and reinsurers have made to the Company.

We have adopted a full suite of policies which provide guidance and direction to our Board and management.

Overcoming challenges and future outlook

Having largely completed the insurance decision phase, the Company's key areas of focus in the 2015-2016 year are:

- Continuing to settle effectively with our customers such that 75% of those claims notified up to June 2015 will have been fully settled by June 2016
- Continuing to communicate effectively with customers and other stakeholders. We will continue to enhance operational communication initiatives, providing staff with tools to build and maintain confidence for our customers who are still working through the claims settlement process
- Executing fully on the 2014-15 'Repairs Pilot'⁴ and implementing any further learnings gained in the Repairs Pilot to the rest of the business, to optimise the delivery of repair numbers into construction or an alternative settlement path. Ensuring repairs that are in construction are delivered in a timely manner and with quality workmanship is also a key deliverable
- Minimising the potential for contractor failure on our build programme and mitigating the impact if it does occur

- Leading industry in quality management and health and safety systems and performance consistent with legislative and regulatory obligations
- Executing on strategies to reduce dispute numbers
- Continuing with the effective delivery for shared property claims including learning from experience. This includes sharing any intellectual property developed with the rest of the insurance industry, as this will ultimately be for the benefit of our customers who will have their shared property claim managed by other insurers
- Managing the commencement of the run-down of the business, with minimum effect on customers and staff.



Ross Butler

Ross Butler
Chairman



Peter Rose

Peter Rose
Chief Executive Officer

17 August 2015

⁴The Repairs Pilot, now operationalised as business as usual, is an initiative that involves providing more intensive Southern Response Claims Specialist resource, accompanied by aligned Project Management support and adaptable build solutions, to assist customers along their preferred claim settlement path of either construction or a self-managed repair.

Our values

Respect

We treat all our stakeholders with care, consideration, fairness and equity.

Integrity

We demonstrate honesty, transparency, fairness, and objectivity in all our interactions.

Honour our promises

We stand by and deliver on all entitlements, rights and commitments AMI has made to policyholders.

Ownership

We hold ourselves accountable for our actions, take ownership, and deliver on our promises.

Passion

We strive, stand up for our customers' rights, and go the extra distance. We want to make a positive difference to people's lives as part of our contribution to the rebuild of Canterbury.

Excellence

We are committed to excellence in everything we do. We are innovative, responsive, adaptive and continually raising the bar. We strive to set the standard against which others will be measured.

Recognition

We recognise and celebrate the contributions our people make as individuals and as teams to deliver on our goals.

Development

We professionally develop our people to provide challenging and rewarding employment and prospects.



Working together to
get people back home

Board of Directors



Ross Butler - *Chairman*

Christchurch born and educated, Ross Butler is a professional Director, with a range of governance roles on commercial, Crown entity, sporting, and community Boards and trusts. After spending most of his executive and governance career in financial service and insurance entities in Australia, Ross is now based in Nelson.

He is currently Chairman of Nelson Marlborough Institute of Technology and Mercer New Zealand, Director of Rangitane Holdings Limited and Rangitane Investments Limited, and a Member of the Code Committee (Financial Advisers Act). Ross is also a Director of Mercer Investments Australia Pty Ltd and has previously been deputy Chair, and Chair of Audit and Risk Committee, of GNS Science.



Anne Urlwin - *Deputy Chairman*

Originally from Christchurch, Wanaka based Anne Urlwin has more than 20 years experience as a professional Director, Chartered Accountant and business consultant in an extensive range of sectors. Anne also has senior management experience in the corporate sector including in the IT and meat industries.

Anne is currently Chairman of commercial construction group Naylor Love. She became a Director of Chorus Ltd upon the Telecom demerger in late 2011. She is also a Director of Steel & Tube Holdings Ltd, Summerset Group Holdings and One Path Life (NZ) Ltd, an ANZ Bank subsidiary Company.



Jenn Bestwick

Jenn Bestwick's professional career has been largely in strategy and business development and includes previously leading the strategic consulting practice for KPMG in Auckland.

Since moving to Christchurch in 1996, Jenn has worked for Ngai Tahu Holdings Group and with local authorities, iwi and the primary and hydro-generation sectors on fresh water management in the Canterbury region.

Jenn is currently Chair of Christchurch Polytechnic Institute of Technology, a Board member of Tourism New Zealand and Advisory Panel member for Development West Coast.



Bevan Killick

Christchurch born and educated, Bevan Killick is a Chartered Accountant and a Chartered Insurance Practitioner (UK).

During his professional career, Bevan held senior positions in the Lloyd's Insurance Market for 12 years. Now based back in Christchurch, Bevan is a professional Director where his roles include being Chairman of St John of God Hauora Trust and Director of Royal Society of the Arts, Australia and NZ.

In the post-earthquake era Bevan also worked with Recover Canterbury, the organisation responsible for helping businesses recover from the Canterbury earthquakes.



Susan Thodey

Susan Thodey is admitted as a barrister and solicitor in New Zealand and as a solicitor in England. She is presently the managing partner of the Auckland based partnership of Heaney & Partners. She will leave the partnership on 30th September 2015 and after that date act as a consultant.


For the past 25 years Susan has been employed by local and overseas insurance companies to advise on a wide range of insurance related matters including policy advice and claims management. She has also acted for local government with an emphasis in recent years on construction disputes.



Sarah Sinclair

Sarah is a chartered civil engineer, a Fellow of the Institute of Civil Engineers (UK) and a Fellow of IPENZ (The Institution of Professional Engineers New Zealand). She has over 20 years experience in infrastructure in New Zealand and the UK. She is a Director of IPWEA NZ.

After working in an engineering consultancy managing design and delivery, Sarah is now Chief Engineer at Auckland Council. She has a strong interest in sustainable and resilient infrastructure.



It's good to
be home



Governance

Southern Response is incorporated as a limited liability Company under the Companies Act 1993, and is listed in Schedule 4A of the Public Finance Act 1989, which automatically makes it subject to many of the provisions of the Crown Entities Act 2004.

The Company became a Crown entity on 5 April 2012 when its shareholders became the Minister of Finance and the Minister for Canterbury Earthquake Recovery. On 5 April 2012 the Company's name changed from AMI Insurance Ltd to Southern Response Earthquake Services Ltd.

Company activities

Until the sale of its fire and general insurance business to IAG (NZ) Holdings Limited on 5 April 2012, the Company's principal activities, while operating under the name AMI Insurance, comprised the writing of fire and general business for the domestic property insurance market in New Zealand.

