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Challenger Life Company Limited ACN 072 486 938

2017 Annual Report

Challenger Life Company Limited

The Directors of Challenger Life Company Limited (the Company or CLC) present their report, together with the financial report of the consolidated entity consisting of the Company and its controlled entities (the Group), for the year ended 30 June 2017.

1. Directors

The names and details of the Directors of the Company holding office during the financial year ended 30 June 2017 and up to the date of this report are listed below. Directors were in office for the entire period, unless otherwise stated.

Name	Position
Peter L Polson	Independent Chair
Brian R Benari	Managing Director and Chief Executive Officer
Graham A Cubbin	Independent Non-executive Director
Steven Gregg	Independent Non-executive Director
Jonathan H Grunzweig	Independent Non-executive Director
Brenda M Shanahan	Independent Non-executive Director
JoAnne M Stephenson	Independent Non-executive Director
Leon Zwier	Independent Non-executive Director

2. Company secretary

Michael Vardanega is a qualified solicitor and was appointed to the position of General Counsel and Group Company Secretary on 1 March 2011.

Andrew Brown has over 20 years' experience in the financial services industry and was appointed to the position of Company Secretary on 25 October 2012.

3. Principal activities and changes in the state of affairs

The principal activities of the Company during the year were the provision of a range of life insurance, annuity, superannuation and investment products to customers in Australia and overseas, backed by a diverse portfolio of assets.

4. Capital management

On 7 April 2017, CLC completed its second notes issue, raising $460.0 million of new funding. The issue features similar structural characteristics to CLC's first $345.0 million hybrid equity issue completed on 9 October 2014. Both note issuances were approved by the Australian Prudential Regulation Authority (APRA) as qualifying as Additional Tier 1 capital of CLC and are classified as equity.

5. Operating and financial review

The consolidated statutory profit after tax for the year attributable to the equity holders was $445.2 million compared to $338.4 million in the prior year.

6. Dividends

On 14 February 2017 the Directors of the Company declared a dividend on ordinary shares of $90.0 million. The dividend was subsequently paid on 27 March 2017.

On 14 August 2017 the Directors of the Company declared a dividend on ordinary shares of $210.0 million.

7. Likely developments and expected results

The Group intends to continue with its current strategy of providing its customers with financial security for retirement. To continue to achieve this vision, the Company is focused on the following core strategic objectives:

1. be recognised as the leader and partner of choice in retirement income solutions with a broad product offering; and
2. increase the Australian retirement savings pool allocation to secure and stable incomes.

8. Significant events after the balance date

CLC's business is growing strongly, with new distribution and product initiatives commencing in 2018. On 14 August 2017, the Board of Challenger Limited (CLC's ultimate parent entity) approved the placement of $500 million of ordinary shares to MS&AD Insurance Group Holdings Inc. The proceeds from the placement will be used to increase CLC's Common Equity Tier 1 capital.

At the date of this financial report and other than described above, no matter or circumstance has arisen that has affected, or may significantly affect, the Group's operations, the results of those operations or the Group's state of affairs in future financial years which has not already been reflected in this report.

9. Indemnification and insurance of officers and Directors

In accordance with its Constitution, and where permitted under relevant legislation or regulation, the Company indemnifies the Directors and officers against all liabilities to another person that may arise from their position as Directors or officers of the Company and its subsidiaries, except where the liability arises out of conduct involving lack of good faith, wilful default, fraud or criminal or dishonest behaviour.

In accordance with the provisions of the *Corporations Act 2001*, the Company has insured the Directors and officers against liabilities incurred in their role as Directors and officers of the Company. The terms of the insurance policy, including the premium are subject to confidentiality clauses and as such the Company is prohibited from disclosing the nature of the liabilities covered and the premium paid.

Indemnification is provided by the ultimate parent entity, Challenger Limited, and the premium is paid by a related party, Challenger Group Services Pty Ltd.

10. Indemnification of Auditors

To the extent permitted by law, the Company has agreed to indemnify its auditor, Ernst & Young, as part of the terms of its audit engagement agreement. The primary purpose of the indemnity is to indemnify Ernst & Young for any loss that it may suffer as a result of a false representation given by the Company's management where a claim is made against Ernst & Young by a third party.

There is a caveat if Ernst & Young's loss results from its own negligence or wrongful or wilful acts or omissions. No payment has been made to indemnify Ernst & Young during or since the financial year.

11. Environmental regulation and performance

The Company owns a number of trusts which own assets both in Australia and overseas. Some of these assets are subject to environmental regulations under Commonwealth, state and offshore legislation. The Directors are satisfied that adequate systems are in place for the management of the Company's environmental responsibilities and compliance with various legislative, regulatory and licence requirements. Further, the Directors are not aware of any breaches of these requirements, and to the best of their knowledge all activities have been undertaken in compliance with environmental requirements.

The Company undertakes a comprehensive review of investment opportunities, including environmental, social and governance (ESG) aspects, to support long-term returns. The Company has adopted an integrated investment management approach to deliver responsible investment outcomes and believes there are links between long-term sustainable returns and the quality of our ESG practices. Challenger Limited is a signatory to the Principles for Responsible Investment (PRI) and in March 2017 lodged an annual PRI assessment report covering the period 1 January 2016 to 31 December 2016.

12. Rounding

The amounts contained in this report and the financial report have been rounded off to the nearest $100,000 unless otherwise stated, under the option available to the Group under Australian Securities and Investments Commission (ASIC) Corporations Instrument 2016/191. The Group is an entity to which the class order applies.

13. Corporate Reporting Reform Act – parent entity reporting

On 30 June 2010 a change was made to the *Corporations Act 2001* to allow companies preparing consolidated accounts to move to a two column, consolidated-only disclosure in the financial report. After discussions with ASIC it was determined that, as an Australian Financial Services Licence holder, the Company was still required to produce parent entity information. On 29 July 2010 ASIC issued class order 10/654 to ensure that a company still required to produce parent entity accounts could do so without being in breach of the *Corporations Amendment (Corporate Reporting Reform) Act 2010.*

14. Auditor's independence declaration

The Directors received the following declaration from the auditor of Challenger Life Company Limited:

EY
Building a better working world

Ernst & Young
200 George Street
Sydney NSW 2000 Australia
GPO Box 2646 Sydney NSW 2001

Tel: +61 2 9248 5555
Fax: +61 2 9248 5959
ey.com/au

Auditor's independence declaration to the Directors of Challenger Life Company Limited

As lead auditor for the audit of Challenger Life Company Limited for the financial year ended 30 June 2017, I declare to the best of my knowledge and belief, there have been:

a) no contraventions of the auditor independence requirements of the *Corporations Act 2001* in relation to the audit; and

b) no contraventions of any applicable code of professional conduct in relation to the audit.

This declaration is in respect of Challenger Life Company Limited and the entities it controlled during the financial year.

Ernst & Young

Louise Burns
Partner

Sydney
14 August 2017

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ACN 004 860 860

15. Authorisation

Signed in accordance with a resolution of the Directors of Challenger Life Company Limited:

G A Cubbin
Director

Sydney
14 August 2017

B R Benari
Director

Sydney
14 August 2017

Contents – Financial report

This financial report covers Challenger Life Company Limited (the Company or CLC) and its controlled entities (the Group).

Statements of comprehensive income

For the year ended 30 June		Consolidated		Parent	
		2017	2016	2017	2016
	Note	$M	$M	$M	$M
Revenue	1	1,800.9	1,601.8	1,484.3	1,222.8
Expenses	2	(1,090.8)	(941.9)	(846.9)	(751.6)
Finance costs	16	(135.9)	(209.6)	(78.1)	(57.2)
Profit before income tax		**574.2**	**450.3**	**559.3**	**414.0**
Income tax expense	4	(128.6)	(110.4)	(114.0)	(97.4)
Profit for the year		**445.6**	**339.9**	**445.3**	**316.6**
Profit attributable to shareholders of Challenger Life Company Limited		445.2	338.4	445.3	316.6
Profit attributable to non-controlling interests		0.4	1.5	-	-
Profit for the year		**445.6**	**339.9**	**445.3**	**316.6**
Other comprehensive income					
Items that may be reclassified to profit and loss, net of tax					
Translation of foreign entities	15	(25.8)	38.1	-	-
Hedge of net investment in foreign operations	15	25.8	(35.5)	-	-
Cash flow hedges – SPV[1]	15	(0.2)	(1.4)	-	-
Other comprehensive (expense)/income for the year		**(0.2)**	**1.2**	**-**	**-**
Total comprehensive income for the year		**445.4**	**341.1**	**445.3**	**316.6**
Comprehensive income attributable to shareholders of Challenger Life Company Limited		445.0	339.6	445.3	316.6
Comprehensive income attributable to non-controlling interests		0.4	1.5	-	-
Total comprehensive income for the year		**445.4**	**341.1**	**445.3**	**316.6**

[1] SPV = Special Purpose Vehicles.

The statements of comprehensive income should be read in conjunction with the accompanying notes.

Statements of financial position

As at 30 June	Note	Consolidated 2017 $M	Consolidated 2016 $M	Parent 2017 $M	Parent 2016 $M
Assets					
Cash and cash equivalents	12	431.0	441.4	136.4	137.3
Cash and cash equivalents – SPV	7	122.4	146.9	-	-
Receivables		734.4	716.7	1,001.5	980.5
Mortgage assets – SPV	7	1,364.7	1,739.7	-	-
Derivative assets	10	565.9	829.8	813.6	1,081.2
Financial assets – fair value through profit and loss	5	15,477.1	13,104.3	16,947.4	14,904.9
Investment property held for sale	6	96.0	70.6	-	-
Investment and development property	6	3,532.9	3,499.3	-	-
Finance leases		51.3	57.8	2.8	3.8
Current tax asset		-	3.3	2.2	-
Property, plant and equipment		75.3	110.1	-	-
Other assets		34.1	39.2	-	6.8
Goodwill	22	61.1	61.1	46.8	46.8
Total assets of shareholders of Challenger Life Company Limited and non-controlling interests		**22,546.2**	**20,820.2**	**18,950.7**	**17,161.3**
Liabilities					
Payables		965.0	800.8	799.6	639.3
Derivative liabilities	10	492.2	863.3	692.8	1,039.1
Interest bearing financial liabilities	14	4,419.9	3,811.0	3,681.1	3,031.0
Interest bearing financial liabilities – SPV	7	1,174.0	1,566.6	-	-
External unit holders' liabilities	9	1,687.8	1,315.5	-	-
Current tax liability		1.7	-	-	
Deferred tax liabilities	4	132.7	190.8	131.8	197.5
Life contract liabilities	8	10,322.2	9,558.5	10,322.2	9,558.5
Total liabilities of shareholders of Challenger Life Company Limited and non-controlling interests		**19,195.5**	**18,106.5**	**15,627.5**	**14,465.4**
Net assets of shareholders of Challenger Life Company Limited and non-controlling interests		**3,350.7**	**2,713.7**	**3,323.2**	**2,695.9**
Equity					
Contributed equity	13	2,001.5	1,541.5	2,001.5	1,541.5
Reserves	15	140.8	141.0	137.8	137.8
Retained earnings	15	1,194.8	1,027.6	1,183.9	1,016.6
Total equity of shareholders of Challenger Life Company Limited		**3,337.1**	**2,710.1**	**3,323.2**	**2,695.9**
Non-controlling interests		13.6	3.6	-	-
Total equity of shareholders of Challenger Life Company Limited and non-controlling interests		**3,350.7**	**2,713.7**	**3,323.2**	**2,695.9**

The statements of financial position should be read in conjunction with the accompanying notes.

Statements of changes in equity

Consolidated	Note	Contributed equity $M	Cash flow hedge reserve – SPV $M	Foreign currency translation reserve $M	Adjusted controlling interest reserve $M	Other reserve $M	Retained earnings $M	Total share-holder equity $M	Non-controlling interests $M	Total equity $M
		Attributable to shareholders of Challenger Life Company Limited								
Balance at 1 July 2015		1,541.5	1.4	(6.1)	18.9	124.8	898.6	2,579.1	95.0	2,674.1
Profit for the year	15	-	-	-	-	-	338.4	338.4	1.5	339.9
Other comprehensive income/(loss) for the year		-	(1.4)	2.6	-	-	-	1.2	-	1.2
Total comprehensive income/(loss) for the year		**-**	**(1.4)**	**2.6**	**-**	**-**	**338.4**	**339.6**	**1.5**	**341.1**
Other equity movements										
Issued capital	13	-	-	-	-	-	-	-	-	-
Changes in controlling interest reserve	15	-	-	-	(6.7)		-	(6.7)	-	(6.7)
Dividends paid	17	-	-	-	-	-	(209.4)	(209.4)	-	(209.4)
Deconsolidation of entities		-	-	-	-	-	-	-	(93.2)	(93.2)
Distributable reserves	15	-	-	-	-	7.5	-	7.5	-	7.5
Non-controlling interests movements		-	-	-	-	-	-	-	0.3	0.3
Balance at 30 June 2016 and 1 July 2016		**1,541.5**	**-**	**(3.5)**	**12.2**	**132.3**	**1,027.6**	**2,710.1**	**3.6**	**2,713.7**
Profit for the year	15	-	-	-	-	-	445.2	445.2	0.4	445.6
Other comprehensive loss for the year		-	(0.2)	-	-	-	-	(0.2)	-	(0.2)
Total comprehensive income/(loss) for the year		**-**	**(0.2)**	**-**	**-**	**-**	**445.2**	**445.0**	**0.4**	**445.4**
Other equity movements										
Issued capital	13	460.0	-	-	-	-	-	460.0	-	460.0
Dividends paid	17	-	-	-	-	-	(278.0)	(278.0)	-	(278.0)
Non-controlling interests movements		-	-	-	-	-	-	-	9.6	9.6
Balance at 30 June 2017		**2,001.5**	**(0.2)**	**(3.5)**	**12.2**	**132.3**	**1,194.8**	**3,337.1**	**13.6**	**3,350.7**

The statements of changes in equity should be read in conjunction with the accompanying notes.

Statements of changes in equity (continued)

Parent	Note	Contributed equity $M	Cash flow hedge reserve – SPV $M	Foreign currency translation reserve $M	Adjusted controlling interest reserve $M	Other reserve $M	Retained earnings $M	Total share-holder equity $M	Non-controlling interests $M	Total equity $M
		Attributable to shareholders of Challenger Life Company Limited								
Balance at 1 July 2015		1,541.5	-	-	-	137.8	909.4	2,588.7	-	2,588.7
Profit for the year	15	-	-	-	-	-	316.6	316.6	-	316.6
Other comprehensive income for the year		-	-	-	-	-	-	-	-	-
Total comprehensive income for the year		**-**	**-**	**-**	**-**	**-**	**316.6**	**316.6**	**-**	**316.6**
Other equity movements										
Dividends paid	17	-	-	-	-	-	(209.4)	(209.4)	-	(209.4)
Balance at 30 June 2016 and 1 July 2016		**1,541.5**	**-**	**-**	**-**	**137.8**	**1,016.6**	**2,695.9**	**-**	**2,695.9**
Profit for the year	15	-	-	-	-	-	445.3	445.3	-	445.3
Other comprehensive income for the year		-	-	-	-	-	-	-	-	-
Total comprehensive income for the year		**-**	**-**	**-**	**-**	**-**	**445.3**	**445.3**	**-**	**445.3**
Other equity movements										
Issued capital	13	460.0	-	-	-	-	-	460.0	-	460.0
Dividends paid	17	-	-	-	-	-	(278.0)	(278.0)	-	(278.0)
Balance at 30 June 2017		**2,001.5**	**-**	**-**	**-**	**137.8**	**1,183.9**	**3,323.2**	**-**	**3,323.2**

The statements of changes in equity should be read in conjunction with the accompanying notes.

Statements of cash flows

For the year ended 30 June	Note	Consolidated 2017 $M	Consolidated 2016 $M	Parent 2017 $M	Parent 2016 $M
Operating activities					
Other income received		429.7	415.4	10.2	10.6
Annuity and premium receipts	8	4,041.6	3,367.8	4,069.8	3,367.8
Annuity and claim payments	8	(3,464.7)	(2,955.1)	(3,464.6)	(2,955.1)
Payments to reinsurer	8	(5.6)	(5.2)	(33.9)	(5.2)
Receipts from external unit holders		941.2	998.5	-	-
Payments to external unit holders		(581.7)	(706.1)	-	-
Payments to vendors		(321.8)	(314.0)	(153.7)	(134.2)
Dividends received		48.6	39.9	335.6	387.4
Interest received		686.4	611.7	668.2	618.2
Interest paid		(87.0)	(75.9)	(75.7)	(56.2)
Income tax paid		(98.0)	(155.3)	(96.2)	(135.9)
Net cash inflows from operating activities	**12**	**1,588.7**	**1,221.7**	**1,259.7**	**1,097.4**
Investing activities					
Payments on net purchases of investments		(2,373.4)	(1,963.6)	(2,101.7)	(1,924.5)
Net mortgage loan repayments		373.6	589.9	-	-
Payments on net purchases of investment properties		(54.5)	(151.6)	-	-
Payments for net purchases of property, plant and equipment		(7.8)	(1.3)	-	-
Net cash outflows from investing activities		**(2,062.1)**	**(1,526.6)**	**(2,101.7)**	**(1,924.5)**
Financing activities					
Net proceeds from borrowings – interest bearing liabilities	14	249.5	589.6	643.0	1,186.9
Proceeds from issue of equity hybrid notes		460.0	-	460.0	-
Dividends paid		(278.0)	(209.4)	(278.0)	(209.4)
Proceeds from/(repayments of) loans		7.0	11.2	16.1	(0.3)
Net cash inflows from financing activities		**438.5**	**391.4**	**841.1**	**977.2**
Net (decrease)/increase in cash and cash equivalents		**(34.9)**	**86.5**	**(0.9)**	**150.1**
Cash and cash equivalents at the beginning of the year		588.3	501.8	137.3	(12.8)
Cash and cash equivalents at the end of the year		**553.4**	**588.3**	**136.4**	**137.3**
Cash and cash equivalents	12	431.0	441.4	136.4	137.3
Cash and cash equivalents – SPV	7	122.4	146.9	-	-
Cash and cash equivalents at the end of the year		**553.4**	**588.3**	**136.4**	**137.3**

The statements of cash flows should be read in conjunction with the accompanying notes.

Section 1: Basis of preparation and overarching significant accounting policies

Challenger Life Company Limited (the Company, the parent entity or CLC) is a company limited by shares, incorporated in Australia.

The parent entity financial report and the financial report for the Company and its controlled entities (the Group) for the year ended 30 June 2017 were authorised for issue in accordance with a resolution of the Directors of the Company on 14 August 2017.

(i) Basis of preparation and statement of compliance

This is a general purpose financial report that has been prepared in accordance and complies with the requirements of the *Corporations Act 2001*, Australian Accounting Standards and other authoritative pronouncements of the Australian Accounting Standards Board (AASB) and International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board. Challenger Life Company Limited is a for-profit entity for the purposes of preparing financial statements.

Unless otherwise stated, amounts in this financial report are presented in Australian dollars and have been prepared on a fair value basis in respect of assets backing life insurance contracts liabilities. The assets and liabilities disclosed in the statement of financial position are grouped by nature and listed in an order that reflects their relative liquidity. In the disclosure notes, the current/non-current split is between items expected to be settled within 12 months (current) and those expected to be settled in greater than 12 months (non-current).

(ii) New and revised accounting standards and interpretations

Except for the matters referred to below, the accounting policies and methods of computation are the same as those adopted in the annual report for the prior comparative period. Where applicable, comparative figures have been updated to reflect any changes in the current period.

New accounting standards and amendments that are effective in the current financial year

There were a number of new accounting standards and amendments to existing accounting standards that were effective from 1 July 2016 but do not have a material impact on the financial statements.

Accounting standards and interpretations issued but not yet effective

AASB 9 *Financial Instruments*

AASB 9 *Financial Instruments* replaces AASB 139 *Financial Instruments: Recognition and Measurement* and is effective for the Group from 1 July 2018. The Group does not intend to early adopt the standard.

The standard makes changes to the classification of financial assets for the purpose of determining their measurement basis, as well as to the amounts relating to fair value changes to be taken directly to equity. The standard replaces the incurred loss model of AASB 139 with a new expected loss model which can result in the acceleration of impairment recognition on financial instruments.

The standard requires entities to account for expected credit losses on financial instruments at the point at which the financial instruments are first recognised and to estimate the expected loss applicable to those financial instruments over the period for which they are held. This requirement can result in expected losses on financial instruments being recognised in full much earlier than would have been the case under AASB 139. In addition, there are also significant changes to hedge accounting requirements, including changes to hedge effectiveness testing, treatment of hedging costs, risk components that can be hedged and associated disclosures.

The Group has performed an initial assessment and does not expect any material impact as a result of complying with the new requirements. This is because the majority of the Group's assets are already measured at fair value through profit and loss as required by AASB 1038 *Life Insurance* and as permitted under both AASB 139 and AASB 9. A new impairment model will be developed, but the impact of any assumption changes with regard to credit losses is not expected to result in a material change to equity. Amendments to hedge documentation will be required, but quantitative impacts from these changes are not expected.

AASB 15 *Revenue from Contracts with Customers*

The new revenue standard establishes a single, comprehensive framework for revenue recognition and will be effective for the Group from 1 July 2018 and replaces the previous revenue standards AASB 118 *Revenue* and AASB 111 *Construction Contracts*. The standard does not apply to leases, financial instruments or insurance contracts. The core principle of AASB 15 is that an entity recognises revenue to depict the transfer of promised goods and services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services.

