

2021 Annual Report

Challenger Life Company Limited

Providing our
customers with
financial security
for a better
retirement



challenger.com.au

Challenger Life Company Limited ACN 072 486 938

challenger 

Contents

Directors' report	1
Financial statements	
Statements of comprehensive income	5
Statements of financial position	6
Statements of changes in equity	7
Statements of cash flows	9
Notes to the financial statements	10
Signed reports	
Directors' declaration	60
Independent auditor's report	61
Additional information	63

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 2021.

1. Directors

The names and details of the Directors of the Company holding office during the financial year ended 30 June 2021 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 Polson	Independent Chair
Richard Howes	Managing Director and Chief Executive Officer
John M Green	Independent Non-executive Director
Steven Gregg	Independent Non-executive Director
Heather Smith (appointed 20 January 2021)	Independent Non-executive Director
JoAnne Stephenson	Independent Non-executive Director
Duncan West	Independent Non-executive Director
Melanie Willis	Independent Non-executive Director

2. Company Secretary

Aron Rattew is a qualified solicitor and was appointed to the position of Acting General Counsel on 20 January 2021.

Linda Matthews, Head of Company Secretariat, is a qualified solicitor with over 18 years' experience and was appointed to the position of Company Secretary on 1 January 2021.

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.

The Company has continued to progress its strategic relationship with MS&AD Insurance Group Holdings Inc. (MS&AD) to support the Company's strategy for growth in Australia and internationally.

There were no other significant changes in the state of affairs of the Company that occurred during the financial year.

4. Operating and financial review

The consolidated statutory profit after tax for the year attributable to the equity holders was \$627.7 million compared to a \$336.6 million loss in the prior year.

5. Capital management

In July 2020, CLC issued \$30.0 million of new fully paid ordinary shares as Common Equity Tier 1 capital.

In November 2020, CLC completed a new hybrid equity notes issue, raising \$385.0 million of funding, of which \$297.5 million was used to repurchase existing hybrid equity notes. The issue features similar structural characteristics to the existing notes. In May 2021, a further \$19.7 million of existing hybrid equity notes were repurchased.

The notes issuance was approved by the Australian Prudential Regulation Authority (APRA) as qualifying as Additional Tier 1 capital of CLC and are classified as equity.

6. Dividends

On 5 February 2021, the Directors of the Company declared a dividend on ordinary shares of \$170.0 million. The dividend was subsequently paid on 28 February 2021.

7. Likely developments and expected results

The Group intends to continue with its current strategy of providing its customers with financial security for a better 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

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 that is fraudulent, dishonest, criminal, malicious or a reckless act, error or omission.

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 continues to be a signatory to the United Nations Principles for Responsible Investment (PRI).

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. Authorisation

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



P Polson
Independent Chair
Sydney
9 August 2021



R Howes
Director
Sydney
9 August 2021

15. Auditor's independence declaration

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



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

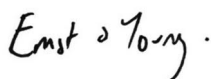
Tel: +61 2 9248 5555
Fax: +61 2 9248 5959
ey.com/au

Auditor's Independence Declaration to the Directors of Challenger Life Company Limited

As lead auditor for the audit of the financial report of Challenger Life Company Limited for the financial year ended 30 June 2021, 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



Graeme McKenzie
Partner
9 August 2021

A member firm of Ernst & Young Global Limited

Liability limited by a scheme approved under Professional Standards Legislation

Contents – Financial report

Financial statements

Statements of comprehensive income	5
Statements of financial position	6
Statements of changes in equity	7
Statements of cash flows	9