At 5 April 2012, the Company's principal activities changed to the management and settlement of insurance claims made by AMI policyholders relating to the Canterbury earthquake events up to 5 April 2012. Managing and settling the earthquake claims involves the Company in:

- Assessing and meeting Canterbury earthquake-related claims including managing all repair and rebuilding work;
- Recovering reinsurance and insurance proceeds, including liaising with the reinsurers and the Earthquake Commission;
- Managing the Company's funds and assets to enable settlement of claims.

The Company does not take on any new insurance business except to the extent that it is ancillary to its claims management business.

Governance framework

The Company's governance framework is designed to ensure that the Company is effectively managed and that statutory obligations are met. The governance framework ensures a clear understanding of the separate roles of Board and management, and demonstrates a shared commitment to the Company's purpose. The Board has delegated to the Chief Executive the day-to-day leadership and management of the Company.

The Board operates under Treasury's Owner's Expectations Manual which sets out the Ministers' expectations of the Board, including the reporting, accountability and financial governance expectations.

Board of Directors

The Board's duties, functions, and powers are governed by the Companies Act 1993, Southern Response's Constitution, the Crown Entities Act 2004, the Company's Statement of Intent and the Shareholders' Letter of Expectations.

The Crown Entities Act imposes the obligation on the Board to ensure that the Company operates in a manner consistent with its objectives, functions and Statement of Intent.

Directors

Under the constitution adopted on 5 April 2012, the Board is appointed by Shareholding Ministers and can comprise up to seven non-executive Directors, including the Chairman. As at 30 June 2015 there were six non-executive Directors of the Company whose appointment dates, terms and Board committee memberships are detailed in the following table.

Director	Position	Term	Board Committee Memberships
Ross Butler Nelson-based professional Director	Non-Executive Chairman	appointed 5 April 2012 reappointed 1 July 2014 term ends 30 June 2017	Member: Governance Committee Member: Capital Committee Member: Human Resources Committee
Anne Urlwin Wanaka-based professional Director	Deputy Chairman	appointed 5 April 2012 reappointed 1 July 2014 term ends 30 June 2016	Chair: Audit and Risk Committee Member: Governance Committee Member: Human Resources Committee
Jenn Bestwick Christchurch-based professional Director	Non-Executive Director	appointed 5 April 2012 reappointed 1 July 2014 term ends 30 June 2016	Chair: Human Resources Committee Member: Health and Safety Committee
Bevan Killick Christchurch-based professional Director	Non-Executive Director	appointed 5 April 2012 reappointed 1 July 2015 term ends 30 June 2017	Chair: Capital Committee Member: Audit and Risk Committee Member: Health and Safety Committee
Susan Thodey Queenstown-based barrister and solicitor	Non-Executive Director	appointed 5 April 2012 reappointed 1 July 2013 term ends 30 June 2016	Chair: Governance Committee Member: Audit and Risk Committee Member: Capital Committee
Sarah Sinclair Auckland-based Chartered Civil Engineer	Non-Executive Director	appointed 1 July 2014 term ends 30 June 2017	Chair: Health and Safety Committee

Board committees

To ensure efficiency, the Board specifically delegates some of its roles to Board committees under formal Terms of Reference which specify the role and responsibility of each committee and its delegated authorities.

With effect from 1 July 2014, the Board committees are:

- Audit and Risk Committee** – sets the principles and standards for financial reporting, the external audit function, maintenance of an effective internal control environment, legislative and contractual compliance and maintenance of an effective risk management environment
 Membership: Anne Urlwin (Chair), Bevan Killick, Susan Thodey
- Capital Committee** – oversees matters associated with insurance claims liabilities, reinsurance receivables, Earthquake Commission receivables and investments
 Membership: Bevan Killick (Chair), Ross Butler, Susan Thodey
- Human Resources Committee** – sets the principles and standards for key policies relating to recruitment and appointment, remuneration and retention and assists with the appointment of the CEO, the annual review of the CEO's performance and remuneration and considers professional development and training for the CEO
 Membership: Jenn Bestwick (Chair), Ross Butler, Anne Urlwin

- Governance Committee** – deals with Board administrative matters related to succession planning, Board performance review and professional development of Directors
 Membership: Susan Thodey (Chair), Ross Butler, Anne Urlwin
- Health and Safety Committee** – monitors compliance with the Health and Safety in Employment Act 1992 and ensures a best practice health and safety environment for Southern Response's staff, visitors and those involved in the delivery of Southern Response's rebuild activities including contractors, sub-contractors and homeowners
 Membership: Sarah Sinclair (Chair), Jenn Bestwick, Bevan Killick.

Disclosure of interests by Directors

The Board is conscious of its obligation to ensure Directors avoid conflicts of interest (both real and perceived) between their duty to Southern Response and their other interests. Directors are required to ensure they immediately advise the Board of any new or changed relationships, and these are recorded in the Board's interests register.

In accordance with the Companies Act 1993, the Board maintains an up-to-date interests register to ensure conflicts of interest are recorded and managed. The table on the following page details new interests or cessations of interests of Directors recorded in the interests register during the year ended 30 June 2015.

Director	Entity	Relationship
Ross Butler	Rangitane Holdings Limited and Rangitane Investments Limited	Director
Anne Urlwin	One Path Insurance Services NZ Ltd	Director (ceased)
Jenn Bestwick	State Services Commission	Lead Reviewer, PIF Panel
Bevan Killick	Royal Society of the Arts, Australia and New Zealand Institute of Directors, Canterbury Branch Taxcheck.co.nz Ltd Credit Union South (trading as NZCU South)	Director Committee member (ceased) Director (ceased) Chairman (ceased)
Susan Thodey	None	
Sarah Sinclair	Auckland Council IPWEA NZ Institution of Civil Engineers (ICE) New Zealand Committee	Chief Engineer Director Chair

There have been no interests registered by Directors in transactions during the financial year ended 30 June 2015.



Indemnities and insurance

As permitted by Southern Response's Constitution, deeds of indemnity have been given to Directors for potential liabilities and costs they may incur for actions or omissions in their capacity as Directors.

The Company has Directors' and officers' liability insurance in place to cover risks usually covered by such policies. Insurance is not provided for dishonest, fraudulent, malicious or wilful acts or

omissions. The insurance premium paid during the year ended 30 June 2015 was \$84,000 relating to cover for the period 5 April 2015 to 5 April 2016.

Use of Company information

During the year the Board received no notices from the Directors requesting to use Company information received in their capacity as Directors and which would not otherwise have been available to them.