The Group has performed an initial assessment on existing revenue streams and does not expect any material impact as a result of complying with the new requirements. Life revenue is mainly derived from income on financial instruments and life insurance contract premiums which are not part of the scope of the standard.

AASB 16 *Leases*

This standard amends the accounting for leases and replaces AASB 117 *Leases*. The standard removes the distinction between operating and finance leases and requires lessees to bring all leases on to the statement of financial position. The standard will be effective for the Group from 1 July 2019, and the Group does not intend to early adopt the standard.

The majority of leases from the lessee perspective within the scope of AASB 16 are expected to be recognised as a 'right-of-use' asset on the Group's statement of financial position together with a related lease liability being recognised subject to the relevant contracts remaining in force at transition. Lessor accounting remains largely unchanged.

The Group is in the process of considering its transition approach to the standard.

AASB 17 *Insurance Contracts*

On 20 July 2017, AASB 17 *Insurance Contracts* was released to align with the new IFRS 17 *Insurance Contracts*. The effective dates are the same and will be applicable to the Group from 1 July 2021. The proposed approach for the measurement of the insurance contract liability is based on the following building blocks:

- expected present value of future cash flows;
- a risk adjustment related to the expected present value of cash flows; and
- a contractual service margin (CSM) that would eliminate any gain at inception of the contract. The CSM would be adjusted subsequently for changes in estimates of future cash flows and the risk adjustment to the extent that these changes relate to future coverage or other future services.

A full review of the impact on the Group will be performed over the coming year.

(iii) Principles of consolidation

The financial statements consolidate the financial information of controlled entities. An entity is controlled when the Company is exposed, or has rights, to variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The statement of financial position date and the accounting policies of controlled entities are consistent with those of the Company.

All intercompany balances and transactions, including unrealised profits arising from intra-Group transactions, are eliminated in full. Unrealised losses are eliminated unless costs cannot be recovered. For controlled entities where the Group owns less than 100% of the issued capital or units, the share of the results and equity attributable to non-controlling interests are shown separately.

The life insurance contract operations of the Company are conducted within the separate statutory funds as required by the Life Insurance Act 1995. Both the shareholder interests, and policyholder interests in the statutory funds are reported in aggregate in the financial report of the Group.

Investments in associates

Associates are entities over which the Group has significant influence over the financial and operating policies but not control. Investments in associates that back life insurance contracts are designated as financial assets at fair value through profit and loss.

(iv) Comparatives

Where necessary, comparative figures have been reclassified to conform to any changes in presentation made in this financial report.

(v) Rounding of amounts

Unless otherwise stated, amounts contained in this report and the financial report have been rounded to the nearest $100,000 under the option available to the Group under Australian Securities and Investments Commission (ASIC) Corporations Instrument 2016/191.

(vi) Foreign currency

Both the presentation currency and the functional currency of the Company and its controlled Australian entities are Australian dollars. A number of foreign controlled entities have a functional currency other than Australian dollars.

Transactions in foreign currency are translated into the Company's presentation currency, at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated into Australian dollars at the foreign exchange rate ruling at the statement of financial position date.

Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate as at the date of the transaction. Non-monetary items measured at fair value in a foreign currency are translated to the functional currency using the exchange rates ruling at the date when the fair value was determined.

Derivatives are used to hedge the foreign exchange risk relating to certain transactions. Refer to Note 10 Derivative financial instruments.

Foreign controlled entities

On consolidation, the assets and liabilities of foreign subsidiaries whose functional currency differs from the presentation currency are translated into Australian dollars at the rate of exchange ruling at the statement of financial position date. Exchange differences arising on the retranslation are taken directly to the foreign currency translation reserve in equity. The change in fair value of derivative financial instruments designated as a hedge of the net investment in a foreign controlled entity is also recognised in the foreign currency translation reserve.

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

(vii) Goods and services tax (GST)

Revenues, expenses and assets are recognised net of the applicable amount of GST, except where the amount of the GST incurred is not recoverable from the taxation authority. In these circumstances, the GST is recognised as part of the cost of the acquisition of the asset or as part of the expense.

Receivables and payables are stated with the applicable amount of GST included. The net amount of GST recoverable from, or payable to, the Australian Taxation Office (ATO) is included as an asset or liability in the statement of financial position.

Cash flows are included in the statement of cash flows on a gross (GST inclusive) basis. The GST components of cash flows arising from investing and financing activities which are recoverable from, or payable to, the ATO are classified as operating cash flows.

(viii) Receivables

Receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They include trade and other receivables and are recognised at their amortised cost less impairment losses, which approximates fair value. Receivables are reviewed at each statement of financial position date to determine whether there is any indication of impairment. If such indication exists, the asset's recoverable amount is estimated.

(ix) Payables

Payables represent unsecured non-derivative, non-interest bearing financial liabilities in respect of goods and services provided to the Group prior to the end of the financial year. They include accruals, trade and other creditors and are recognised at amortised cost, which approximates fair value.

(x) Significant accounting judgements, estimates and assumptions

The carrying values of amounts recognised on the statement of financial position are often based on estimates and assumptions of future events. The key estimates and assumptions that have a significant risk of causing a material adjustment to the recognised amounts within the next annual reporting period are disclosed individually within each of the relevant notes to the financial statements.

(xi) Impairment of assets

At each reporting date, the Group assesses whether there is any indication that an asset not carried at fair value may be impaired. If any such indication exists, the Group makes a formal estimation of the asset's recoverable amount.

An asset's recoverable amount is the greater of the fair value, less costs to sell, and its value in use. It is determined for an individual asset, unless the asset's recoverable amount cannot be estimated as it does not generate cash flows independent of those from other assets or groups of assets. In such cases, the asset is tested for impairment as part of the cash-generating unit (CGU) to which it belongs. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

When the carrying amount of an asset or CGU exceeds its recoverable amount, the asset or cash-generating unit is considered impaired and is written down to its recoverable amount.

Impairment losses are recognised in the statement of comprehensive income, unless an asset has previously been revalued, in which case the impairment loss is recognised as a reversal of that previous revaluation with any excess recognised through the statement of comprehensive income as impairment losses.

Impairment losses recognised in respect of a CGU are allocated first to reduce the carrying amount of any goodwill allocated to that cash-generating unit, then to reduce the carrying amount of the other assets in the unit on a pro rata basis.

An assessment is also made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists, the recoverable amount is estimated. A reversal of the impairment loss may only increase the asset's value up to its carrying amount that would have been determined, net of depreciation, had no impairment loss been recognised for the asset in prior years. Such reversal is recognised in the statement of comprehensive income unless the asset is carried at the revalued amount, in which case it is treated as a revaluation increase. Impairment losses recognised for goodwill are not subsequently reversed.

(xii) Restrictions on assets

Financial assets held by the Company can only be used within the restrictions imposed under the *Life Insurance Act 1995* (the Life Act). The main restrictions are that the assets in a statutory fund can only be used to meet the liabilities and expenses of that statutory fund, to acquire investments to further the business of the statutory fund or as distributions when capital adequacy requirements are met. Refer to Note 8 Life contract liabilities.

Section 2: Key numbers

This section presents the results and performance for the year and provides additional information about those line items on the statement of comprehensive income that the Directors consider most relevant in the context of understanding the financial components of both the Group's and the Company's operations.

Note 1 Revenue

	Consolidated		Parent	
	30 June 2017 $M	30 June 2016 $M	30 June 2017 $M	30 June 2016 $M
Investment revenue				
Fixed income securities and cash				
Interest revenue	784.0	689.4	677.9	591.1
Net realised and unrealised (losses)/gains on fixed income securities[1]	(209.1)	151.7	(188.4)	156.9
Investment property and property securities				
Property rental revenue	328.5	334.1	-	-
Dividend revenue	20.4	19.2	5.2	9.9
Net realised and unrealised gains/(losses) on investment property and property securities	56.3	132.1	(30.3)	76.6
Revenue from sale of development properties	16.6	30.2	-	-
Equity and infrastructure investments				
Dividend revenue	34.7	23.0	336.8	363.0
Net realised and unrealised gains/(losses) on equity investments	65.5	(8.7)	93.1	(52.6)
Net realised and unrealised gains on infrastructure investments	4.5	69.6	12.1	23.4
Other				
Net realised and unrealised gains/(losses) on foreign exchange translation and hedges	23.5	39.7	62.4	(35.7)
Net realised and unrealised gains/(losses) on interest rate derivatives	43.6	(79.4)	14.8	(71.9)
Net realised and unrealised gains/(losses) on equity swap derivatives	37.8	25.2	(5.3)	(5.4)
Management fee revenue	35.2	16.8	7.7	8.6
Other revenue				
Life insurance contract premiums and related revenue	1,624.0	598.0	1,215.9	598.0
Change in life insurance contract liabilities	(1,141.5)	(395.6)	(794.6)	(395.6)
Change in life investment contract liabilities	72.3	(4.9)	71.3	(4.9)
Change in reinsurance contract liabilities	4.6	(38.6)	5.7	(38.6)
Total revenue	**1,800.9**	**1,601.8**	**1,484.3**	**1,222.8**

[1] Includes fair value movements in subordinated debt (Note 19 Fair values of financial assets and liabilities).

Recognition and measurement

Revenue is recognised and measured as the fair value of the consideration received or receivable to the extent that it is probable that economic benefits will flow to the Group and the revenue can be reliably measured. Revenues and expenses are generally recognised on an accrual basis. The following specific policies are applied:

- Interest revenue is recognised as it accrues using an effective interest rate method, taking into account the effective yield of the financial asset. Interest revenue on finance leases is recognised on a basis that reflects a constant periodic return on the net investment in the finance lease.

Note 1 Revenue (continued)

Recognition and measurement (continued)

- Gains or losses arising from changes in the fair value of financial instruments classified as fair value through profit and loss are recognised as revenue in the statement of comprehensive income when the change in value is recognised in the statement of financial position.
- Property rental revenue is accounted for on a straight line basis over the lease term. Contingent rental income is recognised as income in the period in which it is earned. Lease incentives granted are recognised as an integral part of the total rental income. Operating lease rental income is earned on a straight-line basis over the life of the contract.
- Dividend revenue from listed equity shares and listed property securities is recognised as income on the date the share is quoted ex-dividend. Dividend revenue from unlisted equity shares and unlisted property securities is recognised when the dividend is declared.
- Proceeds from the sale of rental assets are recognised upon disposal of the relevant assets.
- Management fee revenue is recognised when the services have been provided.
- Life insurance contract premiums are recognised as revenue when received.
- Changes in life insurance and investment contract liabilities arising from discount rates, inflation rates and other assumptions are recognised as revenue, with other movements being included in Note 2 Expenses. Refer to Note 8 Life contract liabilities for more detail on the recognition and measurement of life contract liabilities.

Note 2 Expenses

	Consolidated		Parent	
	30 June 2017 $M	30 June 2016 $M	30 June 2017 $M	30 June 2016 $M
Life insurance contract claims and expenses	339.3	226.6	278.2	226.6
Cost of life insurance contract liabilities	188.7	146.4	164.5	146.4
Cost of life investment contract liabilities	221.3	242.2	233.2	242.2
Reinsurance contracts	2.5	1.7	14.8	1.7
Investment property related expenses[1]	102.8	100.6	-	-
Development properties cost of sales	17.3	37.6	-	-
Management fee expense	45.5	41.8	33.5	31.1
Distribution expenses	31.0	24.9	30.6	24.5
Expenses SPV	7.3	8.3	-	-
Depreciation and amortisation expense	4.8	9.1	-	-
Infrastructure overheads	8.0	10.8	-	-
Other expenses	122.3	91.9	92.1	79.1
Total expenses	**1,090.8**	**941.9**	**846.9**	**751.6**

[1] Investment property related expenses relate to rental income-generating investment properties.

Recognition and measurement

Expenses are recognised on an accrual basis. The following specific policies are applied:

- Rental expenses incurred under an investment property operating lease are recognised on a straight line basis over the term of the lease.
- Investment property expenditure, including rates, taxes, insurance and other costs associated with the upkeep of a building, are brought to account on an accrual basis. Repair costs are expensed when incurred. Other amounts that improve the condition of the investment are capitalised into the carrying value of the asset.
- Life insurance contract claims and expenses are recognised in expenses when the liability to the policyholder under the contract has been established.
- Cost of life insurance and life investment contract liabilities recognised as an expense consists of the interest expense on the liability and any loss on the initial recognition of new business less the release of liability in respect of expenses incurred in the current period. The interest expense on the liability represents the unwind of the discount on the opening liability over the period, whereas the impacts of changes in the discount rate applied for the current valuation are included in the change in life contract liabilities disclosed in Note 1 Revenue.
- Refer to Note 8 Life contract liabilities for more detail on the recognition and measurement of life contract liabilities.

Note 3 Segment information

The reporting segment[1] of the Group has been identified as follows:

	CLC Segment 2017 $M	CLC Segment 2016 $M
For the year ended 30 June		
Net income	643.0	596.2
Operating expenses	(86.8)	(77.9)
Normalised EBIT	**556.2**	**518.3**
Interest and borrowing costs	-	-
Normalised net profit before tax	**556.2**	**518.3**
Tax on normalised profit	(119.9)	(131.3)
Normalised net profit after tax	**436.3**	**387.0**
Investment experience	17.6	(69.5)
Tax on investment experience	(8.7)	20.9
Profit attributable to shareholders of Challenger Life Company Limited	**445.2**	**338.4**
Other statutory segment information		
Revenue from external customers	1,016.9	912.4
Interest revenue	784.0	689.4
Interest expense	135.9	209.6
Depreciation and amortisation	4.8	19.2
Management view of statement of financial position		
As at 30 June		
Segment assets	16,016.4	14,456.9
Segment liabilities	(12,679.3)	(11,746.8)
Net assets attributable to shareholders of Challenger Life Company Limited	**3,337.1**	**2,710.1**
Non-controlling interests	13.6	3.6
Total equity	**3,350.7**	**2,713.7**

[1] Refer next page for definitions of the terms used in the management view of segments.

Note 3 Segment information (continued)

Definitions

Operating segments

The following segment is identified on the basis of internal reporting to key management personnel, including the Principle Executive Officer (the chief operating decision maker) of the Group, and comprise component parts of the Group that are regularly reviewed by senior management in order to allocate resources and assess performance:

CLC segment

The Group as a regulated life company operates solely in the CLC segment as a consolidated view of all the income and expenses attached to the life company.

Normalised vs. statutory results

Net income and operating expenses differ from revenue and expenses as disclosed in the statement of comprehensive income as certain direct costs (including distribution expenses, property expenses and management fees) included in expenses are netted off against revenues in deriving the management view of net income above. Net income consists of the normalised cash operating earnings (CLC segment).

In addition, the revenues, expenses and finance costs from Special Purpose Vehicles (SPV) are separately disclosed in the statutory view but are netted off in net income.

Revenue also includes investment gains and losses but these are excluded from the management view as they form part of investment experience (refer below).

Normalised cash operating earnings

This is calculated as cash earnings plus normalised capital growth (refer below). Cash earnings represents the sum of investment yield (being the management view of revenue from investment assets, such as net rental income, dividends and interest), interest expense, distribution expense and fees.

Normalised EBIT

Normalised earnings before interest and tax (EBIT) comprises net income less operating expenses, as defined above. It excludes investment experience and tax.

Interest and borrowing costs differ from finance costs as disclosed in the statement of comprehensive income for similar reasons to revenue and expenses, with the major difference arising from the netting of SPV finance costs against SPV revenue in net income in the management view.

Tax on normalised profit

Represents the consolidated statutory tax expense or benefit for the period, less tax attributable to non-controlling interests, less the tax applied to investment experience.

Investment experience after tax

The Group is required by accounting standards to value applicable assets and liabilities supporting the life insurance business at fair value where a fair value approach is available. This can give rise to fluctuating valuation movements being recognised in the statement of comprehensive income, particularly during periods of market volatility. As the Group is generally a long-term holder of assets, due to assets being held to match the term of life contract liabilities, the Group takes a long-term view of the expected capital growth of the portfolio rather than focusing on short-term volatility. Investment experience is a mechanism employed to remove the volatility arising from asset and liability valuation from the results so as to more accurately reflect the underlying performance of the Group.

Investment experience is calculated as the difference between the actual investment gains/losses (both realised and unrealised) and the normalised capital growth (refer below) plus annuity valuation experience. Investment experience after tax is investment experience net of tax at the prevailing income tax rate.

Normalised capital growth

This is determined by multiplying the normalised capital growth rate for each asset class by the average investment assets for the period. The normalised growth rates represent the Group's medium to long-term capital growth expectations for each asset class over the investment cycle.

The normalised growth rates for the year are +4.5% for equity and other investments, +4.0% for infrastructure, +2.0% for property and -0.35% for cash and fixed income. The rates have been set with reference to medium to long-term market growth rates and are reviewed to ensure consistency with prevailing market conditions.

Annuity valuation experience changes represent the impact of changes in macroeconomic variables, including bond yields and inflation factors, expense assumptions, losses on new business and other factors applied in the valuation of life contract liabilities. They also includes the attribution of the corresponding interest rate, foreign exchange and inflation derivatives used to hedge interest rate volatility.

Major customers

The Group does not rely on any large individual customers and consequently there is no significant concentration risk.

Geographical areas

The Group operates predominantly in Australia; hence, no geographical split is provided to the chief operating decision maker.

Note 3 Segment information (continued)

	30 June 2017 $M	30 June 2016 $M
Reconciliation of management to statutory view of after-tax profit		
Normalised net profit before tax (management view of pre-tax profit)	**556.2**	**518.3**
Tax on normalised profit	(119.9)	(131.3)
Normalised net profit after tax	**436.3**	**387.0**
Investment experience after tax	8.9	(48.6)
Profit attributable to non-controlling interests excluded from management view	0.4	1.5
Statutory view of profit after tax	**445.6**	**339.9**
Reconciliation of management view of revenue to statutory revenue		
Net income (management view of revenue)	**643.0**	**596.2**
Expenses and finance costs offset against revenue		
SPV expenses and finance costs offset against SPV income	96.7	61.6
Distribution expenses offset against related income	31.0	24.9
Change in life contract liabilities and reinsurance contracts recognised in expenses	751.8	616.9
Property related expenses offset against property income	120.1	138.2
Interest and loan amortisation costs	35.0	139.4
Management fees	45.5	41.8
Adjustment for non-controlling interests and other items	60.2	52.3
Difference between management view of investment experience and statutory recognition		
Actual capital growth	190.8	(57.7)
Normalised capital growth	(105.0)	(100.5)
Annuity valuation experience	(68.2)	88.7
Statutory revenue (refer Note 1 Revenue)	**1,800.9**	**1,601.8**

Note 4 Income tax

Analysis of income tax expense	Consolidated 30 June 2017 $M	Consolidated 30 June 2016 $M	Parent 30 June 2017 $M	Parent 30 June 2016 $M
Current income tax expense for the year	(180.7)	(80.6)	(178.7)	(66.6)
Current income tax (expense)/benefit prior year adjustment	(2.8)	7.2	(1.0)	5.5
Deferred income tax benefit/(expense)	49.9	(32.9)	73.6	(35.2)
Deferred income tax benefit/(expense) prior year adjustment	5.0	(4.1)	(7.9)	(1.1)
Income tax expense	**(128.6)**	**(110.4)**	**(114.0)**	**(97.4)**
Income tax benefit/(expense) on translation of foreign entities	11.2	(15.4)	-	-
Income tax (expense)/benefit on hedge of net investment in foreign entities	(11.0)	15.2	-	-
Income tax benefit/(expense) from other comprehensive income	**0.2**	**(0.2)**	**-**	**-**
Reconciliation of income tax expense				
Profit before income tax	574.2	450.3	559.3	414.0
Prima facie income tax based on the Australian company tax rate of 30%	(172.3)	(135.1)	(167.8)	(124.2)
Tax effect of amounts not assessable/deductible in calculating taxable income:				
- non-assessable and non-deductible items	35.7	35.6	56.7	27.9
- rate differential on offshore income	10.2	(8.3)	6.0	1.7
- other items	(2.2)	(2.6)	(8.9)	(2.8)
Income tax expense	**(128.6)**	**(110.4)**	**(114.0)**	**(97.4)**
Underlying effective tax rate[1]	**22.4%**	**24.6%**	**20.4%**	**23.5%**

[1] The calculation of the underlying effective tax rate excludes the non-controlling interests' profits of $0.4 million (30 June 2016: $1.5 million).

Consolidated Analysis of deferred tax	Statement of financial position 30 June 2017 $M	Statement of financial position 30 June 2016 $M	Statement of comprehensive income 30 June 2017 $M	Statement of comprehensive income 30 June 2016 $M
Deferred tax assets				
Accruals and provisions	2.1	3.3	(1.2)	1.9
Losses	16.8	10.1	6.7	(6.3)
Other	12.4	9.5	2.9	16.6
Total deferred tax assets	**31.3**	**22.9**	**8.4**	**12.2**
Deferred tax liabilities				
Unrealised foreign exchange movements	(14.4)	(22.3)	7.9	(6.2)
Unrealised gains on investments	(147.5)	(169.5)	18.8	(31.5)
Other	(2.1)	(21.9)	19.8	(11.5)
Total deferred tax liabilities	**(164.0)**	**(213.7)**	**46.5**	**(49.2)**
Net deferred tax liabilities (statement of financial position)	**(132.7)**	**(190.8)**		
Deferred income tax benefit/(expense) (statement of comprehensive income)			**54.9**	**(37.0)**

Note 4 Income tax (continued)

Parent

Analysis of deferred tax	Statement of financial position 30 June 2017 $M	Statement of financial position 30 June 2016 $M	Statement of comprehensive income 30 June 2017 $M	Statement of comprehensive income 30 June 2016 $M
Deferred tax assets				
Accruals and provisions	1.7	1.7	(0.1)	(0.8)
Other	16.7	4.6	12.2	1.4
Total deferred tax assets	**18.4**	**6.3**	**12.1**	**0.6**
Deferred tax liabilities				
Unrealised foreign exchange movements	(2.1)	(3.0)	0.9	0.7
Unrealised gains on investments	(134.2)	(192.9)	58.7	(31.2)
Other	(13.9)	(7.9)	(6.0)	(6.4)
Total deferred tax liabilities	**(150.2)**	**(203.8)**	**53.6**	**(36.9)**
Net deferred tax liabilities (statement of financial position)	**(131.8)**	**(197.5)**		
Deferred income tax benefit/(expense) (statement of comprehensive income)			**65.7**	**(36.3)**

Recognition and measurement

Income tax expense

Income tax expense for the year comprises current and deferred tax. Income tax is recognised in the statement of comprehensive income except to the extent that it relates to items recognised directly in equity.