Notes to the financial statements

Section 1: Basis of preparation and overarching significant accounting policies	10
Section 2: Key numbers	14
Note 1 Revenue	14
Note 2 Expenses	15
Note 3 Segment information	16
Note 4 Income tax	18
Section 3: Operating assets and liabilities	21
Note 5 Financial assets – fair value through profit and loss	21
Note 6 Investment and development property	22
Note 7 Special Purpose Vehicles	27
Note 8 Life contract liabilities	28
Note 9 External unit holders' liabilities	32
Note 10 Derivative financial instruments	33
Note 11 Collateral arrangements	35
Note 12 Notes to the statements of cash flows	35
Section 4: Capital structure and financing costs	36
Note 13 Contributed equity	36
Note 14 Interest bearing financial liabilities	38
Note 15 Reserves and retained earnings	40
Note 16 Finance costs	41
Note 17 Dividends paid and proposed	41
Section 5: Risk management	42
Note 18 Financial risk management	42
Note 19 Fair values of financial assets and liabilities	47
Section 6: Group structure	50
Note 20 Controlled entities	50
Note 21 Related parties	51
Section 7: Other items	53
Note 22 Goodwill	53
Note 23 Contingent liabilities, contingent assets and credit commitments	54
Note 24 Statutory fund information	55
Note 25 Remuneration of auditors	59
Note 26 Subsequent events	59

Signed reports

Directors' declaration	60
Independent auditor's report	61

Additional information 63

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

Statements of comprehensive income

		Consolidated		Parent	
		2021	2020	2021	2020
For the year ended 30 June	Note	\$m	\$m	\$m	\$m
Revenue	1	2,564.4	936.6	1,837.1	534.1
Expenses	2	(1,390.1)	(1,262.5)	(966.6)	(897.6)
Finance costs	16	(292.3)	(172.7)	(17.7)	(58.4)
Profit/(loss) before income tax		882.0	(498.6)	852.8	(421.9)
Income tax (expense)/benefit	4	(253.0)	157.6	(229.2)	85.0
Profit/(loss) for the year after income tax		629.0	(341.0)	623.6	(336.9)
Profit/(loss) attributable to shareholders of Challenger Life Company Limited		627.7	(336.6)	623.6	(336.9)
Profit/(loss) attributable to non-controlling interests		1.3	(4.4)	—	—
Profit/(loss) for the year after income tax		629.0	(341.0)	623.6	(336.9)
Other comprehensive (loss)/income					
Items that may be reclassified to profit and loss, net of tax					
Translation of foreign entities	15	(49.4)	1.7	—	—
Hedge of net investment in foreign entities	15	46.8	0.5	—	—
Cash flow hedges – SPV ¹	15	(0.5)	—	—	—
Other comprehensive (loss)/income for the year		(3.1)	2.2	—	—
Total comprehensive income/(loss) for the year after tax		625.9	(338.8)	623.6	(336.9)
Comprehensive income/(loss) attributable to shareholders of Challenger Life Company Limited		624.6	(334.4)	623.6	(336.9)
Comprehensive income/(loss) attributable to non-controlling interests		1.3	(4.4)	—	—
Total comprehensive income/(loss) for the year after tax		625.9	(338.8)	623.6	(336.9)

¹ SPV = Special Purpose Vehicles.