Glossary of terms as used in this report:

Commercial Operations Group (formerly Crown Ownership Monitoring Unit (COMU)): Treasury's Commercial Operations group monitors the government's investment in companies/entities owned by the Crown, assists with the appointment of Directors, and provides performance and governance advice to Ministers.

Crown support deed: A deed entered into by the Crown and AMI in April 2011 outlining the terms of the Crown's support for the Company. The deed was amended in April 2012 to reflect the increased Crown ownership of the Company.

Out Of Scope (OOS): items that are not covered under the Earthquake Commission Act 1993 including fences, driveways, patios, swimming pools.

Over cap: EQC insures the first \$100,000 + GST (\$115,000) of damage to a house (the "cap") for each earthquake event.

If the level of damage exceeds this for any one earthquake event, EQC pays its contribution for each event and the private insurance company takes over responsibility for managing and settling the claim and paying the amount in excess of the cap - that is "over cap".

Reinsurance: insurance purchased by an insurance company from one or more other special purpose insurance companies (reinsurers) to enable risks assessed to be spread.

Settlement election: a formal confirmation from the customer of their preferred method of claim settlement (if the house is beyond economic repair).

Statement of Intent: an outline of a Crown entity's expected contribution to the government's priorities over the medium term (3-5 years).

Back home and
starting afresh

Statement of responsibility

In accordance with the Public Finance Act 1989, the Board of Southern Response Earthquake Services Limited accept responsibility for:

- The preparation of financial statements and statement of performance and the judgements made in them;
- Establishing and maintaining a system of internal control designed to provide reasonable assurance as to the integrity and reliability of financial statements and the statement of performance.

In the Board's opinion, these summary financial statements and summary statement of performance fairly reflect the financial position and operations of Southern Response Earthquake Services Limited for the year ended 30 June 2015.

Signed on behalf of the Board



Ross Butler
Chairman
17 August 2015



Anne Urlwin
Deputy Chairman
17 August 2015

Independent Auditor's report



TO THE READERS OF SOUTHERN RESPONSE EARTHQUAKE SERVICES LIMITED SUMMARY FINANCIAL STATEMENTS AND SUMMARY STATEMENT OF PERFORMANCE FOR THE YEAR ENDED 30 JUNE 2015

We have audited the summary financial statements and summary statement of performance as set out on pages 31 to 51, which were derived from the audited financial statements and statement of performance of Southern Response Earthquake Services Limited (the Company) for the year ended 30 June 2015 on which we expressed an unmodified audit opinion in our report dated 17 August 2015.

The summary financial statements comprise the summary statement of financial position as at 30 June 2015, and summaries of the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, the related notes and the summary statement of performance.

Opinion

In our opinion, the information reported in the summary financial statements and summary statement of performance complies with FRS-43: Summary Financial Statements and is consistent in all material respects with the audited financial statements and statement of performance from which they have been derived.

The following emphasis of matter paragraphs were included in the Auditor's report on the financial statements of the Company for the year ended 30 June 2015.

"The Company's ability to access additional share capital

Without modifying our opinion, we draw attention to the disclosure in note 1 of the financial statements about going concern. As at 30 June 2015, the liabilities of the Company exceeded its assets by \$420 million. The Directors have concluded that the going concern assumption is appropriate given the funding arrangements available under the Crown support deed which is described in note 8 of the financial statements. Under the Crown support deed, the Company is able to access up to \$500m of additional share capital from the Crown.

Uncertainties associated with the outstanding claims liability

Also without modifying our opinion, we draw your attention to notes 1, 2 and 16 of the financial statements. Those notes describe how the Canterbury earthquakes have affected the outstanding claims liability of the Company. Those notes also describe the significance of the amount of the earthquake related outstanding claims liability, and the inherent uncertainties involved in estimating this amount using actuarial assumptions."

Details of the above matters are outlined in Notes 1, 2, 5 and 9 of the summary financial statements.

Basis of opinion

The audit was conducted in accordance with the Auditor-General's Auditing Standards, which incorporate the International Standards on Auditing (New Zealand).

The summary financial statements and summary statement of performance and the audited financial statements and statement of performance from which they were derived, do not reflect the effects of events that occurred subsequent to our report dated 17 August 2015 on the audited financial statements and statement of performance.

The summary financial statements and summary statement of performance do not contain all the disclosures required for audited financial statements and statement of performance under generally accepted accounting practice in New Zealand. Reading the summary financial statements and summary statement of performance, therefore, is not a substitute for reading the audited financial statements and statement of performance of the Company.

Responsibilities of the Board of Directors and the Auditor

The Board of Directors are responsible for preparing the summary financial statements and summary statement of performance in accordance with FRS-43: Summary Financial Statements. The Board of Directors is also responsible for the publication of

the summary financial statements whether in printed or electronic form. We are responsible for expressing an opinion on those statements, based on the procedures required by the Auditor-General's auditing standards including International Standard on Auditing (New Zealand) 810: Engagements to Report on Summary Financial Statements.

Other than in our capacity as Auditor, we have no relationship with, or interests in, the Company. Partners and employees of our firm deal with Southern Response Earthquake Services on normal terms within the ordinary course of trading activities of the business of Southern Response Earthquake Services.

Michael Wilkes
Deloitte
On behalf of the Auditor-General
Christchurch, New Zealand
17 August 2015

Statement of comprehensive income

For the year ended 30 June 2015

		2015 Budget	2015 Actual	2014 Actual
	Note	\$000	\$000	\$000
Net claims incurred – non-earthquake		-	(282)	484
Net claims incurred - earthquake	3	(16,343)	(339,826)	(148,229)
Less operating costs		-	(68)	(53)
Net underwriting loss		(16,343)	(340,176)	(147,798)
Investment income and expenses		9,369	15,898	23,531
Unrealised gain on fair value of Crown receivable	8	13,025	14,846	8,514
Profit/(loss) for the year before tax		6,051	(309,432)	(115,753)
Tax expense		-	-	-
Profit/(loss) for the year after tax		6,051	(309,432)	(115,753)
Other comprehensive income:				
Other comprehensive income for the year after tax		-	-	-
Total comprehensive profit/(loss) for the year		6,051	(309,432)	(115,753)

The accompanying notes and accounting policies form an integral part of the financial statements.