Current tax assets and liabilities

Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities based on the respective period's taxable income. The tax rates and tax laws used to compute the amounts are those that are enacted or substantively enacted as at the statement of financial position date.

Deferred income tax

Deferred income tax is provided on all temporary differences at the statement of financial position date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred income tax liabilities

Deferred income tax liabilities are recognised for all taxable temporary differences except:

- when the deferred income tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss in the statement of comprehensive income; or
- when the taxable temporary difference is associated with investments in subsidiaries, associates or interests in joint ventures, and the timing of the reversal of the temporary difference can be controlled by the parent and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred income tax assets

Deferred income tax assets are recognised for all deductible temporary differences and carry-forward unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences and the carry-forward of unused tax credits and unused tax losses can be utilised, except:

- when the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss in the statement of comprehensive income; or
- when the deductible temporary difference is associated with investments in subsidiaries, associates or interests in joint ventures, in which case a deferred tax asset is only recognised to the extent that it is probable that the temporary difference will reverse in the foreseeable future and taxable profit will be available against which the temporary difference can be utilised.

Note 4 Income tax (continued)

Recognition and measurement (continued)

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted as at the statement of financial position date.

Income taxes relating to items recognised directly in equity are recognised in equity and not in profit or loss in the statement of comprehensive income. Deferred income tax assets and liabilities are offset only if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred tax assets and liabilities relate to the same taxable entity or tax consolidated group and the same taxation authority.

Tax consolidation

Challenger Limited and its 100% owned Australian tax resident subsidiaries have formed a tax consolidated group with effect from 1 July 2002 and are therefore taxed as a single entity from that date. Challenger Limited is the head entity of the tax consolidated group.

Tax effect accounting by members of the tax group

Members of the tax consolidated group have applied tax funding principles under which Challenger Limited and each of the members of the tax consolidated group agree to pay or receive tax equivalent amounts to or from the head entity, based on the current tax liability or current tax asset of the member. Such amounts are reflected in the amounts receivable from or payable to each member and the head entity. The group allocation approach is applied in determining the appropriate amount of current tax liability or current tax asset to allocate to members of the tax consolidated group.

Tax arrangements with other related parties

On 30 June 2005, the Company entered into a Tax Indemnity Agreement (the Agreement) with Challenger Life Company Holdings Pty Limited (CLH) and Challenger Limited (Challenger). Under the terms of the Agreement, CLH agreed to take responsibility for the majority of the Company's current and future tax related liabilities, and the Company assigned to CLH all the current and future rights and benefits conferred on the Company by Challenger under the Tax Funding Agreements in respect of the Company's Statutory Fund No. 2 (SF2) and Shareholders' Fund (SHF).

Additionally, CLH was responsible for, and indemnified the Group for, actual, contingent and tax-related liabilities of SF2 and SHF. Amounts receivable by the Company from CLH under the Tax Indemnity Agreement total $207.0 million (30 June 2016: $222.0 million). In December 2014, the Agreement was amended such that tax obligations and benefits of CLC arising after 31 December 2014 are no longer indemnified or transferred under the Agreement.

Section 3: Operating assets and liabilities

This section discloses information relating to the assets and liabilities underlying the Group's and the Company's financial performance and the key sources of funding for those assets. It further presents the derivative financial instruments employed to hedge the financial risk exposures, and consolidated information relating to the cash flows and holdings of cash and cash equivalents of both the Group and the Company.

Note 5 Financial assets – fair value through profit and loss

	Consolidated		Parent	
	30 June 2017 $M	30 June 2016 $M	30 June 2017 $M	30 June 2016 $M
Fixed income securities				
Domestic sovereign bonds and semi-government bonds	5,948.0	4,364.4	5,204.0	3,996.3
Floating rate notes and corporate bonds	5,123.1	4,788.0	3,879.1	3,564.6
Residential mortgage and asset-backed securities	2,538.0	2,065.2	1,803.4	1,569.6
Non-SPV mortgage assets	200.7	245.9	-	-
Controlled entities	-	-	2,281.4	2,371.1
	13,809.8	**11,463.5**	**13,167.9**	**11,501.6**
Equity securities				
Controlled entities	-	-	915.5	838.5
Shares in listed and unlisted corporations	64.7	54.8	158.5	49.0
Unit trusts, managed funds and other	664.1	545.4	218.3	189.8
	728.8	**600.2**	**1,292.3**	**1,077.3**
Infrastructure investments				
Units in listed and unlisted infrastructure trusts	336.7	369.4	177.8	158.0
Other infrastructure investments	305.5	331.7	-	-
	642.2	**701.1**	**177.8**	**158.0**
Property securities				
Indirect property investments in listed and unlisted trusts	**296.3**	**339.5**	**152.6**	**196.4**
Controlled trusts				
Infrastructure	-	-	318.6	303.5
Property	-	-	1,045.9	1,066.9
Other	-	-	792.3	601.2
	-	**-**	**2,156.8**	**1,971.6**
Total financial assets – fair value through profit and loss	**15,477.1**	**13,104.3**	**16,947.4**	**14,904.9**
Current	6,296.1	5,744.1	8,969.1	8,205.4
Non-current	9,181.0	7,360.2	7,978.3	6,699.5
	15,477.1	**13,104.3**	**16,947.4**	**14,904.9**

Note 5 Financial assets – fair value through profit and loss (continued)

Recognition and measurement

The Group categorises its financial assets into either financial assets - fair value through profit and loss (being initially designated as such) or available-for-sale (which includes transaction costs at initial recognition). The classification depends on the definition and the purpose for which the investments were acquired. Assets designated as fair value through profit and loss consist of fixed income, equity, infrastructure, and property securities. They are carried at fair value, with unrealised gains and losses being recognised through the statement of comprehensive income. There are currently no available-for-sale financial assets.

Purchases and sales of financial assets are recognised on the date on which the Group commits to purchase or sell the asset and when all risks and rewards of ownership have been substantially transferred. Financial assets are then derecognised when the right to receive cash flows from the asset has expired.

The fair value of financial assets that are actively traded in organised financial markets are determined by reference to quoted market bid prices at the close of business on the statement of financial position date.

Assets backing life contract liabilities of the statutory fund are required to be designated as fair value through profit and loss in accordance with AASB 1038 *Life Insurance Contracts* when permitted by other Australian Accounting Standards.

Key estimates and assumptions

Unlisted investment valuations

Investments held at fair value through profit and loss for which there is no active market or external valuation available are valued making as much use of available and supportable market data as possible and keeping judgemental inputs to a minimum, either by:

- reference to the current market value of another instrument that is substantially the same;
- using recent arm's length market transactions;
- options pricing models refined to reflect the issuer's specific circumstances;
- discounted cash flow analysis; or
- other methods consistent with market best practice.

Refer to Note 18 Financial risk management for further disclosure.

Note 6 Investment and development property

Consolidated	30 June 2017 $M	30 June 2016 $M
Investment property held for sale[1]	96.0	70.6
Investment property in use	3,359.4	3,378.7
Investment property under development	144.1	83.3
Total investment property	**3,599.5**	**3,532.6**
Development property held for resale[2]	29.4	37.3
Total investment and development property[3]	**3,628.9**	**3,569.9**

1 Held for sale properties: 12-30 Toll, 2-10 Toll, Century City Walk, Gennevilliers, Parcay-Meslay and Villeneuve les Beziers (30 June 2016: Elder House and Innaloo Cinema).

2 Development property held for resale is held at the lower of cost or net realisable value.

3 Investment property held for sale and development property held for resale are considered current. All other investment property is considered non-current.

Note 6 Investment and development property (continued)

Consolidated Reconciliation of carrying amounts	Investment property in use		Investment property under development		Development property held for resale	
	30 June 2017 $M	30 June 2016 $M	30 June 2017 $M	30 June 2016 $M	30 June 2017 $M	30 June 2016 $M
Balance at the beginning of the year	3,378.7	2,736.6	83.3	19.2	37.3	70.6
Movements for the year						
- acquisitions[1]	63.3	558.1	10.7	12.0	-	-
- disposals	(45.5)	(84.7)	-	-	(16.3)	(35.3)
- net transfers to investment property held for sale	(73.0)	(25.8)	-	-	-	-
- transfers from investment property under development	23.5	-	(23.5)	-	-	-
- capital expenditure	34.6	16.9	73.6	50.2	13.2	16.8
- net revaluation gain/(loss)	48.5	64.8	-	1.9	(4.8)	(14.8)
- foreign exchange (loss)/gain	(70.7)	112.8	-	-	-	-
Balance at the end of the year	3,359.4	3,378.7	144.1	83.3	29.4	37.3

[1] Investment property acquisitions: 839 Collins Street, VIC $10.7 million; 82 Northbourne Avenue, ACT $60.4 million; Aeon Kushiro, Japan (additional land parcel) $2.7 million.

Recognition and measurement

Investment and development property is initially recognised at cost, including transaction costs. Subsequent to initial recognition, investment and development property is recognised at fair value.

Independent valuations for all investment properties are conducted at least annually by suitably qualified valuers, and the Directors make reference to these independent valuations when determining fair value.

Each independent valuer is appointed in line with the valuation policy, which requires that valuers are authorised to practise under the law of the relevant jurisdiction where the valuation takes place and have at least five years of continuous experience in the valuation of property of a similar type to the property being valued.

The valuer must have no pecuniary interest that could conflict with the valuation of the property, must be suitably indemnified, and must comply with the Australian Property Institute (API) Code of Ethics and Rules of Conduct (or foreign equivalent).

Fair value for the purposes of the valuation is market value as defined by the International Assets Valuation Standards Committee. In determining market value, valuers examine available market evidence and apply this analysis to both the traditional market capitalisation approach and the discounted cash flow approach (using market-determined risk-adjusted discount rates). Valuers are required to provide valuation methodology and calculations for fair value including reference to annual net market income, comparable capitalisation rates, and property-specific adjustments. The values of investment property do not reflect anticipated enhancement from future capital expenditure.

Investment property is classified as held for sale if its carrying value will be recovered principally through a sale transaction rather than through continuing use. This condition is met only when management is committed to the sale, and the sale is highly probable. Investment property held for sale is carried at fair value, being the latest valuation available, or agreed sale price.

Gains or losses arising from changes in the fair values of investment properties are included in the statement of comprehensive income in the period in which they arise.

Investment properties are derecognised when they have either been disposed of or when the investment property is permanently withdrawn from use and no future benefit is expected from its disposal. Any gains or losses on the retirement or disposal of an investment property are recognised in the statement of comprehensive income in the year of retirement or disposal.

Where properties are debt financed, that finance is provided either by secured mortgages or by funding that contains a number of negative undertakings (including undertakings not to create or allow encumbrances, and undertakings not to incur financial indebtedness which ranks in priority to existing debt).

Investment property under development

When redevelopment of an existing investment property commences, it continues to be classified and measured as investment property when the asset is being redeveloped for continued future use as an investment property.

Investment property under construction is held at cost until an estimate of the fair value can be reliably determined.

Note 6 Investment and development property (continued)

Recognition and measurement (continued)

Development property held for resale

Development properties held for the purpose of resale are stated at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business on completion, less estimated costs of completion and selling costs.

Cost includes cost of acquisition, development costs, holding costs and directly attributable interest on borrowed funds where the development is a qualifying asset. Capitalisation of borrowing costs ceases during extended periods in which active development is interrupted. When a development is completed and ceases to be a qualifying asset, borrowing costs and other costs are expensed as incurred.

Property valuations

Analysis of investment property as at 30 June	Acquisition date[1]	Total cost[2] $M	Carrying value 2017 $M	Cap rate 2017[3] %	Last external valuation date	Carrying value 2016 $M	Cap rate 2016[3] %
Investment property in use and held for sale							
Australia							
1-9 Toll Drive, Altona North, VIC	31-Dec-08	-	-	-	-	4.0	7.50
2-10 Toll Drive, Altona North, VIC	31-Dec-08	6.3	7.0	7.00	31-Dec-16	7.1	7.00
12-30 Toll Drive, Altona North, VIC	31-Dec-08	13.9	13.6	7.50	31-Dec-16	13.3	7.50
Spotlight, Laverton North, VIC	31-Dec-08	-	-	-	-	20.6	7.00
Cosgrave Industrial Park, Enfield, NSW	31-Dec-08	91.9	105.8	6.25	31-Dec-16	69.5	6.84
21 O'Sullivan Circuit, NT	27-Jan-16	47.6	42.3	7.75	31-Dec-16	47.6	7.75
31 O'Sullivan Circuit, NT	27-Jan-16	28.6	27.3	8.00	31-Dec-16	28.6	8.25
31 Queen Street, VIC	31-Mar-11	97.4	136.8	5.75	31-Dec-16	118.4	6.50
35 Clarence Street, NSW	15-Jan-15	145.3	180.0	5.75	30-Jun-17	149.0	6.50
53 Albert Street, QLD	12-Dec-14	222.9	216.0	6.50	30-Jun-17	217.5	6.63
82 Northbourne Avenue, ACT	01-Jun-17	60.4	60.4	6.25	-	-	-
565 Bourke Street, VIC	28-Jan-15	88.1	90.1	6.00	31-Dec-16	88.6	6.50
ABS Building, ACT	01-Jan-00	120.1	124.0	7.00	30-Jun-17	126.5	7.50
215 Adelaide Street, QLD	31-Jul-15	242.6	230.0	6.75	30-Jun-17	230.0	6.75
County Court, VIC	30-Jun-00	215.1	301.0	6.25	31-Dec-16	290.6	6.50
DIBP (formerly DIAC) Building, ACT	01-Dec-01	103.3	122.5	6.75	30-Jun-17	121.0	7.50
Discovery House, ACT	28-Apr-98	88.2	105.1	7.50	31-Dec-16	104.2	7.75
Elder House, SA	21-Jun-02	48.3	23.0	9.00	30-Jun-17	25.8	8.75
Executive Building, TAS	30-Mar-01	33.6	40.9	7.50	31-Dec-16	38.2	7.75
Makerston House, QLD	14-Dec-00	67.7	68.3	8.00	31-Dec-16	65.4	8.50
Bunbury Forum, WA	03-Oct-13	152.8	151.0	6.25	30-Jun-17	151.0	6.50
Century City Walk, VIC	16-Oct-06	30.2	45.0	7.00	31-Dec-16	41.2	7.25
Channel Court, TAS	21-Aug-15	80.9	82.5	7.25	30-Jun-17	80.0	7.50
Golden Grove, SA	31-Jul-14	141.1	146.4	6.00	30-Jun-17	142.3	6.50
Innaloo Cinema, WA	17-Dec-01	-	-	-	-	44.8	7.25
Karratha, WA	28-Jun-13	54.2	54.3	7.00	30-Jun-17	62.3	7.00
Kings Langley, NSW	29-Jul-01	15.9	23.0	6.25	30-Jun-17	21.0	6.50
Lennox, NSW	27-Jul-13	28.2	35.5	6.25	30-Jun-17	33.5	6.50
Next Hotel, QLD	25-Mar-15	142.0	130.9	6.84	31-Dec-16	136.5	6.85
North Rocks, NSW	18-Sep-15	137.6	128.0	6.50	30-Jun-17	127.5	6.75
The Barracks, QLD	31-Oct-14	153.8	150.7	6.50	30-Jun-17	149.5	7.50
Total Australia		**2,658.0**	**2,841.4**			**2,755.5**	

1 Acquisition date represents the date of initial acquisition or consolidation of the investment vehicle holding the asset.
2 Total cost represents the original acquisition cost plus additions less full and partial disposals since acquisition date.
3 The capitalisation rate is the rate at which net market income is capitalised to determine the value of the property. The rate is determined with regard to market evidence.

Note 6 Investment and development property (continued)

Analysis of investment property as at 30 June (continued)	Acquisition date[1]	Total cost $M[2]	Carrying value 2017 $M	Cap rate 2017[3] %	Last external valuation date	Carrying value 2016 $M	Cap rate 2016[3] %
Europe							
Rozalia park	12-Apr-07	-	-	-	-	20.4	9.25
Rue Charles Nicolle, Villeneuve les Beziers	31-Dec-08	18.4	12.9	7.25	30-Jun-17	12.5	8.75
Avenue de Savigny, Aulnay sous Bois	31-Dec-08	20.3	12.0	6.25	30-Jun-17	14.0	7.00
105 Route d'Orleans, Sully sur Loire	31-Dec-08	27.1	9.1	8.00	30-Jun-17	10.0	10.00
140 Rue Marcel Paul, Gennevilliers	31-Dec-08	14.1	10.2	7.25	30-Jun-17	10.1	9.75
ZAC Papillon, Parcay-Meslay	31-Dec-08	10.1	7.3	7.50	30-Jun-17	7.2	9.25
Japan							
Aeon Kushiro	31-Jan-10	30.5	32.5	5.50	30-Jun-17	33.0	5.50
Carino Chitosedai	31-Jan-10	118.4	118.4	4.70	31-Dec-16	131.2	4.80
Carino Tokiwadai	31-Jan-10	77.0	76.4	4.70	30-Jun-17	84.3	4.80
DeoDeo Kure	31-Jan-10	31.9	28.8	5.60	30-Jun-17	31.8	5.80
Fitta Natalie Hatsukaichi	28-Aug-15	11.4	13.0	5.90	31-Dec-16	14.5	6.00
Izumiya Hakubaicho	31-Jan-10	68.9	66.9	5.00	31-Dec-16	74.4	5.10
Kansai Super Saigo	31-Jan-10	13.1	12.6	5.50	30-Jun-17	14.1	5.50
Kojima Nishiarai	31-Jan-10	12.2	13.3	4.60	30-Jun-17	14.1	4.90
Life Asakusa	31-Jan-10	27.8	31.3	4.60	30-Jun-17	34.8	4.70
Life Higashi Nakano	31-Jan-10	32.9	33.6	4.70	31-Dec-16	37.3	4.80
Life Nagata	31-Jan-10	25.2	26.2	5.00	30-Jun-17	28.5	5.00
MaxValu Tarumi	28-Aug-15	16.9	18.0	5.70	31-Dec-16	20.2	5.80
Seiyu Miyagino	31-Jan-10	9.7	9.7	5.70	30-Jun-17	10.9	5.70
Valor Takinomizu	31-Jan-10	26.8	23.3	5.70	31-Dec-16	26.3	6.10
Valor Toda	31-Jan-10	42.5	41.4	5.50	30-Jun-17	45.2	5.70
Yaoko Sakato Chiyoda	31-Jan-10	18.8	17.1	5.00	31-Dec-16	19.0	5.10
Total international		**654.0**	**614.0**			**693.8**	
Total investment property in use and held for sale[4]		**3,312.0**	**3,455.4**			**3,449.3**	
Investment property under development							
839 Collins Street, VIC	22-Dec-16	34.6	34.6	-	n/a	-	-
Cosgrave Industrial Park, Enfield, NSW	31-Dec-08	-	-	-	n/a	18.7	-
Gateway, NT	01-Jul-15	95.7	96.4	-	n/a	51.8	-
TRE Data Centre, ACT	14-Apr-10	13.1	13.1	-	n/a	12.8	-
Total investment property under development		**143.4**	**144.1**			**83.3**	
Development property held for resale							
Maitland, NSW	6-Dec-06	49.1	29.4	-	n/a	37.3	-
Total development property		**49.1**	**29.4**			**37.3**	

1 Acquisition date represents the date of initial acquisition or consolidation of the investment vehicle holding the asset.
2 Total cost represents the original acquisition cost plus additions less full and partial disposals since acquisition date.
3 The capitalisation rate is the rate at which net market income is capitalised to determine the value of the property. The rate is determined with regard to market evidence.
4 At 30 June 2017, the investment property portfolio occupancy rate for Australia was 93.8% (30 June 2016: 94.7%) with a weighted average lease expiry of 4.3 years (30 June 2016: 4.1 years), Europe 100.0% (30 June 2016: 95.0%) with a weighted average lease expiry of 1.4 years (30 June 2016: 1.7 years) and Japan 100% (30 June 2016: 100%) with a weighted average lease expiry of 8.7 years (30 June 2016: 8.4 years).

Note 7 Special Purpose Vehicles

Consolidated	30 June 2017 $M	30 June 2016 $M
Cash and cash equivalents	122.4	146.9
Mortgage assets[1]	1,364.7	1,739.7
Derivative assets	0.3	0.7
Total assets	**1,487.4**	**1,887.3**
Payables	69.1	69.7
Derivative liabilities	0.5	0.7
Interest bearing financial liabilities[1,2]	1,323.1	1,712.0
Total liabilities	**1,392.7**	**1,782.4**
Net assets	**94.7**	**104.9**
Cash flow hedge reserve	0.2	–
Total assets attributable to residual income unit (RIU) holders	**94.9**	**104.9**

1 $331.2 million (30 June 2016: $396.0 million) of the Mortgage assets balance is considered current, and $321.1 million (30 June 2016: $389.7 million) of the Interest bearing financial liabilities balance is considered current.