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

Statements of financial position

		Consolidated		Parent	
As at 30 June	Note	2021 \$m	2020 \$m	2021 \$m	2020 \$m
Assets					
Cash and cash equivalents	12	715.6	457.9	177.2	99.5
Cash and cash equivalents – SPV	7	60.8	58.0	—	—
Receivables		989.2	792.6	608.8	1,007.7
Derivative assets	10	730.3	1,084.6	365.0	552.8
Financial assets – fair value through profit and loss	5	22,164.0	20,833.3	22,944.8	21,818.1
Investment and development property – held for sale	6	396.0	—	—	—
Investment and development property	6	3,389.7	3,685.9	—	—
Mortgage assets – SPV	7	597.5	702.4	—	—
Finance leases		26.8	31.7	—	—
Deferred tax assets	4	0.8	1.6	2.2	2.9
Right-of-use lease assets		0.5	0.7	—	—
Other assets		35.3	41.0	0.3	1.0
Other intangibles		1.5	1.6	—	—
Goodwill	22	69.4	69.4	46.8	46.8
Total assets of shareholders of Challenger Life Company Limited and non-controlling interests		29,177.4	27,760.7	24,145.1	23,528.8
Liabilities					
Payables		1,693.4	1,544.3	930.4	1,183.8
Payables – SPV		27.7	28.4	—	—
Current tax liability		2.3	0.6	—	—
Derivative liabilities	10	423.4	610.2	—	—
Interest bearing financial liabilities	14	5,086.0	6,427.5	4,515.6	5,789.3
Interest bearing financial liabilities – SPV	7	379.7	432.7	—	—
External unit holders' liabilities	9	3,632.2	2,415.8	—	—
Lease liabilities		0.5	0.7	—	—
Provisions		4.5	3.2	—	5.5
Deferred tax liabilities	4	116.7	91.8	131.5	125.4
Life contract liabilities	8	13,669.9	12,581.2	14,440.7	12,813.0
Total liabilities of shareholders of Challenger Life Company Limited and non-controlling interests		25,036.3	24,136.4	20,018.2	19,917.0
Net assets of shareholders of Challenger Life Company Limited and non-controlling interests		4,141.1	3,624.3	4,126.9	3,611.8
Equity					
Contributed equity	13	2,869.3	2,771.5	2,869.3	2,771.5
Reserves	15	136.3	139.4	137.8	137.8
Retained earnings	15	1,123.0	701.6	1,119.8	702.5
Total equity of shareholders of Challenger Life Company Limited		4,128.6	3,612.5	4,126.9	3,611.8
Non-controlling interests		12.5	11.8	—	—
Total equity of shareholders of Challenger Life Company Limited and non-controlling interests		4,141.1	3,624.3	4,126.9	3,611.8

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

Statements of changes in equity

Attributable to shareholders of Challenger Life Company Limited

Consolidated		Contributed equity	Cash flow hedge reserve – SPV	Foreign currency translation reserve	Adjusted controlling interest reserve	Other reserve	Retained earnings	Total share-holder equity	Non - controlling interests	Total equity
For the year ended 30 June 2020	Note	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Balance at 1 July 2019		2,501.5	0.1	(0.9)	7.8	132.3	1,324.8	3,965.6	31.3	3,996.9
Loss for the year	15	—	—	—	—	—	(336.6)	(336.6)	(4.4)	(341.0)
Other comprehensive income for the year		—	—	2.2	—	—	—	2.2	—	2.2
Total comprehensive (loss)/income for the year		—	—	2.2	—	—	(336.6)	(334.4)	(4.4)	(338.8)
Other equity movements										
Changes in controlling interest reserve		—	—	—	(2.1)	—	—	(2.1)	—	(2.1)
Issued capital	13	270.0	—	—	—	—	—	270.0	—	270.0
Dividends paid	17	—	—	—	—	—	(286.6)	(286.6)	—	(286.6)
Non-controlling interests movements		—	—	—	—	—	—	—	(15.1)	(15.1)
Balance at 30 June 2020 and 1 July 2020		2,771.5	0.1	1.3	5.7	132.3	701.6	3,612.5	11.8	3,624.3
For the year ended 30 June 2021										
Profit for the year	15	—	—	—	—	—	627.7	627.7	1.3	629.0
Other comprehensive loss for the year		—	(0.5)	(2.6)	—	—	—	(3.1)	—	(3.1)
Total comprehensive (loss)/income for the year		—	(0.5)	(2.6)	—	—	627.7	624.6	1.3	625.9
Other equity movements										
Issued capital and equity hybrid notes	13	97.8	—	—	—	—	—	97.8	—	97.8
Dividends paid	17	—	—	—	—	—	(206.3)	(206.3)	—	(206.3)
Non-controlling interests movements		—	—	—	—	—	—	—	(0.6)	(0.6)
Balance at 30 June 2021		2,869.3	(0.4)	(1.3)	5.7	132.3	1,123.0	4,128.6	12.5	4,141.1