Statement of changes in equity

For the year ended 30 June 2015

2015	Ordinary Shares	Convertible Preference Shares	Accumulated Losses	Property Revaluation Reserve	Total Equity/ (Deficit)
	\$000	\$000	\$000	\$000	\$000
Opening balance 1 July 2014	95,580	382,359	(590,693)	2,052	(110,702)
Loss for the year	-	-	(309,432)	-	(309,432)
Other comprehensive income for the year	-	-	-	-	-
Total comprehensive income for the year	-	-	(309,432)	-	(309,432)
Closing balance 30 June 2015	95,580	382,359	(900,125)	2,052	(420,134)
2014	Ordinary Shares	Convertible Preference Shares	Accumulated Losses	Property Revaluation Reserve	Total Equity/ (Deficit)
	\$000	\$000	\$000	\$000	\$000
Opening balance 1 July 2013	95,580	382,359	(474,940)	2,052	5,051
Loss for the year	-	-	(115,753)	-	(115,753)
Other comprehensive income for the year	-	-	-	-	-
Total comprehensive income for the year	-	-	(115,753)	-	(115,753)
Closing balance 30 June 2014	95,580	382,359	(590,693)	2,052	(110,702)

The accompanying notes and accounting policies form an integral part of the financial statements.

Statement of financial position

As at 30 June 2015

		2015 Budget \$000	2015 Actual \$000	2014 Actual \$000
	Note			
Shareholders' equity				
Total shareholders' deficit		(51,302)	(420,134)	(110,702)
Represented by:				
Assets				
Financial assets				
Cash and cash equivalents		22,431	198,284	135,442
Receivables		1,968	10,352	12,167
Reinsurance receivables	6	16,138	101,802	183,748
Investments	7	-	100,056	620,209
Crown receivable	8	369,736	387,909	373,063
Property held for sale		-	2,280	3,591
Property, plant and equipment		1,549	1,117	1,432
Intangible assets		-	46	46
Total assets		411,822	801,846	1,329,698
Less:				
Liabilities				
Trade and other payables		6,263	3,834	4,388
Employee entitlements		-	1,732	2,299
Outstanding claims – non-earthquake		-	881	869
Outstanding claims – earthquake	9	456,861	1,215,533	1,432,844
Total liabilities		463,124	1,221,980	1,440,400
Net liabilities		(51,302)	(420,134)	(110,702)

On behalf of the Board

Ross Butler, Chairman
Authorised for issue on 17 August 2015

Anne Urlwin, Director

The accompanying notes and accounting policies form an integral part of the financial statements.

Statement of cash flows

For the year ended 30 June 2015

		2015 Budget \$000	2015 Actual \$000	2014 Actual \$000
	Note			
Cash flows from operating activities				
Interest received		9,370	16,710	22,950
Dividends received		-	27	179
Other investment income		-	-	1,050
Claim costs – non-earthquake		-	(1,053)	(575)
Claim costs – earthquake		(864,989)	(547,605)	(385,380)
Claim costs – reinsurance recoveries		199,716	101,548	291,397
Payments to suppliers and employees		(27,011)	(25,541)	(26,207)
Net cash outflow from operating activities	4	(682,914)	(455,914)	(96,586)
Cash flows from investing activities				
Proceeds from sale of property, plant and equipment and property held for sale		-	27	4,004
Payments for property, plant and equipment and property held for sale		(125)	(325)	(910)
Payments for intangible assets		-	(71)	(58)
Sales and maturities of financial assets		630,000	519,125	53,109
Net cash inflow from investing activities		629,875	518,756	56,145
Cash flows from financing activities				
Proceeds from the Crown receivable		22,000	-	-
Net cash inflow from financing activities		22,000	-	-
Net (decrease)/increase in cash and cash equivalents		(31,039)	62,842	(40,441)
Add opening cash and cash equivalents		53,470	135,442	175,883
Ending cash and cash equivalents		22,431	198,284	135,442

The accompanying notes and accounting policies form an integral part of the financial statements.

Notes to the summary financial statements

For the year ended 30 June 2015

1. Summary of accounting policies

Reporting entity

Southern Response Earthquake Services Limited (the Company) is a limited liability Company incorporated and domiciled in New Zealand and registered under the Companies Act 1993.

The Company is a Crown-owned Company listed in schedule 4A of the Public Finance Act 1989. The registered office for the Company is located at 6 Show Place, Addington, Christchurch.

The Company's principal business is to manage the settlement of claims from AMI Insurance customers arising from the Canterbury earthquakes occurring between 4 September 2010 and 5 April 2012. It also manages an investment portfolio.

The financial statements for the Company were authorised for issue by the Directors on 17 August 2015.

Basis of preparation

The summary financial statements and summary statement of performance have been extracted from the full financial statements and statement of performance and have been prepared in accordance with FRS 43 – Summary Financial Statements.

The full financial statements have been prepared in accordance with Generally Accepted Accounting Practice in New Zealand (NZ GAAP) and also in accordance with the Financial Reporting Act 2013 and the Companies Act 1993. They comply with the New Zealand equivalents to International Financial Reporting Standards (NZ IFRS), International Financial Reporting Standards (IFRS) and other applicable financial reporting standards as appropriate for profit oriented companies.

The summary financial statements are presented in the Company's functional currency of New Zealand dollars and, unless specifically stated otherwise, are rounded to the nearest thousand dollars (\$000).

External Reporting Board Standard A1: Accounting Standards Framework (For-profit Entities Update) "XRB A1". XRB A1 establishes a for-profit tier structure and outlines which suite of accounting standards entities in different tiers must comply with. The Company has elected to report as a Tier 1 entity.

Accounting policies have been consistently applied and there have been no changes in accounting policies during the period under review.

The summary financial statements cannot be expected to provide as complete an understanding of the financial affairs of the Company as the full financial statements, which can be found on www.southernresponse.co.nz.

Going concern

The Directors have considered the appropriateness of the financial statements being presented on a going concern basis and have concluded that the going concern assumption is appropriate given the funding arrangements available under the Crown support (note 5).

2. Critical accounting judgements and estimates

The Company makes estimates and assumptions 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. The key areas in which critical estimates and judgements are applied are described below.

The ultimate liability arising from earthquake claims made under insurance contracts

Provision is made at the year-end for the estimated cost of claims incurred but not settled at the reporting date, including the cost of claims incurred but not yet reported to the Company. The estimation of the outstanding claims liability involves a number of key assumptions and is the most critical accounting estimate.

The estimated ultimate cost of claims includes direct costs to be incurred in settling claims, gross of the expected value of salvage and other recoveries. The Company 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 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 Company, where more information about the claim event is generally available.

In calculating the estimated ultimate cost of unpaid claims the Company uses an actuarial valuation carried out by an independent actuary. Refer note 9.