2 Differs to the statement of financial position - Interest bearing liabilities – SPV due to the value of cumulative eliminations between the SPV and other members of the Group of $149.1 million (30 June 2016: $145.4 million).

Recognition and measurement

The Group manages and services Special Purpose Vehicle (SPV) trusts that hold residential mortgage-backed assets and issue securitised financial liabilities. The trusts are entities that fund pools of residential mortgage-backed loans via the issuance of residential mortgage-backed securities (RMBS). All borrowings of these SPV are limited in recourse to the assets of the SPV.

As the Group retains the beneficial interest to the residual income of these trusts, it is deemed to control them and, as a result, they are consolidated. However, the significant risks and rewards (most notably credit risk) lie with the RMBS holders.

The assets and liabilities of the SPV have been separately disclosed in the financial report as, this presentation is considered to provide a more transparent view of the Group's financial position. Transactions between the SPV and other entities within the Group are eliminated on consolidation.

SPV cash and cash equivalents are financial assets and comprise cash at bank plus short-term deposits with an original maturity of three months or less that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. Cash and cash equivalents are recognised at fair value.

SPV mortgage assets are non-derivative financial loan assets with fixed or determinable payments that are not quoted in an active market. They are recognised at their fair value.

The Group uses derivative financial instruments to hedge the risks associated with SPV interest rate and foreign currency fluctuations. All these derivative financial instruments are stated at fair value. Gains or losses arising from fair value changes on derivatives that do not qualify for hedge accounting are recognised in the statement of comprehensive income.

SPV payables represent unsecured non-derivative, non-interest bearing financial liabilities in respect of goods and services provided to the trusts prior to the end of the financial year. They include accruals and other creditors and are recognised at amortised cost.

SPV interest bearing financial liabilities are initially recognised at fair value calculated net of directly attributable transaction costs, and subsequently measured at fair value. Any difference is recognised in the statement of comprehensive income.

Note 8 Life contract liabilities

	Consolidated		Parent	
	30 June 2017 $M	30 June 2016 $M	30 June 2017 $M	30 June 2016 $M
Life investment contract liabilities – at fair value	6,356.5	6,915.3	6,744.7	6,915.3
Life insurance contract liabilities – at margin on services value	3,885.5	2,555.3	3,514.4	2,555.3
Reinsurance contract liabilities – at margin on services value	80.2	87.9	63.1	87.9
Total life contract liabilities	**10,322.2**	**9,558.5**	**10,322.2**	**9,558.5**

Consolidated	Life investment contract liabilities		Life insurance contract liabilities		Outward reinsurance contract liabilities		Total life contract liabilities	
Movement in life contract liabilities	30 June 2017 $M	30 June 2016 $M	30 June 2017 $M	30 June 2016 $M	30 June 2017 $M	30 June 2016 $M	30 June 2017 $M	30 June 2016 $M
Balance at the beginning of the year	6,915.3	6,626.9	2,555.3	2,013.3	87.9	52.8	9,558.5	8,693.0
Deposits and premium receipts	2,417.6	2,769.8	1,624.0	598.0	-	-	4,041.6	3,367.8
Payments and withdrawals	(3,125.4)	(2,728.5)	(339.3)	(226.6)	(5.6)	(5.2)	(3,470.3)	(2,960.3)
Revenue per Note 1	(72.3)	4.9	(482.5)	(202.4)	(4.6)	38.6	(559.4)	(158.9)
Expense per Note 2	221.3	242.2	528.0	373.0	2.5	1.7	751.8	616.9
Balance at the end of the year	**6,356.5**	**6,915.3**	**3,885.5**	**2,555.3**	**80.2**	**87.9**	**10,322.2**	**9,558.5**

Parent	Life investment contract liabilities		Life insurance contract liabilities		Outward reinsurance contract liabilities		Total life contract liabilities	
Movement in life contract liabilities	30 June 2017 $M	30 June 2016 $M	30 June 2017 $M	30 June 2016 $M	30 June 2017 $M	30 June 2016 $M	30 June 2017 $M	30 June 2016 $M
Balance at the beginning of the year	6,915.3	6,626.9	2,555.3	2,013.3	87.9	52.8	9,558.5	8,693.0
Deposits and premium receipts	2,853.9	2,769.8	1,215.9	598.0	-	-	4,069.8	3,367.8
Payments and withdrawals	(3,186.4)	(2,728.5)	(278.2)	(226.6)	(33.9)	(5.2)	(3,498.5)	(2,960.3)
Revenue per Note 1	(71.3)	4.9	(421.3)	(202.4)	(5.7)	38.6	(498.3)	(158.9)
Expense per Note 2	233.2	242.2	442.7	373.0	14.8	1.7	690.7	616.9
Balance at the end of the year	**6,744.7**	**6,915.3**	**3,514.4**	**2,555.3**	**63.1**	**87.9**	**10,322.2**	**9,558.5**

Note 8 Life contract liabilities (continued)

Consolidated Analysis of life insurance and reinsurance contract liability and expenses	30 June 2017 $M	30 June 2016 $M
Best estimate liability		
Value of future life insurance contract benefits	3,783.1	2,564.4
Value of future expenses	207.2	102.8
Value of future premiums	(287.7)	(267.4)
Total best estimate liability	**3,702.6**	**2,399.8**
Value of future profit margins	263.1	243.4
Net life insurance and reinsurance contract liability	**3,965.7**	**2,643.2**
Life insurance and reinsurance contract operating expenses		
Maintenance expenses	27.7	10.0
Total life insurance and reinsurance contract operating expenses	**27.7**	**10.0**
Analysis of life contract profit		
Profit margin release on life insurance contracts	27.3	14.5
Loss recognition in respect of life insurance contracts[1]	(140.5)	(103.7)
Loss recognition in respect of life investment contracts	(94.0)	(106.2)
Difference in actual and assumed experience in respect of life insurance contracts	154.9	102.2
Difference in actual and assumed experience in respect of life investment contracts	289.1	266.7
Profit arising from difference between actual and assumed experience	**236.8**	**173.5**
Investment earnings on assets in excess of life contract liabilities	208.4	164.9
Life contract profit after tax[2]	**445.2**	**338.4**

1 Under Margin on Services (MoS), any profits expected over the life of a contract are recognised over the life of the contract; however, if on the liability valuation basis the contract is expected to be loss making, the capitalised value of these future losses is recognised at the point of sale. Retail insurance contracts are in loss recognition because the liability valuation basis uses a risk-free discount rate but the rates offered to customers are higher.

2 The parent total life contract profit after tax is $445.2 million (30 June 2016: $338.4 million)

Recognition and measurement

The operations of the Group include the selling and administration of life contracts through Challenger Life Company Limited (CLC). These contracts are governed under the *Life Insurance Act 1995* (the Life Act) and are classified as either life insurance contracts or life investment contracts. Life insurance and life investment contract liabilities are collectively referred to as life contract liabilities or policy liabilities.

Life investment contract liabilities

Life investment contracts are contracts regulated under the Life Act but which do not meet the definition of life insurance contracts under AASB 1038 *Life Insurance Contracts* and similar contracts issued by entities operating outside of Australia.

For fixed term policies, the liability is based on the fair value of the income payments and associated expenses, being the net present value of the payments and expenses using an appropriate discount rate curve as determined by the Appointed Actuary.

Life insurance contract liabilities

Life insurance contracts are contracts regulated under the Life Act that involve the acceptance of significant insurance risk. Insurance risk is defined as significant if, and only if, an insured event could cause an insurer to pay significant additional benefits in any scenario, excluding scenarios that lack commercial substance (i.e. have no discernible effect on the economics of the transaction).

The financial reporting methodology used to determine the value of life insurance contract liabilities is referred to as margin on services (MoS). Under MoS, the excess of premiums received over payments to customers and expenses (the margin) is recognised over the life of the contract in a manner that reflects the pattern of risk accepted from the policyholder (the service) unless future margins are negative, in which case the future losses are recognised in the statement of comprehensive income in the period in which they occur. The planned release of this margin is recognised in the statement of comprehensive income as part of the movement in life insurance contract liabilities.

Life insurance contract liabilities are usually determined using a projection method, whereby estimates of policy cash flows (premiums, payments and expenses) are projected into the future. The liability is calculated as the net present value of these projected cash flows using a risk-free discount rate curve.

Note 8 Life contract liabilities (continued)

Life insurance contract liabilities (continued)

The key areas of judgement in the determination of the actuarial assumptions are the duration of claims/policy payments, acquisition and maintenance expense levels, and economic assumptions for discount and inflation rates.

Life insurance premium revenue

Life insurance premiums are recognised as revenue when received.

Life insurance claims expense

Life insurance claims expense is recognised in expenses when the liability to the policyholder under the contract has been established.

Reinsurance

The Group has maintained reinsurance arrangements during the period that meet the definition of a life insurance contract. The MoS methodology requires the present value of future cash flows arising from reinsurance contracts to be included in the calculation of life insurance contract liabilities.

Valuation

The MoS valuation, calculated in accordance with APRA Prudential Standards, results in the systematic release of planned margins over the life of the policy via a 'profit carrier'. The Group maintains life insurance contracts including individual lifetime annuities, wholesale mortality, wholesale morbidity and longevity reinsurance. Annuity payments are used as the profit carrier for individual lifetime annuities and premium receipts or best estimate claim payments are used as the profit carrier for wholesale mortality, wholesale morbidity and longevity reinsurance.

Key assumptions applied in the valuation of life contract liabilities

Discount rates

Under APRA Prudential Standards and AASB 1038 *Life Insurance Contracts*, life insurance contract liabilities are calculated by discounting expected future cash flows at a risk-free rate, set at the Commonwealth Government Bond curve plus an illiquidity premium where applicable or for foreign-denominated liabilities, a curve derived from the yields of highly liquid AAA-rated sovereign risk securities in the currency of the policy liabilities plus an illiquidity premium where applicable. The illiquidity premium is determined by reference to observable market rates including Australian sovereign debt, corporate, securitised and collateralised debt publicly placed in the domestic market, and market swap rates.

Life investment contract liabilities are calculated under the fair value through profit and loss provisions of AASB 139 *Financial Instruments: Recognition and Measurement*. The discount rates are determined based on the current observable, objective rates that relate to the nature, structure and term of the future liability cash flows.

For both insurance and investment contracts the approach is the same as adopted at 2016. Discount rates applied for Australian liabilities were between 2.2%-4.2% per annum (30 June 2016: 2.3%-3.3%).

Expenses

Forecasted expenses for the next year are allocated between acquisition, maintenance and investment based on the nature of the expense. Forecasted maintenance expenses are then converted to a per-contract unit cost or percentage of account balance, depending on the nature of the expense.

Inflation

Inflation estimates are based on long-term expectations and reviewed at least annually for changes in the market environment based on a comparison of real and nominal yields of instruments of equivalent term and credit risk. The current assumption for Australia is 1.4% for short-term inflation and 2.4% for long-term per annum (30 June 2016: 0.9% short-term, 1.8% long-term).

Surrenders

For life investment contracts, no surrenders or voluntary discontinuances are assumed. For inwards reinsurance of Japanese business a rate of surrenders is assumed in line with local experience in relation to similar contracts, currently 3.5% per annum.

Where policyholders have the option to commute a life insurance contract, the value of this option is included within the life contract liabilities.

Mortality

Base mortality rates for individual lifetime annuities are determined as a multiple of annuitant experience based on LML08 and LFL08 tables, adjusted for Challenger's own recent experience. LML08 and LFL08 are mortality tables developed by the Continuous Mortality Investigation (CMI) based on United Kingdom annuitant lives experience from 2007–2010. The tables refer to male and female lives respectively. Rates are adjusted for expected future mortality improvements based on observed and expected improvements. Rates of future mortality improvement for individual lifetime annuities applied are between 0.0%-2.3% per annum (30 June 2016: 0.0%-2.8%).

Base mortality rates for wholesale mortality and longevity reinsurance are determined as a multiple of pensioner mortality rates (based on the self-administered pension schemes or SAPS2 tables mortality investigation developed by the Institute and Faculty of Actuaries (UK) using United Kingdom data collected between 2004–2012) or Vita Curves (proprietary mortality curves developed by Hymans Robertson where mortality rates vary by several rating factors) or population rates as appropriate. Rates are adjusted for expected future mortality improvements based on observed and expected improvements. Rates of future mortality improvement applied are between 0.0%-2.8% per annum (30 June 2016: 0.0%-4.0%). Base mortality rates for retrocession of Japanese business are determined as a multiple of Japanese population mortality rates.

Note 8 Life contract liabilities (continued)

Valuation (continued)

Impact of changes in assumptions on life insurance contracts

Under MoS, changes in actuarial assumptions are recognised by adjusting the value of future profit margins in life insurance contract liabilities. Changes in future profit margins are released over future periods unless that product group is in an expected net loss position (loss recognition), in which case changes in assumptions are recognised in the statement of comprehensive income in the period in which they occur. The valuation impact of changes to discount rate assumptions as a result of market and economic conditions, such as changes in benchmark market yields, are recognised in the statement of comprehensive income in the period in which the changes occur.

Restrictions on assets

The Life Act requires the Group to hold investments to back life contract liabilities in separate statutory funds. The assets in a statutory fund can only be used to meet the liabilities and expenses of that fund, to acquire investments to further the business of the fund or make distributions when capital adequacy requirements are met.

Statutory fund information

The life contract operations of CLC are conducted within four separate statutory funds as required by the Life Act. Both the shareholders' and policyholders' interests in these statutory funds are reported in aggregate in the financial report of the Group. Fund 1 is a non-investment-linked fund and Fund 3 is investment-linked. Both of these are closed to new business. Funds 2 and 4 are the principal operating funds of the Group. Fund 2 contains non-investment-linked contracts, including the Group's term annuity business, lifetime annuity policies and the related reinsurance, plus the wholesale mortality, wholesale morbidity and longevity reinsurance. Fund 4 was established on 7 March 2017 and contains retrocession of fixed term business written in Japan.

Life contract liabilities for Funds 1, 2, 3 and 4 are $2.8 million, $9,746.6 million, $3.0 million and $569.8 million respectively (30 June 2016: $3.3 million, $9,552.1 million, $3.1 million, nil).

Current/non-current split for total life contracts

There is a fixed settlement date for the majority of life contract liabilities. Approximately $1,903.2 million on a discounted basis (30 June 2016: $2,481.6 million) of life contract liabilities have a contractual maturity within 12 months of the reporting date. Based on assumptions applied for the 30 June 2017 valuation of life contract liabilities, $2,318.3 million of principal payments on fixed term and lifetime business are expected in the year to 30 June 2018 (expected in the year to 30 June 2017: $2,781.7 million).

Life insurance risk

The Group is exposed to longevity risk on its individual lifetime annuities and wholesale longevity reinsurance. Longevity risk is the risk that policyholders may live longer than expectations. The Group is exposed to mortality risk on the wholesale mortality reinsurance and retrocession of fixed term business written in Japan. This is the risk that death rates in the reference portfolios exceed expectations. The Group is also exposed to morbidity risk on the wholesale morbidity reinsurance. That is the risk that morbidity rates in the reference portfolios exceed expectation. The Group manages the longevity risk by regular reviews of the portfolio to confirm continued survivorship of policyholders receiving income plus regular review of longevity experience to ensure that longevity assumptions remain appropriate. In addition, the Group has entered into reinsurance arrangements to manage longevity risk in respect of closed books of individual lifetime annuities. The Group manages the mortality and morbidity risk by regular reviews of the portfolio to ensure that mortality and morbidity assumptions remain appropriate.

Insurance risk sensitivity analysis

The table below discloses the sensitivity of life insurance contract liabilities, profit after income tax and equity to changes in the key assumptions relating to insurance risk, both gross and net of reinsurance:

	Increase in life insurance contract liabilities				Loss after tax and equity impact			
	Gross		Net		Gross		Net	
Insurance risk sensitivity analysis	30 June 2017 $M	30 June 2016 $M	30 June 2017 $M	30 June 2016 $M	30 June 2017 $M	30 June 2016 $M	30 June 2017 $M	30 June 2016 $M
50% increase in the rate of mortality improvement	43.0	42.0	26.0	21.5	(30.1)	(29.4)	(18.2)	(15.1)
10% increase in maintenance expenses	12.4	9.0	12.4	9.0	(8.7)	(6.3)	(8.7)	(6.3)

Note 8 Life contract liabilities (continued)

Liquidity risk for insurance contracts

The following table summarises the undiscounted maturity profile of the Group's life insurance contract liabilities. The analysis is based on undiscounted estimated cash outflows, including interest and principal payments. The undiscounted maturity profile of life investment contracts is disclosed in Note 18 Financial risk management:

Undiscounted life insurance contract liabilities	1 year or less $M	1-3 years $M	3-5 years $M	>5 years $M	Total $M
2017	405.1	713.1	580.2	3,310.9	5,009.3
2016	228.5	399.3	344.5	2,310.1	3,282.4

Actuarial information

Mr A Bofinger FIAA, as the Appointed Actuary of CLC, is satisfied as to the accuracy of the data used in the valuations of life contract liabilities in the financial report and the tables in this note. The life contract liabilities have been determined at the reporting date in accordance with the Life Act.

Note 9 External unit holders' liabilities

Consolidated	30 June 2017 $M	30 June 2016 $M
Current	1,225.2	750.0
Non-current	462.6	565.5
Total liabilities to external unit holders	**1,687.8**	**1,315.5**

Recognition and measurement

The Group controls a number of guaranteed index return trusts that contain contributed funds in respect of fixed term wholesale mandates. The fixed term and guaranteed nature of the mandates effectively places the balance of the risks related to the performance of the trusts with the Group. As a result, the Group is deemed to control these trusts.

The contributed funds for these trusts are classed as a liability and external unit holders' liabilities on the statement of financial position represents the funds owing to third parties on these mandates. The liability is recognised at fair value.

Note 10 Derivative financial instruments

Consolidated Analysis of derivative financial instruments	30 June 2017 Notional value $M	30 June 2017 Net fair value assets $M	30 June 2017 Net fair value liabilities $M	30 June 2016 Notional value $M	30 June 2016 Net fair value assets $M	30 June 2016 Net fair value liabilities $M
Non-SPV						
Interest rate swaps						
Less than one year	4,772.0	10.7	(3.3)	3,100.2	42.2	(3.4)
One to three years	7,402.9	43.8	(29.4)	6,730.5	53.9	(29.7)
Three to five years	2,962.3	45.4	(15.8)	2,640.9	68.1	(42.6)
Greater than five years	15,728.2	276.6	(191.0)	12,916.2	499.1	(414.3)
Total interest rate swaps	**30,865.4**	**376.5**	**(239.5)**	**25,387.8**	**663.3**	**(490.0)**
Inflation-linked swaps						
Less than one year	867.1	3.3	(5.8)	297.0	9.4	(0.1)
One to three years	430.0	9.3	-	664.0	16.5	(6.0)
Three to five years	116.8	3.0	(8.5)	162.0	6.2	-
Greater than five years	482.3	22.2	(13.7)	508.0	31.7	(28.9)
Total inflation-linked swaps	**1,896.2**	**37.8**	**(28.0)**	**1,631.0**	**63.8**	**(35.0)**
Futures contracts						
Less than one year	8,967.6	-	(0.5)	3,963.1	-	(0.5)
One to three years	-	-	-			
Total futures contracts	**8,967.6**	**-**	**(0.5)**	**3,963.1**	**-**	**(0.5)**
Forward currency contracts						
Less than one year	2,769.2	34.8	(26.6)	2,523.0	47.2	(16.8)
One to three years	-	-	-	3.7	-	-
Total forward currency contracts	**2,769.2**	**34.8**	**(26.6)**	**2,526.7**	**47.2**	**(16.8)**
Cross-currency swaps						
Less than one year	904.0	7.4	(67.8)	246.0	-	(47.7)
One to three years	1,184.1	28.5	(78.3)	788.4	9.5	(98.7)
Three to five years	897.6	16.4	(36.2)	639.4	22.3	(117.9)
Greater than five years	27.7	-	(6.8)	83.5	-	(23.7)
Total cross-currency swaps	**3,013.4**	**52.3**	**(189.1)**	**1,757.3**	**31.8**	**(288.0)**
Equity swaps						
Less than one year	1,178.4	22.5	(6.7)	1,053.2	16.1	(22.1)
Three to five years	320.7	1.1	(1.1)	261.4	6.0	(5.5)
Total equity swaps	**1,499.1**	**23.6**	**(7.8)**	**1,314.6**	**22.1**	**(27.6)**
Credit default swaps						
Less than one year	131.7	0.3	(0.1)	134.3	0.8	-
One to three years	49.1	0.3	-	175.9	0.1	(3.9)
Three to five years	726.1	40.0	(0.1)	10.0	-	(0.1)
Greater than five years	-	-	-	9.4	-	(0.7)
Total credit default swaps	**906.9**	**40.6**	**(0.2)**	**329.6**	**0.9**	**(4.7)**

Note 10 Derivative financial instruments (continued)

Consolidated Analysis of derivative financial instruments (continued)	30 June 2017 Notional value $M	Net fair value assets $M	Net fair value liabilities $M	30 June 2016 Notional value $M	Net fair value assets $M	Net fair value liabilities $M
Options						
One to three years	2.1	-	-	0.3	-	-
Total options	**2.1**	**-**	**-**	**0.3**	**-**	**-**
Total non-SPV	**49,919.9**	**565.6**	**(491.7)**	**36,910.4**	**829.1**	**(862.6)**
SPV						
Interest rate swaps – SPV						
Less than one year	8.7	-	(0.1)	11.1	-	(0.1)
One to three years	12.0	-	(0.1)	13.2	-	(0.2)
Three to five years	1.6	-	-	2.5	-	(0.1)
Total interest rate swaps – SPV	**22.3**	**-**	**(0.2)**	**26.8**	**-**	**(0.4)**
Cross-currency swaps – SPV						
Greater than five years	471.1	0.3	(0.3)	727.6	0.7	(0.3)
Total cross-currency swaps – SPV	**471.1**	**0.3**	**(0.3)**	**727.6**	**0.7**	**(0.3)**
Total – SPV	**493.4**	**0.3**	**(0.5)**	**754.4**	**0.7**	**(0.7)**
Total derivative financial instruments[1]		**565.9**	**(492.2)**		**829.8**	**(863.3)**

[1] The Group's derivative financial instruments are subject to enforceable netting arrangements under International Swaps and Derivatives Association (ISDA) Master Agreements with derivative counterparties, allowing for net settlement as a single arrangement of multiple instruments with a counterparty in the event of default or other specified circumstances. If applied to the derivative portfolio, the derivative assets would reduce by $275.9 million (30 June 2016: $453.5 million) and the derivative liabilities would reduce by $275.9 million (30 June 2016: $453.5 million).