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

Statements of changes in equity (continued)

Attributable to shareholders of Challenger Life Company Limited										
Parent		Contributed equity	Cash flow hedge reserve – SPV	Foreign currency translation reserve	Adjusted controlling interest reserve	Other reserve	Retained earnings	Total shareholder equity	Non-controlling interests	Total equity
For the year ended 30 June 2020	Note	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Balance at 1 July 2019		2,501.5	—	—	—	137.8	1,326.0	3,965.3	—	3,965.3
Loss for the year	15	—	—	—	—	—	(336.9)	(336.9)	—	(336.9)
Total comprehensive loss		—	—	—	—	—	(336.9)	(336.9)	—	(336.9)
Other equity movements										
Issued capital	13	270.0	—	—	—	—	—	270.0	—	270.0
Dividends paid	17	—	—	—	—	—	(286.6)	(286.6)	—	(286.6)
Balance at 30 June 2020 and 1 July 2020		2,771.5	—	—	—	137.8	702.5	3,611.8	—	3,611.8
For the year ended 30 June 2021										
Profit for the year	15	—	—	—	—	—	623.6	623.6	—	623.6
Total comprehensive profit for the year		—	—	—	—	—	623.6	623.6	—	623.6
Other equity movements										
Issued capital and equity hybrid notes	13	97.8	—	—	—	—	—	97.8	—	97.8
Dividends paid	17	—	—	—	—	—	(206.3)	(206.3)	—	(206.3)
Balance at 30 June 2021		2,869.3	—	—	—	137.8	1,119.8	4,126.9	—	4,126.9

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

Statements of cash flows

		Consolidated		Parent	
		2021	2020	2021	2020
For the year ended 30 June	Note	\$m	\$m	\$m	\$m
Operating activities					
Annuity and premium receipts	8	4,802.9	3,162.9	5,493.3	3,393.9
Annuity and claim payments	8	(3,787.9)	(3,747.0)	(3,957.6)	(3,748.1)
Receipts from external unit holders		2,346.8	2,024.0	—	—
Payments to external unit holders		(1,397.9)	(1,670.9)	—	—
Payments to vendors		(310.0)	(313.6)	(194.1)	(203.5)
Dividends received		31.0	43.6	169.4	156.8
Interest received		651.8	743.4	588.2	641.3
Interest paid		(20.3)	(67.1)	(15.4)	(61.4)
Other income received		355.7	380.0	22.3	106.8
Income tax paid		(118.1)	(10.0)	(203.0)	(15.2)
Net cash inflows from operating activities	12	2,554.0	545.3	1,903.1	270.6
Investing activities					
Payments on net purchases of investments		(930.9)	(1,726.2)	(547.8)	(1,359.2)
Payments for purchases of controlled entities		—	(10.2)	—	—
Net mortgage loan repayments		105.3	164.7	—	—
Receipts on net sale of investment properties		—	47.1	—	—
Net cash outflows from investing activities		(825.6)	(1,524.6)	(547.8)	(1,359.2)
Financing activities					
Net (repayment of)/proceeds from borrowings – interest bearing liabilities	14	(1,359.9)	773.7	(1,280.6)	945.1
Proceeds from issue of ordinary shares		30.0	270.0	30.0	270.0
Total proceeds from issue of hybrid notes		385.0	—	385.0	—
Repayment of hybrid notes		(317.3)	—	(317.3)	—
Dividends paid	17	(206.3)	(286.6)	(206.3)	(286.6)
Net proceeds from loans with related parties		0.6	37.7	111.6	8.6
Net cash (outflows)/inflows from financing activities		(1,467.9)	794.8	(1,277.6)	937.1
Net increase/(decrease) in cash and cash equivalents		260.5	(184.5)	77.7	(151.5)
Cash and cash equivalents at the beginning of the year		515.9	700.4	99.5	251.0
Cash and cash equivalents at the end of the year		776.4	515.9	177.2	99.5

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 and domiciled 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 2021 were authorised for issue in accordance with a resolution of the Directors of the Company on 9 August 2021.