Assets arising from reinsurance contracts

Assets arising from reinsurance contracts are computed using actuarial valuations. 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 Company may not receive amounts due to it and these amounts can be reliably measured. Refer note 6.

Valuation of the Crown receivable

The Crown receivable is recorded at the fair value of projected cash flows based on forecast payments of claim settlements and operating costs. Refer note 8.

3. Net claims incurred

	2015	2014
	\$000	\$000
Earthquake:		
Gross claims expense	358,644	110,936
Reinsurance recovery expense/(revenue)	(18,818)	37,293
Total net earthquake claims incurred	339,826	148,229
Total net claims incurred	340,108	147,745

4. Cash flows from operating activities

Reconciliation of profit/(loss) for the year to cash inflows from operating activities:

	2015 \$000	2014 \$000
Loss for the year	(309,432)	(115,753)
Add/(less) non-cash items:		
Depreciation and amortisation	586	655
Unrealised losses/(gains)	1,372	(145)
Unrealised movement in discounting Crown receivable to fair value	(14,846)	(8,514)
Sub-total "A"	(322,320)	(123,757)
Movement in working capital items:		
Decrease in receivables	1,815	10,851
Decrease in reinsurance and insurance receivables	81,946	328,561
Decrease in payables	(554)	(3,573)
(Decrease)/increase in employee entitlements	(567)	953
Decrease in insurance liabilities	(217,299)	(310,270)
Sub-total "B"	(134,659)	26,522
Items classified as investing activities:		
Decrease in interest receivable capitalised	997	596
Net loss on sale of property, plant and equipment	68	53
Net loss on sale of investments	-	-
Sub-total "C"	1,065	649
Cash outflow from operating activities (A+B+C)	(455,914)	(96,586)

5. Share capital

The Company has ordinary share capital of \$95 million and convertible preference capital of \$382 million. As explained below, as it requires additional capital to meet its claims payment obligations the Company can access a further \$500 million of capital from the Crown.

	2015 \$000	2014 \$000
Ordinary shares:		
Balance 1 July and 30 June	95,580	95,580
Convertible preference share capital:		
Balance at 1 July and 30 June	382,359	382,359

At 30 June 2015, there were 1,000,102 (2014: 1,000,102) ordinary shares, 400,000,000 (2014: 400,000,000) unpaid convertible preference shares and 500,000,000 uncalled ordinary shares (2014: 500,000,000). The issue price of the uncalled ordinary shares (yet to be called) is \$1 per share.

Under the terms of the deed of amendment and restatement to the Crown support deed dated 5 April 2012, once all other assets are utilised to settle claims, the Company may issue a payment notice for a number of unpaid convertible preference shares. On payment the shares will be designated as paid-up convertible preference shares. Such shares are convertible into ordinary shares at the option of the convertible preference shareholder.

Each paid-up convertible preference share will rank equally in respect of dividends and other distributions with all ordinary shares.

Under the terms of the second deed of amendment and restatement to the Crown support deed, dated 30 January 2013, the Crown subscribed for 500,000,000 uncalled ordinary shares. The issue price of the uncalled ordinary shares (yet to be called) is \$1 per share. Following the payment or redemption of all convertible preference shares, the Company may issue a call notice for a number of uncalled ordinary shares. On payment the shares will be designated as paid ordinary shares.

6. Reinsurance receivables

	2015 \$000	2014 \$000
Gross reinsurance receivable	103,463	191,210
Discount to present value	(1,661)	(7,462)
	101,802	183,748
Being:		
Non-earthquake	1,048	265
Earthquake (note 9)	100,754	183,483
	101,802	183,748
Changes in gross reinsurance receivable:		
Balance 1 July	191,210	527,435
Change in gross estimated recovery	13,800	(44,827)
Reinsurance collections	(101,547)	(291,398)
Balance 30 June	103,463	191,210

At 30 June 2015, the Company conducted an impairment review of the reinsurance receivables. No loss was recognised (2014: \$nil).

7. Investments

	2015 \$000	2014 \$000
New Zealand Government Treasury bills	99,753	579,075
Other fixed interest securities	-	40,759
Equity securities	303	375
	100,056	620,209

8. Crown receivable

	2015 \$000	2014 \$000
Opening Balance at 1 July	373,063	364,549
Fair value adjustment at 30 June	14,846	8,514
Closing balance at 30 June	387,909	373,063

The Company has entered into arrangements with the Crown to ensure that the Company has adequate funds available to meet payments of operating expenses and claim settlements as they fall due.

On 7 April 2011, the Company entered into a Crown Support Deed and subscription agreement with the New Zealand Government (the Crown) under which the Crown was issued 500 million convertible preference shares, one special share and one ordinary share. These shares were called but not paid up.

On 5 April 2012 a deed of amendment and restatement to the Crown support deed was signed with the Crown. At this time the Crown paid up 100 million convertible preference shares and converted these to 1 million ordinary shares.

The Company may draw down the Crown receivable by issuing a payment notice for a number of unpaid convertible preference

shares equal to the shortfall amount in any quarter, being the shortfall between the cumulative balance of the Company's reinsurance receivables and financial investments less \$25 million and less any payments of operating expenses and claim settlements forecast to be made in that quarter in the ordinary course of its business.

The Crown receivable as at 30 June 2015 is recorded at its fair value taking into account all relevant circumstances including the timing of the forecast cash flows and the terms of the Crown support deed. The risk free discount rates used are in the range of 2.87% to 3.03% (30 June 2014: 3.77% to 3.94%). Cash flows of \$400 million within 2 years have been assumed (30 June 2014: \$400 million within 3 years).

9. Outstanding earthquake claims liability

	2015	2014
	\$000	\$000
Outstanding earthquake claims		
Discounted central estimate outstanding	1,057,907	1,242,807
Risk margin	108,907	127,114
Claims handling costs	48,719	62,923
Gross discounted outstanding claims liability	1,215,533	1,432,844
Expected reinsurance recoveries	(102,415)	(190,945)
Impact of discounting on reinsurance recoveries	1,661	7,462
Reinsurance receivables (note 6)	(100,754)	(183,483)
Net outstanding claims liability	1,114,779	1,249,361

Changes in gross discounted outstanding claims liability		
Outstanding claims beginning of year	1,432,844	1,742,185
Change in central estimate	351,819	109,348
Change in claims handling expense	(14,204)	(9,313)
Change in discounting to present value	14,200	11,051
Change in risk margin	(18,207)	(23,434)
Claim payments	(550,919)	(396,993)
Outstanding claims end of year	1,215,533	1,432,844

Claims development

Below is a reconciliation of the central estimate to the net outstanding claims liability, reflected in the financial statements.