Recognition and measurement

The Group uses derivative financial instruments predominantly to hedge its risks associated with interest rate and foreign currency fluctuations and to gain exposure to different markets. All derivative financial instruments are stated at fair value. Gains or losses arising from fair value changes on derivatives that do not qualify for hedge accounting are recognised in the statement of comprehensive income.

For the purpose of hedge accounting, hedges are classified as:

- fair value hedges when they hedge the exposure to changes in the fair value of a recognised asset or liability;
- cash flow hedges when they hedge the exposure to variability in cash flows that is attributable either to a particular risk associated with a recognised asset or liability or to a forecast transaction; or
- hedges of net investments in foreign operations when they hedge the exposure to changes in the value of the assets and liabilities of a foreign controlled entity when they are translated from their functional currency to the presentation currency.

At the inception of a hedge relationship to which the Group wishes to apply hedge accounting, the Group formally designates and documents the hedge relationship and the risk management objectives and strategies for undertaking the hedge. The documentation includes identification of the hedging instrument, the hedged item or transaction, the nature of the risk being hedged and how the entity will assess the effectiveness of the instrument in offsetting the exposure to changes in the hedged item.
Such hedges are expected to be highly effective in achieving offsetting changes in fair values, cash flows or foreign exchange difference and are assessed on an ongoing basis to determine that they actually have been highly effective over the period that they were designated.

Fair value hedges

Fair value hedges are hedges of the Group's exposure to changes in the fair value of a recognised asset or liability or an unrecognised firm commitment, or an identified portion of such an asset, liability or firm commitment that is attributable to a particular risk and could affect profit or loss.

For fair value hedges, both the carrying amount of the hedged item and the derivative are remeasured to fair value through the statement of comprehensive income. The same applies where the hedged item is an unrecognised firm commitment. Any subsequent cumulative change in the fair value of the firm commitment attributable to the hedged risk is recognised as an asset or liability, with a corresponding gain or loss recognised in the statement of comprehensive income.

Note 10 Derivative financial instruments (continued)

The Group discontinues fair value hedge accounting if the hedging instrument expires or is sold, terminated or exercised, the hedge no longer meets the criteria for hedge accounting or the Group revokes the designation.

Cash flow hedges

Cash flow hedges are hedges of the Group's exposure to variability in cash flows attributable to a particular risk associated with a recognised asset or liability, or a highly probable forecast transaction, and that could affect the statement of comprehensive income. The effective portion of the gain or loss on the hedging instrument is recognised directly in equity, while the ineffective portion is recognised in the statement of comprehensive income.

Amounts recognised in equity are transferred to the statement of comprehensive income when the hedged transaction affects profit or loss, such as when hedged income or expenses are recognised or when a forecast sale or purchase occurs. When the hedged item is the cost of a non-financial asset or liability, the amounts taken to equity are transferred to the initial carrying amount of the non-financial asset or liability.

If the forecast transaction is no longer expected to occur, amounts previously recognised in equity are transferred to the statement of comprehensive income. If the hedging instrument expires or is sold, terminated or exercised without replacement or rollover, or if its designation as a hedge is revoked, amounts previously recognised in equity remain in equity until the forecast transaction occurs.

Hedges of net investments in foreign operations

The gain or loss on the effective portion of the hedging instrument is recognised directly in equity and the gain or loss on the ineffective portion is recognised immediately in the statement of comprehensive income. The cumulative gain or loss previously recognised in equity is recognised in other comprehensive income on disposal or partial disposal of the foreign operation.

Derivatives designated as hedges of net investment in foreign currency operations

The Group hedges its exposure to accounting gains and losses arising from translation of foreign controlled entities from their functional currency into the Group's presentation currency on consolidation. At 30 June 2017, a post-tax gain of $25.8 million (30 June 2016: post-tax loss $35.5 million) was recognised in equity for the hedging of exposure to the net investment in foreign currency operations.

Derivatives designated as cash flow hedges

The Group applies hedge accounting when it can demonstrate that all, or a portion of, the value movements of a derivative financial instrument effectively hedges the variability in cash flows attributable to a specific risk associated with a recognised asset or liability or probable future transaction. As described in Note 18 Financial risk management, SPV enter into interest rate swap agreements to hedge the interest rate risk between variable rate loans, which generally reprice with changes in official interest rates, and issued RMBS that reprice with changes in the 30-day and 90-day bank bill swap rate. Cross-currency swaps are also entered into to hedge currency movements on foreign denominated RMBS. The SPV apply hedge accounting to both types of transaction, with the fair value change on the effective portion of the derivative being recognised in equity.

For the year ended 30 June 2017, a post-tax loss of $0.2 million (30 June 2016: post-tax loss $1.4 million) was recognised in equity for cash flow hedges with no statement of comprehensive income impact of any ineffective portions during either the current or prior comparative period.

Note 11 Collateral arrangements

The Company receives collateral, where it is considered necessary, when entering into certain financial arrangements. The amount of collateral required is subject to management's credit evaluation of the counterparty, which is performed on a case by case basis. $268.0 million (30 June 2016: $278.3 million) cash received from third parties as collateral is recorded in payables. CLC is not permitted to sell or re-pledge financial or non-financial assets held as collateral in the absence of default by the owner of the collateral.

The Company is required to pledge collateral, as part of standard terms of transactions, when entering into certain financial arrangements. Cash paid to third parties as collateral is recorded in receivables. Other financial assets transferred as collateral are not derecognised from the statements of financial position, as the risks and rewards of ownership remain with the Company. At the balance sheet date, the fair value of cash and financial assets pledged are as follows:

Consolidated Collateral pledged as security	30 June 2017 $M	30 June 2016 $M
Cash	176.3	303.3
Other financial assets	4,375.6	2,700.0
Total collateral pledged	**4,551.9**	**3,003.3**

Note 12 Notes to the statements of cash flows

Reconciliation of profit to operating cash flows	Consolidated 30 June 2017 $M	Consolidated 30 June 2016 $M	Parent 30 June 2017 $M	Parent 30 June 2016 $M
Profit for the year	**445.6**	**339.9**	**445.3**	**316.6**
Adjusted for				
Net realised and unrealised (gains)/loss on investment assets	(8.2)	(325.1)	41.7	(91.3)
Change in life contract liabilities[1]	192.4	458.0	192.4	458.0
Depreciation and amortisation expense	4.8	9.1	-	-
Change in operating assets and liabilities				
Decrease/(increase) in receivables	74.2	(90.0)	2.2	43.8
Decrease/(increase) in other assets	0.8	(6.8)	-	-
Increase/(decrease) in payables	(9.8)	4.3	62.9	(75.7)
Increase in life contract liabilities	571.3	407.5	571.3	407.5
Increase in external unit holders' liabilities	372.3	370.8	-	-
(Decrease)/increase in net tax liabilities	(54.7)	54.0	(56.1)	38.5
Net cash flows from operating activities	**1,588.7**	**1,221.7**	**1,259.7**	**1,097.4**

1 Changes relate to movements through the statement of comprehensive income.

Reconciliation of cash	Consolidated 30 June 2017 $M	Consolidated 30 June 2016 $M	Parent 30 June 2017 $M	Parent 30 June 2016 $M
Cash at bank	422.3	430.7	136.4	137.3
Cash at bank - SPV	122.4	146.9	-	-
Other cash equivalents	8.7	10.7	-	-
Total cash and cash equivalents[1]	**553.4**	**588.3**	**136.4**	**137.3**

1 All cash and cash equivalents are considered current.

Recognition and measurement

Cash and cash equivalents are financial assets and comprise cash at bank plus short-term deposits with an original maturity of three months or less that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. Cash and cash equivalents are recognised at fair value. For the purposes of the statement of cash flows, cash and cash equivalents are stated net of bank overdrafts.

Section 4: Capital structure and financing costs

This section outlines how the Group and the Company manages its capital structure and related financing costs, as well as capital adequacy and reserves. It also provides details on the dividends of the Company.

Note 13 Contributed equity

	30 June 2017		30 June 2016	
	No. of shares/notes M	Value of shares $M	No. of shares/notes M	Value of shares $M
Ordinary shares				
Opening ordinary shares issued	1,196.5	1,196.5	1,196.5	1,196.5
New ordinary shares issued	-	-	-	-
Total ordinary shares	**1,196.5**	**1,196.5**	**1,196.5**	**1,196.5**
Equity hybrid notes				
Opening equity hybrid notes	3.5	345.0	3.5	345.0
New equity hybrid notes	4.6	460.0	-	-
Total equity hybrid notes	**8.1**	**805.0**	**3.5**	**345.0**
Total contributed equity		**2,001.5**		**1,541.5**

Recognition and measurement

Ordinary shares are classified as equity. Issued capital in respect of ordinary shares is recognised as the fair value of the consideration received by the parent entity. Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

On 7 April 2017, CLC completed its second notes issue, raising $460.0 million of new funding. The issue features similar structural characteristics to CLC's first $345.0 million hybrid equity issue completed on 9 October 2014. Both note issuances were approved by APRA as qualifying as Additional Tier 1 capital of CLC and are classified as equity.

Terms and conditions of contributed equity

Ordinary shares

A holder of an ordinary share is entitled to receive dividends and to one vote on a show of hands and on a poll.

Equity hybrid notes

The holder of a note is entitled to receive distributions on the notes at the discretion of the Board of CLC and to the extent that the Board has determined that a distribution can be paid. Distributions are non-cumulative. Holders are not permitted to vote at any meeting of shareholders of CLC or to otherwise participate in the profits of CLC. Holders of notes rank ahead of ordinary shares, equally among other instruments approved as Additional Tier 1 capital of CLC and behind any claims of creditors of CLC.

On the occurrence of a non-viability trigger event as determined by APRA, the notes can be written-off or converted to shares in CLC in part or in whole in an amount that is sufficient to ensure that CLC does not become non-viable. CLC is also entitled to optionally redeem the notes (subject to APRA approval) on a specified date or as a result of certain tax or regulatory events occurring (as defined in the note terms and conditions).

Capital management

A company is generally limited in the risk-taking activities that it can engage in by the amount of capital it holds, with capital acting as a buffer against risk, ensuring that there are sufficient resources to enable the company to continue normal business in the event of an unexpected loss.

Credit ratings

Standard & Poor's long-term credit rating for CLC at the date of the statement of financial position is 'A' (stable). The rating remained unchanged during the year.

Equity issue and Additional Tier 1 instrument

The Company is growing strongly and expects to materially increase the size of its annuity business. Following the equity and Additional Tier 1 instrument issuance in 2015, a $460.0 million equity hybrid note issuance (regarded as Additional Tier 1 capital under APRA prudential standards) was issued during the year.

Internal Capital Adequacy Assessment Process (ICAAP) Summary Statement – CLC

CLC is a life insurance company regulated under the *Life Insurance Act 1995* (Life Act). The Life Act, via Prudential Standards issued by APRA, imposes minimum statutory capital requirements on all life insurance companies. Under these standards, a life company must have in place an ICAAP, documented in an ICAAP Summary Statement. CLC complied with these requirements at all times during the year.

Note 13 Contributed equity (continued)

Capital management (continued)

Prescribed capital amount (PCA)

CLC holds capital in order to ensure that under a range of adverse scenarios it can continue to meet its regulatory and contractual obligations to its customers. CLC is regulated by APRA and is required to hold a minimum level of regulatory capital.

CLC's regulatory capital base and PCA have been calculated based on the prudential standards issued by APRA.

In April 2017, CLC completed its second hybrid notes issue, raising $460.0 million. The proceeds of the issue were used for Additional Tier 1 capital issued by CLC to support the forecast growth of its annuity business.

The PCA ratio at 30 June 2017 was 1.57 times (30 June 2016: 1.57 times), reflecting changes in asset allocation, net AUM growth, changes in retained earnings, increased Additional Tier 1 capital and repayment of Tier 2 regulatory capital.

Subordinated debt

CLC's total regulatory capital base includes $395.4 million (30 June 2016: $445.5 million) of admissible subordinated debt. Subordinated debt totalling $190.3 million was repaid during the period. These tranches had an eligible Tier 2 regulatory capital value of $65.7 million. Under prudential standards, subordinated debt tranches issued prior to 1 January 2013 will continue to be fully eligible as Tier 2 regulatory capital until each tranche's first call date after 1 January 2013, and will then amortise over the ensuing four years.

As at 30 June 2017, CLC's remaining subordinated debt balance has a call date in November 2017. As such, this tranche will continue to be fully eligible as Tier 2 regulatory capital until its call date in November 2017 and will continue to be partially eligible until November 2021.

CLC's target surplus

CLC maintains a target level of capital representing APRA's PCA plus a target surplus. The target surplus is a management guide to the level of excess capital that CLC seeks to hold over and above APRA's minimum requirements. CLC's target surplus is set to ensure that it provides a buffer against adverse market conditions and having regard to CLC's credit rating. CLC uses internal capital models to determine its target surplus, which are risk-based and are responsive to changes in CLC's asset allocation and market conditions.

Details of the CLC capital adequacy multiple are below:

	30 June 2017 $M	30 June 2016 $M
CLC's excess capital under prudential standards		
Common equity Tier 1 regulatory capital	2,169.0	2,003.6
Additional Tier 1 regulatory capital	805.0	345.0
Tier 2 regulatory capital – subordinated debt[1]	395.4	445.5
CLC total regulatory capital base	**3,369.4**	**2,794.1**
Prescribed capital amount		
Asset risk charge[2]	2,067.1	1,712.0
Insurance risk charge	157.5	168.3
Operational risk charge	38.7	28.7
Aggregation benefit	(119.2)	(125.3)
CLC prescribed capital amount	**2,144.1**	**1,783.7**
CLC excess over prescribed capital amount	**1,225.3**	**1,010.4**
Capital adequacy ratio (times)	**1.57**	**1.57**

1 Differs from $393.6 million disclosed in Note 14 Interest bearing financial liabilities due to $1.8 million (30 June 2016: $2.3 million) of accrued interest and nil (30 June 2016: $133.5 million) inadmissible Tier 2 regulatory capital.

2 Asset risk charge includes the combined stress scenario adjustment and default stress.

Note 14 Interest bearing financial liabilities

Consolidated[1]	30 June 2016 Facility $M	Opening balance $M	Cash flows Proceeds/ (repayments)[3] $M	Non-cash movements Foreign exchange $M	Fair value changes $M	Other $M	30 June 2017 Closing balance $M	Facility $M
Bank loans								
Controlled property trusts[2]	568.5	556.3	4.4	(42.9)	0.9	1.3	520.0	537.0
Controlled infrastructure trusts	204.3	204.3	(3.2)	-	-	-	201.1	201.1
Repurchase agreements	2,454.2	2,454.2	833.3	-	-	-	3,287.5	3,287.5
Total bank loans	**3,227.0**	**3,214.8**	**834.5**	**(42.9)**	**0.9**	**1.3**	**4,008.6**	**4,025.6**
Non-bank loans								
Subordinated debt issuance	576.7	576.7	(190.3)	(11.3)	18.5	-	393.6	393.6
Other finance	19.5	19.5	(2.1)	(2.7)	3.0	-	17.7	17.7
Total non-bank loans	**596.2**	**596.2**	**(192.4)**	**(14.0)**	**21.5**	**-**	**411.3**	**411.3**
Total interest bearing financial liabilities	**3,823.2**	**3,811.0**	**642.1**	**(56.9)**	**22.4**	**1.3**	**4,419.9**	**4,436.9**
Current		2,737.8					3,336.0	
Non-current		1,073.2					1,083.9	
		3,811.0					**4,419.9**	

1 The amounts held directly by the parent entity are the repurchase agreements (current) and subordinated debt issuance (non-current).
2 Total facility limit consists of redraw loan facilities limits totalling $101.0 million (30 June 2016: $121.0 million) and non-redraw loan facilities limits totalling $436.0 million (30 June 2016: $447.5 million).
3 Differs to Statement of cash flows due to $392.6 million (30 June 2016: $570.3 million) repayments relating to SPV.

Recognition and measurement

All borrowings and subordinated debt are financial liabilities and are initially recognised at fair value. In the case of borrowings which are subsequently measured at amortised cost, the initial measurement is calculated net of directly attributable transaction costs. For borrowings and subordinated debt which are subsequently measured at fair value through profit or loss, directly attributable transaction costs are expensed.

Borrowings of certain controlled investment trusts of CLC's statutory funds are subsequently measured at amortised cost for the purpose of determining the unit price of those trusts. These borrowings are measured at amortised cost in this financial report, with a difference between the proceeds (net of transaction costs) and the redemption amount recognised in the statement of comprehensive income over the period of the contract using the effective interest rate method.

All other borrowings of the controlled entities of the statutory funds, or their controlled entities, are subsequently measured at fair value, with movements recognised in the statement of comprehensive income. Subordinated debt is recognised at fair value. The determination of fair value includes the assessment of movements in interest rates, credit spreads and foreign exchange. These movements are reviewed at each reporting date to take into account market conditions.

Repurchase agreements are all short-term in nature, and are therefore valued at amortised cost.

Details of liabilities

Bank loans

Controlled property trusts

The loans have variable terms and are generally secured by way of first-ranking mortgages over the investment properties. The 30 June 2017 balance includes $333.3 million (30 June 2016: $377.2 million) of Australian dollar equivalent of Yen denominated loans in the Japanese property trusts. Other controlled property trusts loans total $186.7 million (30 June 2016: $179.1 million).

Controlled infrastructure trusts

The facility has an expiry date of June 2022 and is secured by way of first-ranking mortgages over the corresponding infrastructure assets.

Repurchase agreements

CLC has entered into repurchase agreements with certain counterparties whereby fixed income securities are sold for cash whilst simultaneously agreeing to repurchase the fixed income security at a fixed price and fixed date in the future. These agreements finance bonds held for hedging purposes and are interest bearing, with interest factored into the price at which the bonds are repurchased and paid on repurchase. All agreements as at 30 June 2017 are current and all except $630.0 million matured in July 2017. The remaining agreements mature in August 2017 ($595.0 million) and September 2017 ($35.0 million). They will continue to be rolled into new agreements in the future.

Note 14 Interest bearing financial liabilities (continued)

Non-bank loans

Subordinated debt issuance

The Group issued subordinated notes into the US private placement market of US$150.0 million in December 2006 and $400.0 million in November 2007.

The December 2006 notes were fully repaid during the period. The November 2007 issuance matures at 30 years with a non-call period of 10 years and carries a floating rate of interest. The proceeds of this issuance were made available to Statutory Fund No. 2 of CLC (SF2) and ranks in right of payment either pari passu with, or senior to, all other unsecured and subordinated indebtedness of SF2, except for such indebtedness preferred by operation of bankruptcy laws or similar laws of general application. Subordinated debt is measured at fair value through the profit and loss and adjusted for movements in interest rates, credit spreads and foreign exchange rates (if applicable).

The notes were issued under Australian Prudential Regulation Authority (APRA) approved Instruments of Issue and are counted as Approved Subordinated Debt for regulatory capital purposes. As at 30 June 2017, all remaining subordinated debt is fully eligible as Tier 2 regulatory capital.

Other finance

Other finance includes a limited recourse non-bank loan held for the financing of equipment totalling $17.0 million. The loan has a maturity date of November 2020.

Key estimates and assumptions

Subordinated debt valuation

Subordinated debt is recognised at fair value and is valued by reference to the trading margin on the Challenger Capital Notes, adjusted to allow for both issues' higher ranking in the capital structure (using market comparable instruments) and illiquidity.

The change recognised in the statement of comprehensive income in respect of valuation changes for the year ended 30 June 2017 was a loss of $18.5 million (30 June 2016: $3.9 million).