(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 contract 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, 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) 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. The impact of COVID-19 has been considered in relation to the disclosures made in these financial statements.

Coronavirus (COVID-19) impact

Background

COVID-19, a respiratory illness caused by a new virus, was declared a worldwide pandemic by the World Health Organisation in March 2020. COVID-19, as well as measures to slow the spread of the virus, has since had a significant impact on global economies and equity and debt markets. The Group has considered the impact of COVID-19 and associated market volatility in preparing its financial statements. The impact of COVID-19 has resulted in the application of further judgement in the areas in which significant judgement already occurs. Given the dynamic and evolving nature of COVID-19 and limited recent experience of the economic and financial impacts of such a pandemic, changes to the estimates and

outcomes that have been applied in the measurement of the Group's assets and liabilities may arise in the future.

Processes applied

As a consequence of COVID-19 and in preparing these consolidated financial statements, management:

- re-evaluated whether there were any additional areas of judgement or estimation uncertainty;
- reviewed external market communications to identify other COVID-19 related impacts;
- reviewed public forecasts and experience from previous downturns and conducted several internal processes to ensure consistency in the application of the expected impact of COVID-19 across all asset classes;
- assessed the carrying values of its assets and liabilities and determined any impact that may occur as a result of market inputs and variables impacted by COVID-19;
- ran multiple stress testing scenarios, which are an integral component of the Group's risk management framework and a key input to the capital adequacy assessment process, to assess the potential impacts of the COVID-19 pandemic on its portfolio to assist in the organisation's prudent risk management; and
- considered the impact of COVID-19 on the Group's financial statement disclosures.

As a result of applying these processes, the Group has made additional disclosures in respect of the impact of COVID-19 on accounting judgements and estimates for the following:

- Basis of preparation and overarching significant accounting policies – (ix) Receivables;
- Note 6 Investment and development property;
- Note 19 Fair values of financial assets and liabilities; and
- Note 22 Goodwill and other intangible assets.

(iii) New and revised accounting standards and policies

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 have been no new or revised accounting standards or interpretations that are effective from the year beginning on or after 1 July 2020 which materially impact the financial results. Where applicable, comparative figures have been updated to reflect any changes in the current period.

Accounting standards and interpretations issued but not yet effective

AASB 17 Insurance Contracts

AASB 17 *Insurance Contracts* replaces AASB 4 *Insurance Contracts*, AASB 1038 *Life Insurance Contracts* and AASB 1023 *General Insurance Contracts*, and is effective for Challenger from 1 July 2023. The Group is not expected to early adopt the standard. AASB 17 *Insurance Contracts*

establishes globally consistent principles for the recognition, measurement, presentation and disclosure of life insurance contracts issued. Life investment contracts are currently measured under the financial instruments standard and will continue to be recognised under this standard.

AASB 17 introduces changes to the profit emergence profiles of life insurance contracts but does not affect the underlying economics or cash flows of the contracts. The impacts on capital requirements and income tax are unknown, pending regulatory responses from APRA and the Australian Taxation Office (ATO) respectively.

The main changes anticipated for the Group under AASB 17 are set out below.

- Insurance contract portfolios will be disaggregated to more granular levels and will be required to be evaluated by risk type, issue year and profitability.
- Although conceptually similar, the Contractual Service Margin (CSM) recognises profit on a different basis to the current Margin on Services (MoS) approach and therefore the profit signature is likely to change for portfolios with positive profit margins.
- A new risk adjustment for non-financial risk will be introduced which reflects the compensation that the Group requires for bearing the uncertainty in relation to the amount and timing of cash flows. The confidence level used to determine the risk adjustment will need to be disclosed.
- Additional disclosures will be more extensive, requiring increased granularity and more analysis of movements.

The Group has conducted a business impact assessment and has identified the following focus areas.