	2015	2014
	\$000	\$000
Central estimate	2,716,207	2,364,388
Claims handling expense	48,719	62,923
Cumulative payments	(1,618,269)	(1,067,350)
Discount of unpaid liability to present value	(40,031)	(54,231)
Discounted central estimate	1,106,626	1,305,730
Risk margin	108,907	127,114
Gross discounted outstanding claims liability	1,215,533	1,432,844
Reinsurance receivables (refer note 6)	(100,754)	(183,483)
Net outstanding claims liability	1,114,779	1,249,361

Actuarial calculation, assumptions and methods

The effective date of the actuarial report on the earthquake insurance liabilities is 30 June 2015. The actuarial report was prepared by the appointed actuary, Colin Brigstock (Fellow of the Institute of Actuaries of Australia and Fellow of the New Zealand Society of Actuaries) and peer reviewed by Karen Cutter (Fellow of the Institute of Actuaries of Australia) of Finity Consulting Pty Limited. Finity Consulting are satisfied with the quality of data provided for the purpose of estimating insurance liabilities.

In the actuary's opinion the insurance liabilities have been prepared in accordance with the New Zealand equivalents to International Financial Reporting Standard (NZ IFRS 4 Insurance

Contracts) and the NZ Society of Actuaries Professional Standard 4.1 governing technical liability valuations for general insurance business.

Key actuarial assumptions – earthquake

The valuation of the net outstanding claims liabilities for the current financial year is based on detailed assumptions about the number of properties damaged, the mix and cost of rebuilds/repairs/cash settlements, with adjustments for estimated contributions from the Earthquake Commission (EQC). In addition assumptions are made regarding future economic conditions and claims handling expenses, as set out in the following table.

	2015	2014
	\$000	\$000
Future inflation average		
■ Building cost	4.00%	5.80%
■ Temporary accommodation	0.00%	0.00%
■ Other cover types	3.00%	3.00%
■ Claims handling expenses	4.67%	5.07%
Discount rate	2.80%	3.60%
Risk margin – outstanding claims liabilities	10.00%	10.00%
Average weighted term to settlement from financial reporting date (years)	1.37	1.22

Process to determine assumptions

Inflation

The actuarial models allowed for the following inflationary impacts on expected future payments:

- Building costs inflation is based on the New Zealand Treasury national forecast inflation curve, with an allowance for the additional inflation expected in the Canterbury area;
- 0% per annum on temporary accommodation; and
- 3% per annum for the other cover types, based on CPI.

Overall this equates to 4.0% per annum (as applicable to cash flows gross of EQC and reinsurance recoveries).

Discount rate

Discounting has been applied to the outstanding claims by reference to the risk free zero coupon yields published by the New Zealand Treasury at 30 June 2015.

Claims handling expenses

The estimate of outstanding claims liabilities includes an allowance for the future cost of administering claims. It is based on the Company's budgeted operating costs.

Risk margin

The risk margin is expressed as a percentage of the gross (of reinsurance) discounted outstanding claims liability including claims handling expenses and intended to achieve a 75% probability of adequacy for the outstanding claims liability.

Three key sources of uncertainty are considered in determining the risk margin:

- Independent risk: variations of outcomes inherent in the underlying modeling processes

- Internal systemic risk or modeling error: the risk that the models have not captured all of the dynamics in relation to the event
- External systemic risk or external factors: external factors that contribute additional uncertainty.

There continues to be uncertainty attaching to many elements of the likely ultimate cost of the Company's earthquake related outstanding claims liabilities. In particular;

- While the Company has progressed most of the way through the damage assessment phase, a significant amount of the overall incurred cost is yet to be settled
- There remains some uncertainty as to the eventual cost of enhanced foundations in TC3 and TC2 properties, and the extent of land remediation compensation the Company will receive from the EQC in respect of these issues
- The run-off is exposed to a higher level of variability in claims experience than a typical residential property run-off portfolio. As the claim settlement process has progressed, a greater proportion of the outstanding claims liability relates to more complex claims, meaning the uncertainty around future settlement outcomes for outstanding claims is magnified (as compared to 'normal' residential property claims).

In response to the inherent uncertainties, the risk margin remains at 10%.

Average weighted term to settlement

Expected payment patterns have been used to determine the outstanding claims liability. The payment patterns adopted have been set based on the actuary's best estimate of when the payments are likely to be made.

Sensitivity analysis – impact of changes in key variables

The impact of change in key assumptions on the net outstanding claims liabilities are shown in the table below for the Company. Each change has been calculated in isolation to other changes.

Variable	Change in Variable	2015	2014
		\$000	\$000
Inflation rate	+1% p.a.	15,379	18,936
	-1% p.a.	(14,663)	(18,812)
Discount rate	+1% p.a.	(14,209)	(13,686)
	-1% p.a.	14,613	14,056
Claims handling expense	+10%	5,357	6,916
	-10%	(5,357)	(6,916)
Risk margin	+1%	10,723	12,711
	-1%	(10,723)	(12,711)
Construction schedule	+6 months	4,425	11,172
	-6 months	(3,483)	(11,620)

10. Employee remuneration

Remuneration band	2015	2014
	Number of employees	
\$530,000 pa - \$539,999 pa	-	1
\$470,000 pa - \$479,999 pa	1	-
\$380,000 pa - \$389,999 pa	1	-
\$330,000 pa - \$339,999 pa	-	1
\$260,000 pa - \$269,999 pa	1	-
\$250,000 pa - \$259,999 pa	1	-
\$230,000 pa - \$239,999 pa	-	1
\$220,000 pa - \$229,999 pa	-	1
\$210,000 pa - \$219,999 pa	1	-
\$190,000 pa - \$199,999 pa	2	1
\$180,000 pa - \$189,999 pa	-	1
\$170,000 pa - \$179,999 pa	-	1
\$160,000 pa - \$169,999 pa	2	1
\$150,000 pa - \$159,999 pa	2	2
\$140,000 pa - \$149,999 pa	3	-
\$130,000 pa - \$139,999 pa	3	1
\$120,000 pa - \$129,999 pa	3	6
\$110,000 pa - \$119,999 pa	4	5
\$100,000 pa - \$109,999 pa	7	7

Remuneration includes salary, performance bonuses, employer's contributions to superannuation, health and insurance plans, motor vehicle and other sundry benefits received in their capacity as

employees or former employees of the Company, excluding Directors.