Note 15 Reserves and retained earnings

	Consolidated		Parent	
	30 June 2017 $M	30 June 2016 $M	30 June 2017 $M	30 June 2016 $M
Foreign currency translation reserve[1]				
Balance at the beginning of the year	(3.5)	(6.1)	-	-
(Loss)/gain on translation of foreign entities[2]	(25.8)	38.1	-	-
Gain/(loss) on hedge of net investment in foreign entities[2]	25.8	(35.5)	-	-
Balance at the end of the year	**(3.5)**	**(3.5)**	**-**	**-**
Adjusted controlling interests reserve[1]				
Balance at the beginning of the year	12.2	18.9	-	-
Change in holdings in controlled entities	-	(6.7)	-	-
Balance at the end of the year	**12.2**	**12.2**	**-**	**-**
Cash flow hedge reserve – SPV[1]				
Balance at the beginning of the year	-	1.4	-	-
Net loss on cash flow hedges	(0.2)	(1.4)	-	-
Balance at the end of the year	**(0.2)**	**-**	**-**	**-**
Other reserve				
Balance at the beginning of the year	132.3	124.8	137.8	137.8
Movement in distributable reserves	-	7.5	-	-
Balance at the end of the year	**132.3**	**132.3**	**137.8**	**137.8**
Total reserves	**140.8**	**141.0**	**137.8**	**137.8**
Retained earnings				
Balance at the beginning of the year	1,027.6	898.6	1,016.6	909.4
Profit attributable to equity holders	445.2	338.4	445.3	316.6
Dividends paid	(278.0)	(209.4)	(278.0)	(209.4)
Total retained earnings	**1,194.8**	**1,027.6**	**1,183.9**	**1,016.6**

1 These items may eventually be recycled to the profit and loss section of the statement of comprehensive income.
2 Net of tax.

Note 15 Reserves and retained earnings (continued)

Recognition and measurement

Foreign currency translation reserve

This reserve is used to record foreign exchange differences arising from the translation of the foreign subsidiaries. It also includes the effective portion of fair value changes on foreign exchange derivative contracts designated as hedges of a net investment in a foreign entity.

Adjusted controlling interests reserve

This reserve relates to changes arising from movements in the ownership interests in entities already controlled by the Group. The difference between the fair value of the consideration paid/received for the change in holding and the change in the Group's share of the net assets of the entity is recorded in this reserve.

Cash flow hedge reserve – SPV

This comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments related to hedged transactions.

Other reserve

This distributable reserve relates to amounts indemnified to CLC by its parent.

Note 16 Finance costs

	Consolidated		Parent	
	30 June 2017 $M	30 June 2016 $M	30 June 2017 $M	30 June 2016 $M
Interest expense	89.4	139.4	78.1	57.2
Interest expense – SPV	35.0	53.3	-	-
Interest expense – property trusts	11.5	16.9	-	-
Total finance costs	**135.9**	**209.6**	**78.1**	**57.2**

Recognition and measurement

Finance costs represent interest incurred on interest bearing financial liabilities (primarily repurchase agreements and the securitised residential mortgage-backed securities (RMBS) issued by the consolidated Special Purpose Vehicles (SPV), subordinated debt, bank loans and other borrowings) and are recognised as an expense in the period in which they are incurred.

Finance costs that are directly attributable to the acquisition, construction or production of qualifying property assets (being assets that take a substantial period of time to develop for their intended use or sale) are capitalised as part of the cost of those assets. Revenue earned on the investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalisation.

To the extent that the Group allocates general borrowed funds for the purpose of obtaining a qualifying property asset, the borrowing costs eligible for capitalisation are determined by applying a capitalisation rate to the expenditure on that asset. The capitalisation rate is the weighted average of the borrowing costs applicable to the borrowings that are outstanding during the period, other than borrowing made specifically for the purpose of obtaining the qualifying asset.

Note 17 Dividends paid and proposed

Parent	30 June 2017 $M	30 June 2016 $M
Unfranked dividends declared and paid during the year		
Ordinary shares	260.0	190.0
Equity hybrid notes	18.0	19.4
Total unfranked dividends declared and paid during the year	**278.0**	**209.4**
Unfranked dividends proposed (not recognised as a liability at 30 June)		
Ordinary shares	210.0	170.0
Total unfranked dividends proposed (not recognised as a liability at 30 June)	**210.0**	**170.0**

Section 5: Risk management

This section outlines how financial risk is managed within the Group and the Company, providing additional information about how the overall risk management program seeks to minimise potentially adverse financial effects associated with key financial risks. This section also provides disclosures on the fair values of assets and liabilities of the Group, the valuation techniques used in determining fair value of those assets and liabilities, and the sensitivities of assets categorised as Level 3 instruments to reasonable changes in valuation assumptions.

Note 18 Financial risk management

Governance and risk management framework

The Group's activities expose it to a variety of financial risks, such as market risk (including currency risk, interest rate risk, equity price risk and credit spread risk), credit default risk and liquidity risk. The management of these risks is fundamental to the Group's business and to building shareholder value. The Board is responsible, in conjunction with senior management, for understanding the risks associated with the activities of the Group and implementing structures and policies to adequately monitor and manage those risks.

The Board has established the Life Risk Committee (LRC) and the Life Audit Committee (LAC) to assist in the discharge of certain responsibilities. In particular, the LRC assists the Board in setting the risk appetite and ensuring that the Group has an effective risk management framework incorporating management, operational and financial controls.

The Board has established the Asset Liability Committee (ALCo) to identify, monitor and report on financial risks.

The ALCo is an executive committee chaired by the Chief Risk Officer (CRO) and is responsible for driving the required actions to ensure that risks are managed in accordance with the Board approved policies. The management of these risks is supported by a comprehensive range of policies and practice notes.

Financial risks are managed by the Group in the context of the wider Challenger Limited Group risk management framework. The Executive Risk Management Committee (ERMC) is an executive committee, chaired by the Chief Risk Officer (CRO), which assists the LRC, LAC and Board in the discharge of their risk management obligations by implementing the Board-approved risk management framework.

The Challenger Limited Group's Risk Management division has day-to-day responsibility for monitoring the implementation of the framework with oversight, analysis, monitoring and reporting of risks. The CRO provides regular reporting to the LRC and the Board.

The Group's principal financial instruments consist of derivatives, cash and cash equivalents, receivables, available-for-sale assets, financial assets at fair value through profit. and loss, payables, life investment contract liabilities and other interest bearing financial liabilities.

Details of the significant accounting policies and methods adopted, including the criteria for recognition, the basis of measurement and the basis on which income and expenses are recognised, in respect of each class of financial instruments, are disclosed in Section 1: Basis of preparation and overarching significant accounting policies or the relevant note.

Market risk

Market risk is the risk that the fair value and/or future cash flows from a financial instrument will fluctuate as a result of changes in market factors. Market risk comprises (amongst others) interest rate risk (due to fluctuations in market interest rates), price risk (due to fluctuations in the fair value of equities or credit spreads) and currency risk (due to fluctuations in foreign currency exchange rates).

Interest rate risk

Interest rate risk is the risk of fluctuations in the Group's earnings and equity arising from movements in market interest rates, including changes in the absolute levels of interest rates, the shape of the yield curve, the margin between the different yield curves and the volatility of interest rates.

The Company's market risk policy is approved by the Board and sets out the relevant risk limits for interest rate exposure. It is the Company's policy to minimise the impact of interest rate movements on its projected future cash flows. The management of the risks associated with life investment and life insurance contracts, including interest rate risk, are subject to the prudential requirements of the Life Act and APRA. This includes satisfying capital adequacy requirements, which in turn include consideration of how the interest rate sensitivities of assets and liabilities are matched.

For the SPV, the impact of a rising/falling bank bill swap rate (BBSW) benchmark over the Reserve Bank of Australia's target cash rate results in an increase/decrease in the cost of funding and therefore on the profit of the trusts. This interest rate risk is mitigated by actively adjusting the interest rates charged to borrowers if a sustained adverse differential to the benchmark is evidenced. SPV entities are also exposed to the risks arising from borrowers fixing the rates on their mortgage. This interest rate risk is managed by using cash flow hedges to swap the fixed rate to a floating rate exposure at an amount equal to the notional value of the mortgages being fixed.

Note 18 Financial risk management (continued)

Interest rate sensitivity

The Group's sensitivity to movements in interest rates in relation to the value of financial assets and liabilities is shown in the table below. It is assumed that the change happens at the statement of financial position date and that there are concurrent movements in interest rates and parallel moves in the yield curve. All material underlying exposures and related hedges are included in the analysis. The impact on profit and equity is post-tax at a rate of 30%. The risks faced and methods used in the sensitivity analysis are the same as those applied in the comparative period.

As shown below, 100 basis points (1%) movements in interest rates would have only a small net impact on the Group's financial position, as upside risks in the Company and the property trusts largely offset downside risk in the SPV, and vice versa:

	Change in variable	30 June 2017 Profit/(loss) $M	30 June 2017 Change in equity $M	30 June 2016 Profit/(loss) $M	30 June 2016 Change in equity $M
Non-SPV	+100bps	2.6	2.6	5.7	5.7
	-100bps	(2.6)	(2.6)	(5.7)	(5.7)
SPV	+100bps	(1.2)	(1.2)	(1.5)	(1.5)
	-100bps	1.2	1.2	1.5	1.5
Total	**+100bps**	**1.4**	**1.4**	**4.2**	**4.2**
	-100bps	**(1.4)**	**(1.4)**	**(4.2)**	**(4.2)**

Price risk

Price risk is the risk that the fair value of a financial instrument will fluctuate as a result of changes in market prices (other than those arising from interest rate or currency risk), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting all similar financial instruments. The Group is exposed to equity price risk on its holdings in equity securities, which include a range of investments in absolute return strategies where returns are considered to be generally uncorrelated to listed equity market returns, and credit spread risk on its fixed income securities. The Group is required to fair value all equities and fixed income securities held to back life contract liabilities.

Equity risks will arise as a natural result of the Company's Asset Allocation Plan. The Group's primary tools for managing investment price risks are the Internal Capital Adequacy Assessment Process (ICAAP) and Asset Allocation Plan.

Equity price risk sensitivity

The potential impact of movements in the market value of listed and unlisted equities on the Group's statement of comprehensive income and statement of financial position is shown in the below sensitivity analysis.

The impact on profit and equity is post-tax at a rate of 30%. The risks faced and methods used in the sensitivity analysis are the same as those applied in the comparative period. As shown below, a 10% movement in equity prices would have a material impact on the consolidated Group's financial position. It is assumed that the relevant change occurs as at the reporting date:

Equity securities by asset class classification	Change in variable	30 June 2017 Profit/(loss) $M	30 June 2017 Change in equity $M	30 June 2016 Profit/(loss) $M	30 June 2016 Change in equity $M
Property securities	+10%	20.7	20.7	23.8	23.8
	-10%	(20.7)	(20.7)	(23.8)	(23.8)
Infrastructure investments	+10%	23.6	23.6	25.9	25.9
	-10%	(23.6)	(23.6)	(25.9)	(25.9)
Other assets	+10%	43.0	43.0	30.3	30.3
	-10%	(43.0)	(43.0)	(30.3)	(30.3)
Total assets	**+10%**	**87.3**	**87.3**	**80.0**	**80.0**
	-10%	**(87.3)**	**(87.3)**	**(80.0)**	**(80.0)**

Note 18 Financial risk management (continued)

Price risk (continued)

Credit spread risk sensitivity

The Group is exposed to price movements resulting from credit spread fluctuations through its fixed income securities net of subordinated debt. As at 30 June 2017, a 50 basis point increase/decrease in credit spreads would result in a post-tax (at 30%) unrealised loss/gain in the statement of comprehensive income and equity of $98.9 million (30 June 2016: $71.3 million).

Currency risk

It is the Company's policy to minimise the exposure of all statement of financial position items to movements in foreign exchange rates other than instruments considered to be Tier 2 capital under regulatory standards. Currency exposure arises primarily as a result of investments in the Eurozone, Japan, the United Kingdom and the United States, so currency risk therefore arises from fluctuations in the value of the Euro, Japanese yen, British pound and US dollar against the Australian dollar. In order to protect against foreign currency exchange rate movements, the Group has entered into foreign currency derivatives.

In addition, the Group has exposure to foreign exchange risk upon consolidation of its foreign currency denominated controlled entities and mitigates this by designating foreign currency derivatives as hedges of net investments in foreign entities in equity to match its foreign currency translation reserve exposure. Effectiveness is monitored on a regular basis to ensure that the hedge remains between 80-125% effective and any ineffective portion of the hedge is recognised directly in the statement of comprehensive income.

The SPV entities hedge exposure to foreign currency risk arising from issuing mortgage-backed securities in foreign currencies. The currencies impacted are primarily the British pound, Euro and US dollar. All derivatives in the SPV are designated as cash flow hedges. These hedges are effective, and there is no material impact on the profit and loss. The following table details the Group's net exposure to foreign currency as at the reporting date in Australian dollar equivalent amounts:

	GBP $M	USD $M	Euro $M	JPY $M	Other $M
30 June 2017					
Financial assets	665.1	1,877.6	608.9	260.2	388.6
Financial liabilities	(18.4)	(3.0)	(16.0)	-	-
Foreign currency contracts and cross currency swaps	(649.8)	(1,876.5)	(593.1)	(258.3)	(389.6)
Net exposure in Australian dollars	**(3.1)**	**(1.9)**	**(0.2)**	**1.9**	**(1.0)**
30 June 2016					
Financial assets	581.4	1,852.6	475.6	297.0	378.6
Financial liabilities	(43.3)	(201.0)	(21.2)	-	-
Foreign currency contracts and cross currency swaps	(531.6)	(1,687.5)	(458.9)	(286.4)	(373.9)
Net exposure in Australian dollars	**6.5**	**(35.9)**	**(4.5)**	**10.6**	**4.7**

The analysis in the currency risk table shows the impact on the statement of comprehensive income and equity of a movement in the Group's major foreign currency exposure exchange rates against the Australian dollar using the net exposure at the balance date. All underlying exposures and related hedges are included in the analysis.

A sensitivity of 10% has been applied, as this reflects a reasonable measurement given the current level of exchange rates and the volatility observed on an historic basis. The impact on profit and equity is post-tax at a rate of 30%.

The risks faced and methods used in the sensitivity analysis are the same as those applied in the comparative period. As shown in the table on the following page, a 10% movement in foreign currency exchange rates would have minimal impact on the Group's financial position.

Note 18 Financial risk management (continued)

Currency risk (continued)

	Movement in variable against $	30 June 2017 Profit/(loss) $M	30 June 2017 Change in equity $M	30 June 2016 Profit/(loss) $M	30 June 2016 Change in equity $M
British pound (GBP)	+10%	(0.2)	(0.2)	0.5	0.5
	-10%	0.2	0.2	(0.5)	(0.5)
US dollar (USD)	+10%	(0.1)	(0.1)	2.2	2.2
	-10%	0.1	0.1	(2.2)	(2.2)
Euro (EUR)	+10%	-	-	(0.3)	(0.3)
	-10%	-	-	0.3	0.3
Japanese yen (JPY)	+10%	-	0.1	-	0.7
	-10%	-	(0.1)	-	(0.7)
Other	+10%	(0.1)	(0.1)	0.3	0.3
	-10%	0.1	0.1	(0.3)	(0.3)

Credit default risk

The Group makes use of external ratings agencies (Standard & Poor's, Fitch, Moody's or other reputable credit rating agencies) to determine credit ratings. Where a counterparty or debt obligation is rated by multiple external rating agencies, the Group will use Standard & Poor's ratings where available or otherwise in accordance with the current APRA Prudential Standards. All credit exposures with an external rating are also rated internally and cross-referenced to the external rating, if applicable. Where external credit ratings are not available, internal credit ratings are assigned by appropriately qualified and experienced credit personnel who operate separately from the risk originators.

Each business unit is responsible for managing credit risks that arise with oversight from a centralised credit risk management team.

Credit exposure by credit rating

The table below provides information regarding the maximum credit risk exposure of the Group in respect of the major classes of financial assets by equivalent credit rating. The maximum credit exposure is deemed to be the carrying value of the asset not including any collateral or other credit protection in place. The analysis classifies the assets according to internal or external credit ratings. Assets rated investment grade are those rated S&P BBB– or above, with non-investment grade therefore being below BBB–.

	Investment grade				Non-inv.		
	AAA $M	AA $M	A $M	BBB $M	grade $M	Other $M	Total $M
30 June 2017							
Cash and cash equivalents	431.0	-	-	-	-	-	431.0
Cash and cash equivalents – SPV	122.4	-	-	-	-	-	122.4
Receivables	29.8	13.7	161.0	24.9	6.0	499.0	734.4
Mortgage assets – SPV	757.5	332.4	269.5	-	5.3	-	1,364.7
Fixed income securities	6,797.4	933.8	1,350.1	2,716.0	1,935.0	77.5	13,809.8
Derivative assets	-	483.6	42.2	3.1	37.0	-	565.9
Total assets with credit exposures	**8,138.1**	**1,763.5**	**1,822.8**	**2,744.0**	**1,983.3**	**576.5**	**17,028.2**
30 June 2016							
Cash and cash equivalents	441.4	-	-	-	-	-	441.4
Cash and cash equivalents – SPV	146.9	-	-	-	-	-	146.9
Receivables	22.7	12.4	307.3	24.5	6.6	343.2	716.7
Mortgage assets – SPV	960.2	458.9	314.5	4.8	1.3	-	1,739.7
Fixed income securities	5,320.4	714.4	1,519.6	2,103.2	1,703.8	102.1	11,463.5
Derivative assets	-	770.9	58.0	0.9	-	-	829.8
Total assets with credit exposures	**6,891.6**	**1,956.6**	**2,199.4**	**2,133.4**	**1,711.7**	**445.3**	**15,338.0**

Note 18 Financial risk management (continued)

Credit default risk (continued)

Mortgage assets - SPV

Mortgage assets – SPV are funded via securitised residential mortgage-backed security (RMBS). As a result, the Group is not exposed to significant credit risk on these assets as this is borne by the RMBS holder. The credit risk of the mortgage loans within the SPV is therefore taken as being equivalent to that of the RMBS.

Collateral held over assets

In the event of a default against any of the mortgages in the SPV, the Trustee has the legal right to take possession of the secured property and sell it as a recovery action against settlement of the outstanding mortgage account balance. At all times of possession, the risks and rewards associated with ownership of the property are held by the trustee on behalf of the RMBS holder.

Ageing and impairment

The table below gives information regarding the carrying value of the Group's receivables. The analysis splits these assets by those that are neither past due nor impaired, those that are past due and not impaired (including an ageing analysis), and those past due and impaired at the statement of financial position date:

	Not past due/not impaired $M	Past due but not impaired 0-1 months $M	1-3 months $M	3-6 months $M	> 6 months $M	Past due and impaired $M	Total $M
30 June 2017							
Receivables	733.6	0.8	-	-	-	-	734.4
30 June 2016							
Receivables	716.5	0.2	-	-	-	-	716.7

Concentration risk

The credit risk framework includes an assessment of the counterparty credit risk in each business unit and at a total Group level. The Group has no significant concentrations of credit risk at the statement of financial position date.

Liquidity risk

Liquidity risk is the risk that the Group will encounter difficulty in raising funds to meet cash commitments. This may result from either the inability to sell financial assets at their face values, a counterparty failing on repayment of a contractual obligation, or the inability to generate cash inflows as anticipated.

The Group aims to ensure that it has sufficient liquidity to meet its obligations on a short, medium and long-term basis. The CLC liquidity management policy is approved by the CLC Board and sets out liquidity targets and management actions depending on actual liquidity levels relative to those targets. Detailed forecast cash positions are reported regularly to the CLC Asset Liability Committee. At the reporting date, all requirements of the CLC Board approved liquidity management policy were satisfied.

Note 18 Financial risk management (continued)

Maturity profile of undiscounted financial liabilities

The table below summarises the maturity profile of the Group's undiscounted financial liabilities. This is based on contractual undiscounted repayment obligations. Totals differ to the amounts on the statement of financial position by the amount of time value of money discounting reflected in the statement of financial position values:

	1 year or less $M	1-3 years $M	3-5 years $M	>5 years $M	Total $M
30 June 2017					
Payables	871.2	8.8	61.5	23.5	965.0
Interest bearing financial liabilities	3,344.7	170.4	397.4	650.7	4,563.2
Interest bearing financial liabilities – SPV	366.6	493.7	285.3	365.1	1,510.7
External unit holders' liabilities	1,225.2	462.6	-	-	1,687.8
Life investment contract liabilities	2,359.2	2,716.7	1051.6	612.8	6,740.3
Life insurance contract liabilities[1]	405.1	713.1	580.2	3,310.9	5,009.3
Derivative liabilities	111.1	108.9	60.6	211.6	492.2
Total undiscounted financial liabilities[1]	**8,683.1**	**4,674.1**	**2,436.6**	**5,174.7**	**20,968.5**
30 June 2016					
Payables	704.5	6.8	83.9	5.6	800.8
Interest bearing financial liabilities	2,814.1	104.8	462.4	695.5	4,076.8
Interest bearing financial liabilities – SPV	449.1	618.6	368.8	536.6	1,973.1
External unit holders' liabilities	750.0	565.5	-	-	1,315.5
Life investment contract liabilities	2,973.6	2,551.8	1,087.1	684.8	7,297.3
Life insurance contract liabilities[1]	228.5	399.3	344.5	2,310.1	3,282.4
Derivative liabilities	90.7	144.1	160.8	467.7	863.3
Total undiscounted financial liabilities[1]	**8,010.5**	**4,390.9**	**2,507.5**	**4,700.3**	**19,609.2**

[1] Disclosure of life insurance contract liabilities is not required under AASB7 *Financial risk management*, for reference purposes they have been included. Refer to Note 8 Life contract liabilities for further details.

Note 19 Fair values of financial assets and liabilities

Fair value determination and classification

Fair value reflects the price that would be received on sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The majority of the Group's financial instruments are held in the life insurance statutory funds of the Company backing its life investment and life insurance liabilities, and, as a result, are required by AASB 1038 *Life Insurance Contracts* to be designated at fair value through profit and loss where this is permitted under AASB 139 *Financial Instruments: Recognition and Measurement*.