- **Measurement model** – The Group will adopt the General Model approach, also referred to as the Building Block Approach (BBA). In principle, the General Model approach is similar to the current MoS methodology as prescribed under AASB 1038. The General Model approach is a more detailed methodology that will require enhanced data capture and storing for additional modelling and processes.
- **Contracts affected** – The Group expects that all contracts classified as insurance contracts under AASB 1038 will meet the definition of insurance contracts under AASB 17.
- **Separating components** – The Group has assessed the requirement to unbundle features and components under AASB 17 and expects that no change will be required given no contracts are currently unbundled under AASB 1038.
- **Under AASB 17, assumptions are to be reviewed on an annual basis at a minimum with some items requiring more frequent review.**
- **Level of aggregation** – AASB 17 requires insurance contracts that are subject to similar risks and managed together, be allocated to a portfolio. AASB 17 requires that each portfolio be divided into a minimum of:
 1. a group that is onerous (loss-making) at initial recognition;
 2. a group that at initial recognition has no significant possibility of becoming onerous subsequently; and
 3. a group of any remaining contracts in the portfolio.

The Group has conducted a high-level review of historical data to ascertain the feasibility of meeting the level of aggregation required by AASB 17. In addition, the Group will be formalising a policy for defining portfolios and contract groups. Due to the nature of the insurance

products that Challenger offers its customers, the Group expects that most of the portfolios will be designated as onerous. If a portfolio is designated as onerous, a CSM calculation will not be required but the loss component will need to be tracked under AASB 17.

- **Risk adjustment** – The Group expects the risk adjustment methodology to align with the cost of capital approach.
- **Disclosure** – AASB 17 introduces a new way of viewing life insurance revenue and expenses and accompanying financial disclosures. Under AASB 17, insurance contract revenue will be allocated to each period in a proportion to the reduction in liability over the remaining coverage period. The Group has assessed the capability of the Group's general ledger system and confirms that no issues are anticipated for configuring the system to meet the new financial reporting and disclosure requirements under AASB 17.
- **Insurance contracts will need to be restated at 1 July 2023** (being the date of initial application). The first full year financial statements presented under AASB 17 will be for the year ended 30 June 2024 with comparatives required for 30 June 2023. The first half year financial statements will be for the period ended 31 December 2023, with comparatives required for 31 December 2022. The Group notes that the full retrospective approach maybe impracticable in some cases, especially for older cohorts where assumptions cannot be determined without hindsight.

While the standard is expected to impact the Group's comprehensive income, it is not yet practicable to determine the quantum.

Existing standards and interpretations not yet effective

Other amendments to existing standards or interpretations that are not yet effective are not expected to result in a material impact to the Group's financial statements.

(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 functional 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) Finance leases

Some entities within the Group acts as lessor on lease arrangements. Leases are classified at their inception as either operating or finance leases based on the economic substance of the agreement so as to reflect the risks and benefits incidental to ownership. Contracts to lease assets and hire purchase agreements are classified as finance leases for accounting purposes if they transfer substantially all the risks and rewards of ownership of the asset to the customer or an unrelated third party. Assets held under a finance lease are recognised at the beginning of the lease term at an amount equal to the net investment in the lease which comprises the gross investment in the lease discounted at the interest rate implicit in the lease. The collectability of lease receivables is assessed on an ongoing basis and a provision for expected credit loss (ECL) is made using inputs such as historical rates of arrears and the current delinquency position of the portfolio. The Group applies the simplified approach which measures the ECL equal to the discounted lifetime expected credit loss. Bad debts are written off as incurred.

(viii) 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.

(ix) Receivables

Receivables are recognised at amortised cost using the effective interest method, less any allowance for expected credit losses. The entity has applied a simplified approach to measuring expected credit losses, which uses a lifetime expected loss allowance. To measure the expected credit losses, receivables have been grouped based on days overdue. The modelling methodology applied in estimating expected credit losses in these financial statements is consistent with that applied in the financial statements for the year ended 30 June 2020. The impact of COVID-19 on the global economy and how governments, businesses and consumers respond is uncertain. This uncertainty is reflected in the Group's assessment of expected credit losses from its receivables portfolio which are subject to a number of management judgements and estimates.