11. Director remuneration

	Total 2015	Total 2014
	\$	\$
Ross Butler	72,000	72,000
Anne Urlwin	45,000	45,000
Jenn Bestwick	36,000	36,000
Bevan Killick	36,000	36,000
Susan Thodey	36,000	36,000
Sarah Sinclair (appointed 1 July 2014)	36,000	-
David Whyte (term ended 30 June 2014)	-	36,000

The shareholding Ministers approved ordinary fees of \$261,000 (2014: \$261,000).

12. Related party transactions

Remuneration of key management personnel

Key management personnel are executive managers who have authority and responsibility for planning, directing and controlling the activities of the Company.

	2015	2014
	\$000	\$000
Remuneration of key management personnel:		
Short term employee benefits	1,125	1,291

Transactions with various Crown entities

Included in investments at 30 June 2015 are \$99.753 million (2014: \$579.178 million) of Treasury bills and Government bonds. Included in cash and cash equivalents at 30 June 2015 are \$20 million (2014: \$9.030 million) of term deposits held in a State Owned Enterprise.

Details relating to the Crown receivable are disclosed in note 8. Accrued receivables of \$2.069 million (2014: \$4.794 million) included in receivables are the expected recovery from the Earthquake Commission of the Commission's contribution to claims which have been settled in full by the Company.

On 9 September 2013, Crown Asset Management Limited purchased property held for sale from the Company for \$4 million.

Statement of performance

1 July 2014 – 30 June 2015

Objective 1:

To operate efficient, cost-effective, consistent and fair claims management and rebuild processes in accordance with the Company's insurance policy obligations, and consistent with preserving its rights under reinsurance treaties.

13. Contingent liabilities

The Company from time to time receives notification of legal claims and disputes in relation to claim settlements as a commercial outcome of conducting its business. The Company defends all such claims.

14. Explanation of significant variances against budget

As disclosed in Notes 2 and 9, the estimation of the ultimate cost of settling earthquake related claims involves a number of key assumptions and is the most critical accounting estimate. Note 2 further notes that the estimation of claims incurred but not reported is generally subject to a greater degree of uncertainty.

The 2015 financial year budget was approved by the Board in April 2014, and was based on the latest available actuarial valuation at that time. Since then, the Company has experienced a significant increase in the projected ultimate number of over cap properties. Over half of the increase is due to the EQC settlement programme which resulted in more over cap claims being transferred to the Company than previously expected.

Statement of comprehensive income

- Net earthquake claims incurred is greater than budget principally due to the \$352 million increase in the central estimate (refer to above comments)
- Investment income is greater than budget as investment funds' utilisation is delayed in line with slower than forecast claim settlements.

Statement of financial position

- Cash and investments are \$276 million greater than budget, reflecting claims settlements being behind budget due to slower than anticipated progress in the repair work stream
- Reinsurance receivables as at 30 June 2015 are \$86 million greater than budget reflecting claim settlements - and therefore recoveries from reinsurers - being behind budget
- The outstanding claims liability is \$759 million greater than budget due to the combination of claim settlements being below budget and the increase in the central estimate, as commented on above.

Statement of cash flows

- Claim payments are \$317 million below budget, reflecting the delay in claim settlements commented on above
- Reinsurance receipts are \$98 million below budget, reflecting the delay in claim settlements commented on above
- Utilisation of investment funds (sales and maturities of financial assets) is \$111 million below budget, as investment funds utilisation is delayed in line with slower than forecast claim settlements.

Initiative	Performance measure	KPI target	Status
Comply with industry code of practice standards to facilitate successful outcomes for customers in a cost effective manner	Operation of effective systems to deliver consistent and fair claims decisions in an efficient cost-effective and timely manner	30 June 2015: decision packs (offers) distributed to 99% of customers for whom a claim notification has been received by February 2015	Partially met: 7,348 claims were notified by 28 February 2015. 6,884 or 93.7% of these assessments have been presented as offers to customers as at 30 June 2015
		30 June 2015: settlement elections have been made by 92.5% of customers issued with decision packs prior to 31 March 2015	Met: 97.3% of customers presented with offers by 31 March 2015 had selected a settlement option as at 30 June 2015
		30 June 2015: damage assessments completed for 100% of those customers from whom a claim notification has been received by February 2015	Met: 7,348 claims had been notified to Southern Response by 28 February 2015, all of which had assessments completed by 30 June 2015
	Timely and effective communication with customers regarding claims progress and building opportunities	30 September 2014: regular and measurable communication is taking place with customers who are in the build queue – 90% compliance to agreed metrics	Met
Build costs efficiency managed		31 December 2014 and 30 June 2015: Solutions Team ¹ has processed all cases referred to it more than three months earlier	Partially met: during the year, 78% of claims referred to the Solutions Team were resolved within three months. Complex claims are dependent on external resource and require three to six months to resolve
		Actual build cost within 5% of the estimated value of scope of repair/rebuild (RFP/DRA ²)	Met

¹ A specialty team charged with seeking to identify the issues that are disrupting progress of a claim towards settlement

² Detailed Repair/Rebuild Analysis

Initiative	Performance measure	KPI target	Status
Seek to take industry-leading roles in utilisation of building capacity, procurement systems and in research and innovation that expedite and enhance the effectiveness of the rebuild	Demonstrable assessment of Southern Response industry-leading contribution and progress with claim and building throughput; engagement with leading building industry participants; geo-technical, building regulatory and structural advice integrated in operations	31 December 2014: 1,053 house repairs/rebuilds completed	Partially met: 819 repairs and rebuilds completed as at 31 December 2014
		30 June 2015: 1,578 house repairs/rebuilds completed	Partially met: 1,167 repairs and rebuilds completed by 30 June 2015
		Survey of all Southern Response contracted volume group builders and MBIE ³ as to Southern Response's contribution carried out	Met
Operate a dispute resolution system that is equitable and responsive to all customers while strictly observing customers' entitlements from their AMI policy		30 September 2014: completion and assessment of the outcomes of a trial of expansion of the jurisdiction of the ISO with results having determined the future of the revised approach	Met
		31 December 2014: completion of review and assessment of ISO's experiences of dealing with Southern Response matters and implementation of recommendations for improvements	Met

Objective 2:

To maintain effective relationships with key stakeholders.