Financial instruments measured at fair value are categorised under a three level hierarchy, reflecting the availability of observable market inputs when estimating the fair value. If different levels of inputs are used to measure a financial instrument's fair value, the classification within the hierarchy is based on the lowest level that is significant to the fair value measurement. The three levels are:

Level 1 Unadjusted quoted prices in active markets are the valuation inputs for identical assets or liabilities (i.e. listed securities).

Level 2 Valuation inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (as prices) or indirectly (derived from prices) are used.

Level 3 There are valuation inputs for the asset or liability that are not based on observable market data (unobservable inputs).

Note 19 Fair values of financial assets and liabilities (continued)

Fair value determination and classification (continued)

The unobservable inputs into the valuation of the Group’s Level 3 assets and liabilities are determined based on the best information available, including the Group's own assessment of the assumptions that market participants would use in pricing the asset or liability. Examples of unobservable inputs are estimates about the timing of cash flows, discount rates, earnings multiples and internal credit ratings.

Valuation techniques

The Group’s listed and unlisted fixed income securities, government/semi-government securities and over-the-counter derivative financial instruments are all classified as Level 2. This recognises the availability of a quoted price but not from an active market as defined by the standard. Fixed income securities where market observable inputs are not available are classified as Level 3. The Group derivative financial instruments are traded over-the-counter so, whilst they are not exchange traded, there is a market observable price. All of the fixed income and government/semi-government securities have prices determined by a market. Externally rated unlisted fixed income securities are valued by applying market observable credit spreads on similar assets with an equivalent credit rating. Internally-rated fixed income securities are Level 3, as the determination of an equivalent credit rating is a significant non-observable input.

Equity, infrastructure and property securities that are exchange traded are classified as Level 1. Where quoted prices are available, but are not from an active market, they are classified as Level 2. If market observable inputs are not available, they are classified as Level 3. Valuations can make use of cash flow forecasts discounted using the applicable yield curve, earning-multiple valuations or, for managed funds, the net assets of the trust per the most recent financial report.

The interest bearing financial liabilities classified as Level 3 include the subordinated debt that has been valued by reference to the trading margin on Challenger Limited’s Capital Notes, adjusted to allow for its higher ranking in the capital structure (using market comparable instruments) and illiquidity. External unit holders’ liabilities are valued at the face value of the amounts payable and classified as Level 2. The portion of life investment contract liabilities classified as Level 2 represents products or product options for which the liability is determined based on an account balance, rather than a discounted cash flow as applied to the rest of the portfolio.

Cash and cash equivalents are carried at amortised cost. To determine a fair value where the asset is liquid or maturing within three months, the fair value is approximate to the carrying amounts. This assumption is applied to liquid assets and the short-term elements of all other financial assets and financial liabilities.

Valuation process

For financial instruments and investment properties categorised within Level 3 of the fair value hierarchy, the valuation process applied in valuing such instruments is governed by the CLC Practice Note on Investment Asset and Financial Liability Valuation. The Practice Note outlines the Valuation Committee’s responsibilities in the valuation of investment assets and financial liabilities for the purposes of financial reporting. All significant Level 3 financial instruments are referred to the Valuation Committee, which generally meets monthly, or more frequently if required.

All financial instruments and investment properties are measured on a recurring basis. Refer Note 5 and Note 6 for further details on the valuation process applied to unlisted financial instruments and investment properties.

The table on the following page summarises the financial instruments and investment properties measured at fair value at each level of the fair value hierarchy as at the statement of financial position date.

Note 19 Fair values of financial assets and liabilities (continued)

	Level 1 $M	Level 2 $M	Level 3 $M	Total $M
30 June 2017				
Derivative assets	-	565.8	0.1	565.9
Fixed income securities[1]	-	11,724.0	2,085.8	13,809.8
Equity securities	134.0	333.4	261.4	728.8
Infrastructure investments[1]	122.4	110.6	409.2	642.2
Property securities	152.7	-	143.6	296.3
Investment and development property[2]	-	96.0	3,503.5	3,599.5
Assets attributable to RIU - SPV[3]	-	-	94.9	94.9
Total assets	**409.1**	**12,829.8**	**6,498.5**	**19,737.4**
Derivative liabilities	0.5	491.7	-	492.2
Interest bearing financial liabilities	-	61.0	410.6	471.6
External unit holders' liabilities	-	1,687.8	-	1,687.8
Life investment contract liabilities	-	75.9	6,280.6	6,356.5
Total liabilities	**0.5**	**2,316.4**	**6,691.2**	**9,008.1**
30 June 2016				
Derivative assets	-	829.8	-	829.8
Fixed income securities[1]	-	9,455.2	2,008.3	11,463.5
Equity securities	40.6	291.3	268.4	600.3
Infrastructure investments[1]	82.6	109.4	509.1	701.1
Property securities	196.3	-	143.2	339.5
Investment and development property[2]	-	70.6	3,462.0	3,532.6
Assets attributable to RIU – SPV[3]	-	-	104.9	104.9
Total assets	**319.5**	**10,756.3**	**6,495.9**	**17,571.7**
Derivative liabilities	-	863.2	0.1	863.3
Interest bearing financial liabilities	-	70.9	595.5	666.4
External unit holders' liabilities	-	1,315.5	-	1,315.5
Life investment contract liabilities	-	80.1	6,835.2	6,915.3
Total liabilities	**-**	**2,329.7**	**7,430.8**	**9,760.5**

1 The Group has exposures to structured entities (entities designed so that voting or similar rights are not the dominant factor in determining who controls the entity; for example when any voting rights relate purely to administrative tasks) via investments in asset-backed finance vehicles (where it may act as a lender or purchaser of notes and/or residual income units) and securitisations (such as mortgages, finance leases and other types of collateralised vehicles). The maximum exposure to loss is limited to the reported fair value of the underlying securities plus any guaranteed undrawn commitments to the counterparties. At 30 June 2017, the carrying value of asset-backed financing assets was $32.0 million (30 June 2016: $8.4 million) with zero undrawn commitments (30 June 2016: none) and securitisations was $2,347.4 million (30 June 2016: $2,815.9 million) plus $71.8 million undrawn commitments (30 June 2016: $142.1 million).

2 Refer to Note 6 Investment and development property for valuation techniques and key unobservable inputs.

3 Refer Note 7 Special Purpose Vehicles for more information.

Note 19 Fair values of financial assets and liabilities (continued)

Level 3 reconciliation

The following table shows a reconciliation of the movement in the fair value of financial instruments categorised within Level 3 of the fair value hierarchy during the year:

	30 June 2017		30 June 2016	
	Assets $M	Liabilities $M	Assets $M	Liabilities $M
Balance at the beginning of the year	3,033.9	7,430.8	3,125.6	7,107.2
Fair value gains/(losses)	2.6	133.1	26.0	259.8
Acquisitions	1,664.7	2,329.7	1,373.6	2,695.4
Maturities and disposals	(1,759.3)	(3,202.4)	(1,413.7)	(2,631.6)
Transfers (to)/from other categories[1,2]	53.1	-	(77.6)	-
Balance at the end of the year[3]	**2,995.0**	**6,691.2**	**3,033.9**	**7,430.8**
Unrealised gains/(losses) included in the statement of comprehensive income for assets and liabilities held at the statement of financial position date	38.5	(16.1)	68.3	260.1

1 The Group transfers between levels of the fair value hierarchy as at the end of the reporting period during which the transfer has occurred.

2 Transfers to/from other categories are due to changes in the market observability of inputs used in the valuation of financial instruments. There were no transfers between Level 1 and Level 2 during the reporting period.

3 Does not include investment property.

Note 19 Fair values of financial assets and liabilities (continued)

Level 3 sensitivities

The following table shows the sensitivity of Level 3 financial instruments to a reasonable change in alternative assumptions in respect of the non-observable inputs into the fair value calculation:

	Level 3 value[1] $M	Positive impact $M	Negative impact $M	Valuation technique	Reasonable change in non-observable input[2,3]
30 June 2017					
Derivative assets	0.1	0.8	(0.3)	Discounted cash flow	Primarily credit spreads
Fixed income securities	2,085.8	36.0	(32.9)	Discounted cash flow	Primarily credit spreads
Interest bearing financial liabilities	(410.6)	(7.7)	7.9	Discounted cash flow	Primarily credit spreads
Equity, infrastructure, property assets	814.2	33.6	(35.1)	Discounted cash flow, External financial report	Primarily discount rate on cash flow models
Investment contract liabilities	(6,280.6)	4.8	(4.8)	Discounted cash flow	Primarily expense assumptions
Assets attributable to RIU – SPV	94.9	3.1	(3.1)	Discounted cash flow	Primarily prepayment rates
Total Level 3[4]	**(3,696.2)**	**70.6**	**(68.3)**		
30 June 2016					
Fixed income securities	2,008.3	26.7	(43.2)	Discounted cash flow	Primarily credit spreads
Interest bearing financial liabilities	(595.5)	(9.3)	9.6	Discounted cash flow	Primarily credit spreads
Equity, infrastructure, property assets	920.7	49.3	(50.7)	Discounted cash flow, External financial report	Primarily discount rate on cash flow models
Investment contract liabilities	(6,835.2)	3.8	(3.8)	Discounted cash flow	Primarily expense assumptions
Assets attributable to RIU – SPV	104.9	4.2	(4.0)	Discounted cash flow	Primarily prepayment rates
Derivative liabilities	(0.1)	0.2	(0.1)	Discounted cash flow	Primarily credit spreads
Total Level 3[4]	**(4,396.9)**	**74.9**	**(92.2)**		

1 The fair value of the asset or liability would increase/decrease if the credit spread, discount rate or expense assumptions decrease/increase or if the other inputs increase/decrease.
2 Specific asset valuations will vary from asset to asset, as each individual industry profile will determine appropriate valuation inputs to be utilised.
3 The effect of a change to reflect a reasonable possible alternative assumption was calculated by moving the credit band by one tier, adjusting the discount rates by between 50bps – 100bps, credit spreads by 50bps, changing the valuation of the unlisted schemes by 5% and adjusting the expense assumption allocation splits by 10%.
4 Does not include investment property.

Section 6: Group structure

This section provides details and disclosures relating to controlled entities and any acquisitions and/or disposals of businesses in the year. Disclosure on related parties is also provided in this section.

Note 20 Controlled entities

The material controlled entities, based on contribution to the Company's statement of comprehensive income, total assets and total liabilities, are:

Balloon Inflation Linked Bond Trust[3]
Challenger Adelaide Street Trust
Challenger Albert Street Trust
Challenger Australia Listed Property Holding Trust
Challenger Barracks Trust
Challenger Bunbury Trust
Challenger CKT Holding Trust
Challenger Clarence Street Trust
Challenger Diversified Property Trust 1
Challenger Golden Grove Trust
Challenger Index Plus Fund[2,3]
Challenger Life Debt Investments (Europe) Limited (UK)
Challenger Life Fund Property Invts Pty Ltd
Challenger Life IRP Trust
Challenger Life MN Trust
Challenger Millennium Series 2007-1E Trust
Challenger Millennium Series 2013-1 Trust
Challenger Next Hotel Trust
Challenger North Rocks Trust
Challenger UK Terminals Ltd (Jersey)
Challenger Welcome Break Limited
Clashfern Investments (UK) Limited (UK)
CLC Commercial Mortgages Trust
CLC Leveraged Loan Trust
CLS US Holdings,LLC (USA)
Crown Domestic Sovereign Bond Trust[3]
GIR StatePlus Trust[3]
Harris Global Sovereign Bond Trust[3]
Interstar Millennium Series 2005-3E Trust
Interstar Millennium Series 2006-2G Trust
Interstar Millennium Series 2006-3L Trust
Godo Kaisha Kenedix Master Tokumei Kumiai (Japan)[1]
Oaklands Hill Pty Ltd
Offshore Reinsurer (Bermuda) Co Ltd[2]
Godo Kaisha Sub Tokumei Kumiai One (Japan)[1]
Godo Kaisha Sub Tokumei Kumiai Two (Japan)[1]
TLG Unit Trust
US LLC Hldgs Pty Ltd
Waterford County Pty Ltd[1]

Unless otherwise stated, all material entities are incorporated in Australia and 100% owned.

1 Percentage holding is less than 100%.
2 Consolidated in 2017.
3 CLC consolidates the funds due to control over the trust and the existence of a total return swap.

Recognition and measurement

Controlled entities are consolidated from the date on which control is transferred to the Group and cease to be consolidated from the date on which control is transferred out of the Group. The acquisition method of accounting is applied on acquisition or initial consolidation. This method ascribes fair values to the identifiable assets and liabilities acquired. The difference between the net fair value acquired and the fair value of the consideration paid (including the fair value of any pre-existing investment in the entity) is recognised as either goodwill on the statement of financial position or a discount on acquisition through the statement of comprehensive income.

Note 21 Related parties

Controlled entities

The immediate parent entity of the Company is Challenger Life Company Holdings Pty Limited and the ultimate parent entity is Challenger Limited.

Unless an exception applies under relevant legislation, transactions between commonly-controlled entities within the Group (except where otherwise disclosed) are conducted on an arm's length basis under normal commercial terms and conditions. The Group's interests in controlled entities are disclosed in Note 20 Controlled entities

Directors

The Directors and key executives of Challenger Life Company Limited during the financial year were as follows:

Directors	
Peter L Polson	Independent Chair
Brian R Benari	Managing Director and Chief Executive Officer
Graham A Cubbin	Independent Non-Executive Director
Steven Gregg	Independent Non-Executive Director
Jonathan H Grunzweig	Independent Non-Executive Director
Brenda M Shanahan	Independent Non-Executive Director
JoAnne M Stephenson	Independent Non-Executive Director
Leon Zwier	Independent Non-Executive Director
Key executives	
Anthony Bofinger	Chief Financial Officer and Appointed Actuary
Christopher Plater (from 13 February 2017)	Chief Executive, Chief Investment Officer and Principal Executive Officer
Richard Howes (up to 13 February 2017)	Chief Executive
Richard Willis	Chief Risk Officer

From time to time, Directors of the Company or their Director-related entities may purchase insurance products from the Company. These purchases are on the same arm's length terms and conditions as those offered to other employees or customers.

Key management personnel compensation

The key management personnel (KMP) of the Company includes the Directors and those executives who have the authority and responsibility for planning, directing and controlling the activities of the Company, either directly or indirectly. A summary of this compensation is shown in the table below:

Consolidated and parent	30 June 2017 $	30 June 2016 $
KMP compensation		
Short-term benefits	5,674,995	5,489,297
Post-employment benefits	109,373	109,700
Share-based payments	4,393,467	4,475,099
Total	**10,177,834**	**10,074,096**

A KMP of the company may also be considered a KMP of other entities in the wider Challenger Group and receive remuneration for activities spanning those entities. In this situation, an allocation of KMP compensation is made based on an apportionment of each KMP's activities attributable to the Company.

Note 21 Related parties (continued)

Other related parties

During the year, there were transactions between the Group and other companies that are related parties of the Challenger Limited consolidated group. This included the provision of investment management, transaction advisory, accounting and administration and other professional services.

Transactions are conducted on an arm's length basis under normal commercial terms and conditions.

Amounts paid under the above arrangements are reflected in the table below:

	Consolidated		Parent	
	30 June 2017 $M	30 June 2016 $M	30 June 2017 $M	30 June 2016 $M
Accounting and administrative services	86.0	77.3	86.0	77.3
Investment management and advisory fees	42.9	36.6	31.7	31.0
Realised hedge (receipts)/payments[1]	(11.5)	(7.3)	(11.5)	(7.3)

[1] The Company hedges certain foreign exchange and interest rate exposures with transactions with Challenger Treasury Limited. The outstanding balance at 30 June 2017 was $9.9 million (30 June 2016: $24.2 million).

At 30 June 2017, amounts recoverable from related entities were $206.8 million (30 June 2016: $222.0 million) and $214.8 million (30 June 2016: $222.7 million) for the consolidated group and parent respectively, and amounts payable to related entities were $83.1 million (30 June 2016: $7.1 million) and $92.2 million (30 June 2016: $0.4 million) for the consolidated group and parent respectively.

Section 7: Other items

This section provides information that is less significant in understanding the financial performance and position of the Group and the Company perhaps due to lack of movement in the amount or the overall size of balance. Nevertheless, these items assist in understanding the Group or are required under Australian or International Accounting Standards, the *Corporations Act 2001* and/or the *Corporations Regulations*.

Note 22 Goodwill and other intangible assets

Consolidated	30 June 2017 $M	30 June 2016 $M
Goodwill[1]	61.1	61.1
Other intangible assets		
Balance at the beginning of the year	-	13.3
Movements for the year		
- amortisation expense	-	(0.8)
- foreign exchange gain	-	(0.4)
- impairment	-	(12.1)
Balance at the end of the year	**-**	**-**

[1] All goodwill is considered non-current. The parent has $46.8 million of goodwill (30 June 2016: $46.8 million).

Recognition and measurement

Goodwill

Goodwill acquired in a business combination is initially measured at cost, being the excess of the fair value of the consideration for the business combination over the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses.

For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to the Group's cash-generating unit.

The cash-generating unit represents the lowest level within the Group at which the goodwill is monitored for internal management purposes. Impairment is determined by assessing the recoverable amount of the cash-generating unit to which the goodwill relates. When the recoverable amount of the cash-generating unit is less than the carrying amount, an impairment loss is recognised and allocated first to reduce the carrying amount of any goodwill allocated to that cash-generating unit, then to reduce the carrying amount of the other assets in the unit on a pro rata basis. Impairment losses recognised for goodwill are not subsequently reversed.

When goodwill forms part of a cash-generating unit and an operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this manner is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained.

Other intangible assets

Other intangible assets acquired are recorded at cost less accumulated amortisation and impairment losses. The cost of an intangible asset acquired in a business combination is its fair value as at the date of acquisition. Amortisation is calculated based on the timing of projected cash flows over the estimated useful lives.

Leases, where the lessor retains substantially all the risk and benefits of ownership, are classified as operating leases. Initial direct costs incurred in negotiating an operating lease are added to the carrying amount of the leased asset and recognised as an expense over the term of the lease on the same basis as the lease income. Incentives received on entering into operating leases are recognised as liabilities and are amortised over the life of the lease.

Where the Group acquires, as part of a business combination, an operating lease over land, the fair value of this lease is recognised separately from goodwill. This intangible asset is recorded at fair value less accumulated amortisation. Amortisation is calculated using the straight line method over the effective life of the lease (in this case, 25 years).

Goodwill recoverable amounts

The Group assesses whether goodwill is impaired at least annually in accordance with its accounting policy. These value in use calculations involve an estimation of the recoverable amount of the cash-generating unit to which the goodwill is allocated using cash flow projections based on financial forecasts approved by senior management which cover an appropriate time horizon.

Note 22 Goodwill and other intangible assets (continued)

Recognition and measurement (continued)

The discount rates are based on the Group's weighted average cost of capital.

The relevant assumptions in deriving the value of cash-generating unit are as follows:

- bond rate, taken as the yield on a government bond at the beginning of the budgeted year;
- budgeted gross margins, being the average gross margins achieved in the year ended immediately preceding the budgeted year, adjusted for the expected impact of competitive pressure on margins and expected efficiency improvements; and
- growth rates, which are consistent with long-term trends in the industry segments in which the businesses operate.

The derived values for the cash-generating unit are in excess of the carrying values of goodwill.

Useful lives of intangible assets used in the calculation of the amortisation expense are examined on an annual basis and, where applicable, adjustments are made on a prospective basis.

Impairment testing of goodwill

The following represent the carrying amounts of goodwill:

CGU	30 June 2017 $M	30 June 2016 $M	30 June 2017 Discount rate %	30 June 2016 Discount rate %	Cash flow horizon (years)
CLC	61.1	61.1	10.5	10.5	5

The cash flow projections derived a value for the Group that was in excess of the carrying value of goodwill. Consequently, no impairment of goodwill was recorded.

Sensitivity to change in assumptions

Management is of the view that reasonably possible changes in the key assumptions, such as an increase in the discount rate by 1%, would not cause the respective recoverable amounts for the Group to fall below the carrying amounts as at 30 June 2017.

Note 23 Contingent liabilities, contingent assets and credit commitments

Warranties

Over the course of its corporate activity, the Group has given, as a vendor of assets including real estate properties, warranties to purchasers on several agreements that are outstanding at 30 June 2017. Other than noted below, at the date of this report no material claims against these warranties have been received by the Group.

Contingent future commitments

The Group has made capital commitments to external counterparties for future investment opportunities such as development or investment purchases. As at 30 June 2017, there are potential future commitments totalling $301.3 million (30 June 2016: $242.4 million) in relation to these opportunities.

Subsidiary guarantees

CLC has provided a guarantee to a third party regarding the performance of its subsidiary in respect of certain reinsurance arrangements.

Other information

In the normal course of business, the Group enters into various contracts that could give rise to contingent liabilities in relation to performance obligations under those contracts. The information usually required by Australian Accounting Standards is not disclosed for a number of such contracts on the grounds that it may seriously prejudice the outcome of the claims. At the date of this report, significant uncertainty exists regarding any potential liability under these claims.

Operating leases

Group as lessee

The Group has entered into a commercial operating lease for the rental of a property that would not be available for purchase. The Group then rents the site to the external parties as an active operation. The current lease expires in 2033. During the year, a contract was exchanged to assign the lease to another party.

The Group also has an operating lease (leasehold) over an industrial site with a subsidiary of the Group operating a business from the site. The current leasehold expires in 2032.

Group as lessor

Investment properties owned by the Group are leased to third parties under operating leases. Lease terms vary between tenants and some leases include percentage rental payments based on sales volume.

Note 23 Contingent liabilities, contingent assets and credit commitments (continued)

Contracted capital expenditure commitments

These represent amounts payable in relation to capital expenditure commitments contracted for at the reporting date but not recognised as liabilities. They primarily relate to the investment property portfolio and property plant and equipment.