The judgements and associated assumptions have been made within the context of the impact of COVID-19, and reflect historical experience and other factors that are considered to be relevant, including expectations of future events that are believed to be reasonable under the circumstances. In relation to COVID-19, judgements and assumptions include the extent and duration of the pandemic, the impacts of actions of governments and other authorities, and the responses of businesses and consumers in different industries, along with the associated impact on the global economy. Accordingly, the Group's expected credit losses estimates are inherently uncertain and, as a result, actual results may differ from these estimates.

(x) 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.

(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.

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 2021 \$m	30 June 2020 \$m	30 June 2021 \$m	30 June 2020 \$m
Investment revenue				
Fixed income securities and cash				
Interest revenue for items at fair value through profit and loss	664.2	759.1	597.0	637.7
Net realised and unrealised gains/(losses) on fixed income securities	42.7	(94.7)	(161.5)	(51.0)
Investment property and property securities				
Property rental revenue	291.1	283.9	—	—
Dividend revenue	5.6	2.0	—	—
Net realised and unrealised gains/(losses) on investment property and property securities	114.6	(112.1)	108.0	(12.9)
Equity and infrastructure investments				
Dividend revenue	22.1	37.9	156.2	250.7
Net realised and unrealised gains/(losses) on equity investments	124.8	(12.7)	130.2	(251.5)
Net realised and unrealised (losses) on infrastructure investments	(13.0)	(96.7)	(11.2)	(132.5)
Other				
Net realised and unrealised (losses) on foreign exchange translation and hedges	(78.6)	(51.5)	(49.8)	(87.4)
Net realised and unrealised gains/(losses) on interest rate derivatives	366.4	(70.7)	327.0	159.2
Net realised and unrealised gains/(losses) on equity swap derivatives	(16.1)	(202.2)	33.4	(255.5)
Net realised and unrealised gains/(losses) on credit default derivatives	23.6	(199.7)	23.6	(155.7)
Transaction fee revenue	8.6	18.4	3.2	8.6
Other revenue				
Life insurance contract premiums and related revenue	1,600.6	1,192.7	835.8	479.4
Change in life insurance contract liabilities	(622.0)	(502.1)	(263.1)	(27.0)
Change in life investment contract liabilities	29.8	(15.4)	110.5	(27.9)
Change in reinsurance contract liabilities	—	0.4	(2.2)	(0.1)
Total revenue	2,564.4	936.6	1,837.1	534.1

Accounting policy

Revenue is recognised at an amount that reflects the consideration to which the Group expects to be entitled in exchange for providing services to a customer. 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. The effective interest rate is the rate that discounts estimated future cash flows through the expected life of a financial instrument, or where appropriate, a shorter period. 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)

Accounting policy (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.
- Transaction fee revenue is recognised when the transaction is executed.
- Life insurance contract premiums are recognised as revenue when risk is transferred to the Group.
- 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 accounting policy of life contract liabilities.

Note 2 Expenses

	Consolidated		Parent	
	30 June 2021	30 June 2020	30 June 2021	30 June 2020
	\$m	\$m	\$m	\$m
Life insurance contract claims and expenses	852.4	749.6	518.5	500.5
Cost of life insurance contract liabilities	104.1	99.2	92.9	88.4
Cost of life investment contract liabilities	125.6	121.9	163.4	133.3
Reinsurance contracts	—	—	(1.8)	(0.6)
Investment property related expenses ¹	91.2	86.7	—	(0.6)
Management fee expense	46.1	46.8	37.9	35.5
Distribution expenses	51.2	42.3	51.2	42.2
Expenses SPV	3.2	4.5	—	—
Other expenses	116.3	111.5	104.5	98.9
Total expenses	1,390.1	1,262.5	966.6	897.6

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

Accounting policy

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

- 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. Rental expenses incurred under an investment property operating lease are recognised on a straight line basis over the term of the lease. 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 accounting policy of life contract liabilities.