Initiative	Performance measure	KPI target	Status
Optimise the strategic and operational interaction with CERA, EQC, MBIE, insurers and key community groups	Operation of effective relationship management protocols	Ongoing: maintain a relationship management protocol that provides for appropriate strategic and operational interaction with CERA, EQC, insurers and ICNZ	Met
		Ongoing: participate in relevant MBIE forums and working groups to facilitate the development and implementation of measures to aid the rebuild of Canterbury houses	Met

³ Ministry of Business Innovation and Employment
⁴ Insurance and Savings Ombudsman

Objective 3:

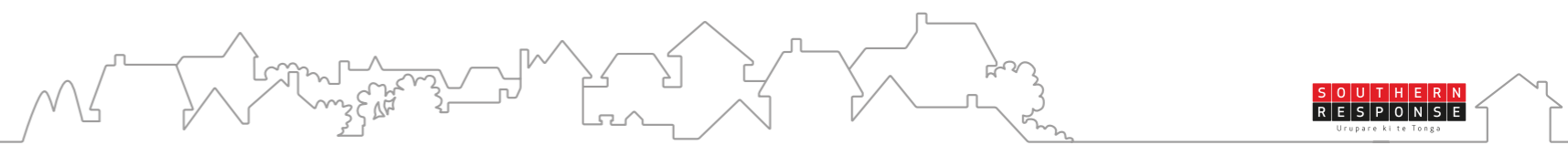
To manage the business and associated risk consistent with minimising the net cost to the Crown.

Initiative	Performance measure	KPI target	Status
Maintain an effective risk management framework that balances risk with progress	Risk management framework	Ongoing: maintain risk monitoring and management reporting framework and report on exceptions quarterly	Met
Maintain systems to achieve good ratings in the Company's management, financial and service performance information systems and controls	Assessment by the Company's Auditors	31 December 2014: ratings of "good" or better in the assessment provided by the external Auditors as part of the 2014 annual financial statements audit process	Met
Maintain monitoring and management systems to ensure compliance with contractual obligations	Compliance with contractual obligations	Ongoing half yearly September and March: maintain a monitoring and reporting system for key contractual obligations	Met
Maintain appropriate reinsurance claim processes to ensure the receipt of all reinsurance recoveries	Keep reinsurers fully informed of financial cash flow projections and policy interpretation issues	Ongoing: manage funding requests to reinsurers to minimise impact on the Company's cash reserves	Met

Objective 4:

To manage investments and liquidity in accordance with the Investment Management policy.

Initiative	Performance measure	KPI target	Status
To manage investments and liquidity in accordance with the terms of the Investment Management policy and the Crown support deed	Investment Management policy and cash flow forecasting systems implemented	Liquidity managed in accordance with Investment Management policy	Met
		Draw-downs under the Crown support deed forecast to Treasury in accordance with the terms of the Crown support deed	Met



Objective 5:

To operate the business within operational budgets.

Initiative	Performance measure	KPI target	Status
Achieve cost and operational efficiencies by progressively integrating resources to achieve economies of scale thereby ensuring an overall efficient and seamless claims management cost structure	Integration of resources	30 September 2014: review staff resourcing and develop transition resource model	Met
		30 September 2014 and 31 March 2015: review accommodation options and develop project plan for any accommodation changes	Met
Controls and scrutiny in place to manage the cost of Arrow International and other key suppliers	Cost control	30 September 2014: re-evaluate Arrow value for money equation. Take necessary actions and/or identify management synergies. Implement results by 31 March 2015	Met
Maintain employer policies and practices to enhance the Company's ability to attract, retain and manage optimisation of skilled staff with realistic pay and employment conditions	Operation of policies and practices		Met

Objective 6:

To promote healthy and safe workplaces.

Initiative	Performance measure	KPI target	Status
To take a leading role in health and safety matters in relation to the Canterbury earthquake recovery	Ensure a best practice health and safety environment for staff, visitors and those involved in the delivery of Southern Response's rebuild activity including Arrow contractors, sub-contractors and home owners	31 December 2014: develop and execute an end to end health and safety monitoring system consistent with emerging legislative requirements	Met
		31 December 2014: determine a Board health and safety charter describing <ul style="list-style-type: none"> ■ Strategy and goals ■ Targets for tracking effectiveness of strategy and goals ■ Reporting protocols 	Met

Directory

Shareholders

Minister of Finance
Minister for Canterbury Earthquake Recovery

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Executive Management

Peter Rose Chief Executive
Tony Feaver Chief Financial Officer
Casey Hurren Earthquake Strategy Manager
Sarah Giles Corporate Services Manager
Linda Falwasser Strategic Communications Manager
Anthony Honeybone Technical and Performance Manager
Darrell Hansen Operations Manager

Project Management Office

Arrow International (NZ) Limited

Actuary

Finity Consulting Pty Limited

Auditor

The Auditor-General pursuant to section 15 of the Public Audit Act 2001.

Michael Wilkes of Deloitte was appointed to perform the audit on behalf of the Auditor-General.

Banker

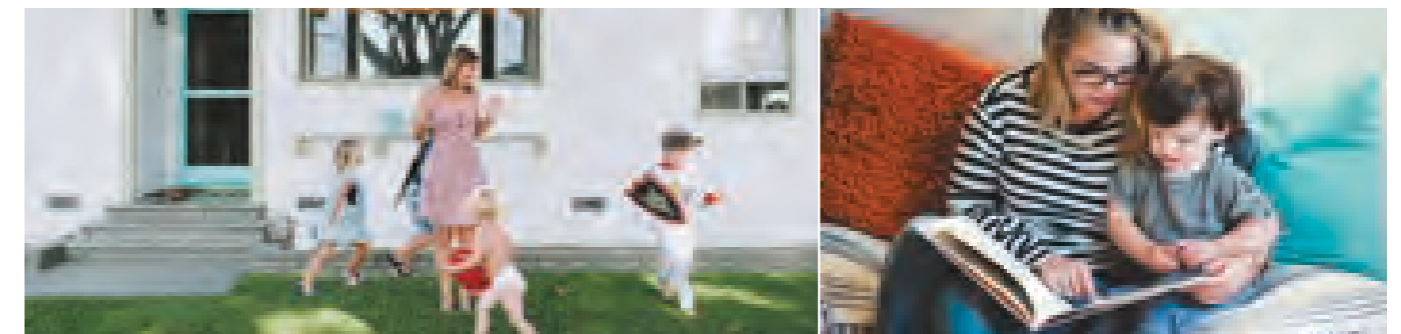
ANZ Bank New Zealand Limited

Legal Advisors

Bell Gully
DLA Piper
Wynn Williams

Affiliations

Insurance Council of New Zealand, associate member
Insurance and Savings Ombudsman (ISO) scheme, participant





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Southern Response is the government-owned company responsible for settling claims by AMI policyholders for Canterbury earthquake damage which occurred before 5 April 2012 (the date AMI was sold to IAG).

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