Other contracted commitments

This represents amounts payable in relation to acquisition of investment properties that have exchanged pre balance date and will settle subsequent to the end of the financial year.

Analysis of credit commitments	30 June 2017 $M	30 June 2016 $M
Non-cancellable operating leases – Group as lessee		
Amounts due in less than one year	1.8	4.4
Amounts due between one and two years	-	4.5
Amounts due between two and five years	-	14.3
Amounts due in greater than five years	0.1	65.0
Total operating leases – Group as lessee	**1.9**	**88.2**
Contracted capital expenditure		
Amounts due in less than one year	182.8	65.3
Amounts due between one and two years	173.4	4.0
Amounts due between two and five years	5.8	5.2
Amounts due in greater than five years	-	2.6
Total capital expenditure commitments	**362.0**	**77.1**
Non-cancellable operating leases – Group as lessor		
Amounts due in less than one year	(218.1)	(237.6)
Amounts due between one and two years	(200.1)	(209.3)
Amounts due between two and five years	(457.9)	(471.3)
Amounts due in greater than five years	(293.2)	(318.2)
Total operating leases – Group as lessor	**(1,169.3)**	**(1,236.4)**
Other contracted commitments		
Amounts due in less than one year	2.0	2.0
Total other contracted commitments	**2.0**	**2.0**
Net commitments	**(803.4)**	**(1,069.1)**

Note 24 Statutory fund information

Life insurance funds

On 7 March 2017, CLC established a new statutory fund, Statutory Fund No. 4, and transferred all policy liabilities reinsured from Mitsui Sumitomo Primary from Statutory Fund No. 2 with effect from 3 April 2017.

New business from Mitsui Sumitomo Primary with a commencement date on or after 3 April 2017 has been written directly into Statutory Fund No. 4 with accompanying assets purchased directly into Statutory Fund No. 4.

The types of life contracts written within each statutory fund of the company are as follows:

Statutory Fund	Type of business	Major products	Type of contract
1	Unit-linked superannuation business	Capital guaranteed bonds[1]	Investment contract
		Performance annuity bonds[1]	Insurance/investment contract[2]
2	Non-linked superannuation business	Fixed-rate annuity	Investment contract
		Lifetime annuity	Insurance contract
		Allocated pension	Investment contract
		Personal super	Investment contract
		Wholesale longevity	Insurance contract
		Wholesale mortality and morbidity	Insurance contract
3	Unit-linked superannuation business	Investment-linked bonds	Investment contract
		Investment-linked allocated pensions	Investment contract
	Unit-linked ordinary business	Investment-linked bonds	Investment contract
4	Non-linked superannuation business	Fixed-rate annuity	Investment contract[3]
		Lifetime annuity	Insurance contract

[1] These products are non-investment linked per the Life Act definitions
[2] Performance annuity bonds have a portion of life insurance risk being a life time option component
[3] On consolidation this product is considered an insurance contract

Note 24 Statutory fund information (continued)

Disaggregated information by statutory fund

Statement of comprehensive income	Statutory Fund No.1 $M	Statutory Fund No.2 $M	Statutory Fund No.3 $M	Statutory Fund No.4 $M	Statutory Fund Total $M	Shareholder Fund $M	Total $M
2017							
Revenue	0.1	1,689.2	0.1	(3.2)	1,686.2	114.7	1,800.9
Expenses	-	(1,074.7)	-	(13.1)	(1,087.8)	(3.0)	(1,090.8)
Finance costs	-	(101.9)	-	-	(101.9)	(34.0)	(135.9)
Profit before tax	**0.1**	**512.6**	**0.1**	**(16.3)**	**496.5**	**77.7**	**574.2**
Income tax expense	-	(110.2)	-	4.9	(105.3)	(23.3)	(128.6)
Profit for the year	**0.1**	**402.4**	**0.1**	**(11.4)**	**391.2**	**54.4**	**445.6**
Profit attributable to non-controlling interest	-	(0.4)	-	-	(0.4)	-	(0.4)
Profit attributable to equity holders	**0.1**	**402.0**	**0.1**	**(11.4)**	**390.8**	**54.4**	**445.2**
2016							
Revenue	0.2	1,479.4	0.2	-	1,479.8	122.0	1,601.8
Expenses	(0.1)	(938.7)	(0.1)	-	(938.9)	(3.0)	(941.9)
Finance costs	-	(124.0)	-	-	(124.0)	(85.6)	(209.6)
Profit before tax	**0.1**	**416.7**	**0.1**	**-**	**416.9**	**33.4**	**450.3**
Income tax expense	-	(100.4)	-	-	(100.4)	(10.0)	(110.4)
Profit for the year	**0.1**	**316.3**	**0.1**	**-**	**316.5**	**23.4**	**339.9**
Profit attributable to non-controlling interest	-	1.5	-	-	1.5	-	1.5
Profit attributable to equity holders	**0.1**	**314.8**	**0.1**	**-**	**315.0**	**23.4**	**338.4**

Abbreviated statement of financial position	Statutory Fund No.1 $M	Statutory Fund No.2 $M	Statutory Fund No.3 $M	Statutory Fund No.4 $M	Statutory Fund Total $M	Shareholder Fund $M	Total $M
30 June 2017							
Cash and cash equivalents	2.8	481.5	2.3	35.1	521.7	31.7	553.4
Investment assets	3.5	15,694.6	3.3	669.5	16,370.9	3,301.0	19,671.9
Other assets	0.2	2,076.9	(0.5)	9.8	2,086.4	234.7	2,321.1
Total assets	**6.5**	**18,253.0**	**5.1**	**714.4**	**18,979.0**	**3,567.4**	**22,546.4**
Life contract liabilities	2.8	9,746.6	3.0	569.8	10,322.2	-	10,322.2
Other liabilities	-	6,039.4	-	-	6,039.4	2,834.1	8,873.5
Total liabilities	**2.8**	**15,786.0**	**3.0**	**569.8**	**16,361.6**	**2,834.1**	**19,195.7**
Net assets	**3.7**	**2,467.0**	**2.1**	**144.6**	**2,617.4**	**733.3**	**3,350.7**
Contributed equity	-	-	-	-	-	2,001.5	2,001.5
Reserves	1.6	396.5	0.8	156.0	554.9	(414.1)	140.8
Retained earnings	2.1	2,056.9	1.3	(11.4)	2,048.9	(854.1)	1,194.8
Non-controlling interests	-	13.6	-	-	13.6	-	13.6
Total equity	**3.7**	**2,467.0**	**2.1**	**144.6**	**2,617.4**	**733.3**	**3,350.7**

Note 24 Statutory fund information (continued)

Abbreviated statement of financial position

30 June 2016	Statutory Fund No.1 $M	Statutory Fund No.2 $M	Statutory Fund No.3 $M	Statutory Fund No.4 $M	Statutory Fund Total $M	Shareholder Fund $M	Total $M
Cash and cash equivalents	3.2	568.2	2.1	-	573.5	14.8	588.3
Investment assets	3.5	15,458.9	3.6	-	15,466.0	2,038.0	17,504.0
Other assets	0.3	2,372.5	(0.4)	-	2,372.4	77.2	2,449.6
Total assets	**7.0**	**18,399.6**	**5.3**	**-**	**18,411.9**	**2,130.0**	**20,541.9**
Life contract liabilities	3.3	9,551.9	3.3	-	9,558.5	-	9,558.5
Other liabilities	0.1	6,296.5	-	-	6,296.6	1,973.1	8,269.7
Total liabilities	**3.4**	**15,848.4**	**3.3**	**-**	**15,855.1**	**1,973.1**	**17,828.2**
Net assets	**3.6**	**2,551.2**	**2.0**	**-**	**2,556.8**	**156.9**	**2,713.7**
Contributed equity	-	(0.1)	-	-	(0.1)	1,541.6	1,541.5
Reserves	1.6	892.8	0.8	-	895.2	(754.2)	141.0
Retained earnings	2.0	1,654.9	1.2	-	1,658.1	(630.5)	1,027.6
Non-controlling interests	-	3.6	-	-	3.6	-	3.6
Total equity	**3.6**	**2,551.2**	**2.0**	**-**	**2,556.8**	**156.9**	**2,713.7**

Capital adequacy

30 June 2017	Statutory Fund No.1 $M	Statutory Fund No.2 $M	Statutory Fund No.3 $M	Statutory Fund No.4 $M	Statutory Fund Total $M	Shareholder Fund $M	Total $M
Net assets[1]	3.7	2,453.4	2.1	144.6	2,603.8	733.3	3,337.1
Regulatory adjustments	-	(310.1)	-	(5.6)	(315.7)	(47.4)	(363.1)
Tier 1 regulatory capital	**3.7**	**2,143.3**	**2.1**	**139.0**	**2,288.1**	**685.9**	**2,974.0**
Tier 2 capital[2]	-	395.4	-	-	395.4	-	395.4
Capital base	**3.7**	**2,538.7**	**2.1**	**139.0**	**2,683.5**	**685.9**	**3,369.4**
Prescribed capital amounts components							
Insurance risk charge	0.3	155.9	-	1.2	157.4	0.1	157.5
Asset risk charge	0.3	1,717.3	0.1	26.2	1,743.9	123.8	1,867.7
Operational risk charge	-	36.7	-	2.0	38.7	-	38.7
Default stress	-	14.7	-	-	14.7	0.1	14.8
Aggregation benefit	(0.1)	(118.1)	-	(0.9)	(119.1)	(0.1)	(119.2)
Combined stress scenario adjustment	-	184.6	-	-	184.6	-	184.6
Prescribed capital Amount	**0.5**	**1,991.1**	**0.1**	**28.5**	**2,020.2**	**123.9**	**2,144.1**
Capital adequacy multiple	**7.4**	**1.3**	**21.0**	**4.9**	**1.3**	**5.5**	**1.6**

Note 24 Statutory fund information (continued)

Capital adequacy 30 June 2016	Statutory Fund No.1 $M	Statutory Fund No.2 $M	Statutory Fund No.3 $M	Statutory Fund No.4 $M	Statutory Fund Total $M	Shareholder Fund $M	Total $M
Net assets[1]	3.6	2,547.6	2.0	-	2,553.2	156.9	2,710.1
Regulatory adjustments	-	(316.2)	-	-	(316.2)	(45.3)	(361.5)
Tier 1 regulatory capital	**3.6**	**2,231.4**	**2.0**	**-**	**2,237.0**	**111.6**	**2,348.6**
Tier 2 capital[2]	-	445.5	-	-	445.5	-	445.5
Capital base	**3.6**	**2,676.9**	**2.0**	**-**	**2,682.5**	**111.6**	**2,794.1**
Prescribed capital amounts components							
Insurance risk charge	0.3	167.9	-	-	168.2	0.1	168.3
Asset risk charge	0.4	1,412.6	0.1	-	1,413.1	64.0	1,477.1
Operational risk charge	-	28.7	-	-	28.7	-	28.7
Default stress	-	14.6	-	-	14.6	0.1	14.7
Aggregation benefit	(0.2)	(125.1)	-	-	(125.3)	-	(125.3)
Combined stress scenario adjustment	-	220.0	-	-	220.0	0.2	220.2
Prescribed capital amount	**0.5**	**1,718.7**	**0.1**	**-**	**1,719.3**	**64.4**	**1,783.7**
Capital adequacy multiple	**7.2**	**1.6**	**20.0**	**-**	**1.6**	**1.7**	**1.6**

1 Net assets includes additional tier 1 capital.

2 Differs from the $393.6 million (30 June 2016: $567.7 million) disclosed in Note 14 Interest bearing financial liabilities due to $1.8 million (30 June 2016: $2.3 million) accrued interest and nil (30 June 2016: $133.5 million) inadmissible Tier 2 regulatory capital.

Disaggregated information by linked/non-linked

As stated above, the Company's non-linked business is contained in Statutory Funds No.1, No.2 and No.4 and the linked business in Statutory Fund No.3.

Note 25 Remuneration of auditors

Auditors' remuneration in respect of the entities within the Group is incurred and paid by Challenger Group Services Pty Limited, a subsidiary of the ultimate parent entity, Challenger Limited.

Note 26 Subsequent events

CLC's business is growing strongly, with new distribution and product initiatives commencing in 2018. On 14 August 2017, the Board of Challenger Limited (CLC's ultimate parent entity) approved the placement of $500 million of ordinary shares to MS&AD Insurance Group Holdings Inc. The proceeds from the placement will be used to increase CLC's Common Equity Tier 1 capital.

At the date of this report and other than those described above, no matter or circumstance has arisen that has affected, or may significantly affect, Challenger's operations, the results of those operations or the Group's state of affairs in future financial years.

Directors' declaration

In accordance with a resolution of the Directors of Challenger Life Company Limited, we declare that, in the opinion of the Directors:

a. the financial statements and notes of Challenger Life Company Limited and its controlled entities (the Group) are in accordance with the *Corporations Act 2001*, including:

   i. giving a true and fair view of the Group's financial position as at 30 June 2017 and of its performance for the year ended on that date; and

   ii. complying with Australian Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Regulations 2001*;

b. the financial statements and notes of the Group also comply with International Financial Reporting Standards as disclosed in Section 1(i) Basis of preparation and statement of compliance to the financial statements;

c. there are reasonable grounds to believe that the Group will be able to pay its debts as and when they become due and payable; and

d. this declaration has been made after receiving the declarations required to be made to the Directors in accordance with section 295A of the *Corporations Act 2001* for the financial year ended 30 June 2017.

On behalf of the Board

G A Cubbin
Director

Sydney
14 August 2017

B R Benari
Director

Sydney
14 August 2017

Building a better working world

Ernst & Young
200 George Street
Sydney NSW 2000 Australia
GPO Box 2646 Sydney NSW 2001

Tel: +61 2 9248 5555
Fax: +61 2 9248 5959
ey.com/au

Independent auditor's report

Independent auditor's report to the shareholders of Challenger Life Company Limited

Opinion

We have audited the financial report of Challenger Life Company Limited (the Company) and its subsidiaries (collectively the Group), which comprises the consolidated statements of financial position as at 30 June 2017, the consolidated statements of comprehensive income, consolidated statements of changes in equity and consolidated statements of cash flows for the year then ended, notes to the financial statements, including a summary of significant accounting policies, and the directors' declaration.

In our opinion, the accompanying financial report of the Group is in accordance with the *Corporations Act 2001*, including:

a) giving a true and fair view of the consolidated financial position of the Group as at 30 June 2017 and of its consolidated financial performance for the year ended on that date; and

b) complying with Australian Accounting Standards and the *Corporations Regulations 2001*.

Basis for Opinion

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Report section of our report. We are independent of the Group in accordance with the auditor independence requirements of the Corporations Act 2001 and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 Code of Ethics for Professional Accountants (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

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

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial report of the current year. These matters were addressed in the context of our audit of the financial report as a whole, and in forming our opinion thereon, but we do not provide a separate opinion on these matters. For each matter below, our description of how our audit addressed the matter is provided in that context.

We have fulfilled the responsibilities described in the Auditor's Responsibilities for the Audit of the Financial Report section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the financial report. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying financial report.

1 Valuation of Life Contract Liabilities

30 June 2017 Financial report reference: **Note 8**

Why significant	How our audit addressed the key audit matter
A provision is recognised for future claims associated with sold insurance policies. The valuation methodology adopted by the Group involves complex and subjective judgements about future events. Key assumptions involved in the valuation of the policy liabilities include: • Discount rates • Inflation • Future claims administration expenses • Mortality and redemptions These assumptions are incorporated into an internal model, which is used to generate the valuation. This was a key audit matter due to the size of the balance (30 June 2017: $10,322.2 million), and the degree of judgement and estimation uncertainty associated with the valuation.	Our audit of the valuation of the life contract liabilities involved an assessment of the design and operating effectiveness of relevant controls over data inputs into the valuation process. This also extended to the involvement of our IT specialists testing the completeness and accuracy of data extracted from the underlying administration system into the valuation process. We involved our actuarial specialists to assist in assessing the appropriateness of the valuation methodology, key assumptions and models deriving the life contract liabilities. In doing so, we: • Evaluated the governance process in place to determine the methodology and assumptions. • Assessed the results of the experience investigations carried out by the Group to determine whether they supported the assumptions used by the Group. • Assessed the movements in modelled profit margins and best estimate liabilities for insurance risk transactions. • Performed a recalculation of a sample of the life contract liability valuations. We assessed the adequacy and completeness of policy liability disclosures against the requirements of Australian Accounting Standards – AASB 1038 *Life Insurance Contract Liabilities.*

2 Valuation Level 3 Financial Assets

30 June 2017 Financial report reference: **Note 19**

Why significant	How our audit addressed the key audit matter
The Group holds a portfolio of financial assets for which an observable market value is not readily available. These assets are classified as Level 3 within the fair value hierarchy of the financial report and include: • Unlisted debt instruments, e.g. residential mortgage and asset backed securities • Infrastructure assets • Unlisted indirect property holdings • Mortgage loans • Unlisted equities • Unlisted unit trusts • Direct properties Level 3 assets require judgement to be applied in determining their fair value as the valuation inputs for these assets are not based on observable market data. In determining the fair value of these assets the Group utilises a range of methodologies, models and assumptions. Accordingly there are a number of risks associated with the valuation and modelling methodologies adopted. This was a key audit matter due to the size of the balance (30 June 2017: $6,498.5 million), and the degree of judgement and estimation uncertainty associated with the valuation.	For the Level 3 assets we assessed both the methodology and assumptions in the calculation of the year end value as well as assessed the design and operating effectiveness of governance controls the Group has in place to monitor these investments. In obtaining sufficient audit evidence, we: • Checked the mathematical accuracy of the valuation models and consistency with the Group's documented methodology and assumptions. • Involved our valuation specialists to assess the appropriateness of valuation and modelling methodologies and assessed the key assumptions used in the year end valuations, specifically the discount rate and terminal value. • Assessed the independence and competence of the external property valuation experts used by the Group, and assessed the internal property models and appropriateness of the methodologies and assumptions used in the year end property valuations. • Involved our credit and valuation specialists to assess the adequacy of the internal credit rating process. • Obtained valuation statements provided by external investment managers in respect of controlled unit trusts and hedge funds. We assessed the valuations of investments as provided by external investment managers, including an assessment of the reliability of the information provided by the investment manager, such as key assumptions, multiples and discounts applied.

3 Valuation of Goodwill

30 June 2017 Financial report reference: **Note 22**

Why significant	How our audit addressed the key audit matter
Goodwill has been recognised as a result of the Group's historical acquisitions, representing the excess of the purchase consideration over the fair value of assets and liabilities acquired. On acquisition this goodwill has been allocated to the applicable Cash Generating Unit's (CGUs). An impairment assessment is performed at each reporting period, comparing the carrying value of the CGU with its recoverable amount. The recoverable amount of each CGU is determined using a value in use calculation. This calculation incorporates a range of assumptions, including future cash flows, discount rates and terminal growth rates. This was a key audit matter due to the size of Goodwill held on the consolidated statement of financial position (30 June 2017: $61.1 million), and the degree of judgement and estimation uncertainty associated with the impairment assessment.	Our audit of the impairment assessment of the CGU required valuation expertise to assist in the testing of the underlying model and key assumptions. Accordingly we involved our valuation specialists and: • Assessed the valuation methodology and appropriateness of the impairment model used to calculate the recoverable amount of the CGU. • Agreed the projected cash flows used in the impairment models to the Board approved Challenger Life Company Limited five year plan. We compared the Group's implied growth rate assumption to comparable companies for reasonableness. • Assessed the methodology and assumptions used in the calculation of the discount rate, including comparison of the rate to market benchmarks. • Assessed the methodology and assumptions used in the calculation of the terminal growth rate. • Assessed the mathematical accuracy of the impairment model. • Assessed the Group's sensitivity analysis and evaluated whether any reasonable foreseeable change in assumptions could lead to an impairment. We assessed the Group's determination of the CGU to which goodwill is allocated and the adequacy of the disclosures in the financial report for compliance with applicable Australian Accounting Standards.

Information Other than the Financial Report and Auditor's Report Thereon

The Directors are responsible for the other information. The other information comprises the information included in the Company's 2017 Annual Report, but does not include the financial report and our auditor's report thereon.

Our opinion on the financial report does not cover the other information and accordingly we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial report, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial report or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the Directors for the Financial Report

The Directors of the Company are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the Directors determine is necessary to enable the preparation of the financial report that gives a true and fair view and is free from material misstatement, whether due to fraud or error.

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

Auditor's Responsibilities for the Audit of the Financial Report

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

As part of an audit in accordance with the Australian Auditing Standards, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial report, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Directors.
- Conclude on the appropriateness of the Directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial report or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial report, including the disclosures, and whether the financial report represents the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the financial report. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

We communicate with the Directors regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the Directors with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated to the Directors, we determine those matters that were of most significance in the audit of the financial report of the current year and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Ernst & Young

S J Ferguson
Partner

Sydney
14 August 2017

L Burns
Partner

Sydney
14 August 2017

Directory

Principal place of business and registered office in Australia

5 Martin Place

Sydney NSW 2000

Telephone: 02 9994 7000

Investor services: 13 35 66

Facsimile: 02 9994 7777

Website: www.challenger.com.au

Directors

Peter Polson (Chair)

Brian Benari (Managing Director and Chief Executive Officer)

Graham Cubbin

Steven Gregg

Jonathan Grunzweig

Brenda Shanahan

JoAnne Stephenson

Leon Zwier

Company secretaries

Michael Vardanega

Andrew Brown

Auditor

Ernst & Young

200 George Street

Sydney NSW 2000