Note 3 Segment information

The reporting segment¹ of the Group has been identified as follows:

	CLC Segment	
	2021	2020
	\$m	\$m
For the year ended 30 June		
Net income	544.0	679.6
Operating expenses	(111.1)	(104.1)
Normalised EBIT	432.9	575.5
Interest and borrowing costs	—	—
Normalised net profit before tax	432.9	575.5
Tax on normalised profit	(118.7)	(163.3)
Normalised net profit after tax	314.2	412.2
Investment experience	447.8	(1,069.7)
Tax on investment experience	(134.3)	320.9
Profit/(loss) attributable to shareholders of Challenger Life Company Limited	627.7	(336.6)
Other statutory segment information		
Revenue from external customers	1,900.5	177.5
Interest revenue	663.8	759.1
Interest expense	292.3	172.7
Management view of statement of financial position		
As at 30 June		
Segment assets ²	22,044.5	19,350.3
Segment liabilities ²	(17,915.9)	(15,737.8)
Net assets attributable to shareholders of Challenger Life Company Limited	4,128.6	3,612.5
Non-controlling interests	12.5	11.8
Total equity	4,141.1	3,624.3

¹ Refer below for definitions of the terms used in the management view of segments.

² Differs to Statement of financial position due to netting of interest bearing liabilities with segment assets.

Definitions

Operating segments

The following segment is identified on the basis of internal reporting to key management personnel, including the Principal 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, investment experience and significant items.

Note 3 Segment information (continued)

Normalised vs. statutory results (continued)

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 life contract valuation changes and new business loss. 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 period are +4.0% for equity and infrastructure and 0% for alternative investments (30 June 2020: +3.5% for equity and other investments and

+4.0% for infrastructure), +2.0% for property (30 June 2020: +2.0%) and -0.35% for cash and fixed income (30 June 2020: -0.35%). The rates are set with reference to medium to long-term market growth rates and are reviewed to ensure consistency with prevailing market conditions.

Annuity valuation experience

Life contract valuation experience changes represent the impact of changes in macroeconomic variables, including bond yields and inflation factors, expense assumptions and other factors applied in the valuation of life contract liabilities. It also includes the attribution of the corresponding interest rate, foreign exchange and inflation derivatives used for hedging.

Major customers

No individual customer amounted to greater than 10% of the Group's segment revenue as defined above.

Geographical areas

The Group operates predominantly in Australia, hence no geographical split is provided to the chief operating decision maker. Reinsurance of annuities issued by MS Primary accounted for \$901.6 million of the Group's life insurance premium income in 2021 out of total life insurance premium income of \$1,363.7 million (2020: \$742.6 million out of a total of \$1,157.1 million) and comprised 15.2% of total policy liabilities outstanding as at 30 June 2021 (2020: 13.7%); while the underlying annuitant resides in Japan, the reinsurance service provided by CLC is considered to be Australian business and is therefore not recognised as a geographically separate segment.

	30 June 2021 \$m	30 June 2020 \$m
Reconciliation of management to statutory view of after-tax profit		
Normalised net profit before tax (management view of pre-tax profit)	432.9	575.5
Tax on normalised profit	(118.7)	(163.3)
Normalised net profit after tax	314.2	412.2
Investment experience after tax	313.5	(748.8)
Profit/(loss) attributable to non-controlling interests excluded from management view	1.3	(4.4)
Statutory view of profit/(loss) after tax	629.0	(341.0)
Reconciliation of management view of revenue to statutory revenue		
Net income (management view of revenue)	544.0	679.6
Expenses and finance costs offset against revenue		
SPV expenses and finance costs offset against SPV income	287.8	160.0
Distribution expenses offset against related income	51.1	42.3
Change in life contract liabilities and reinsurance contracts recognised in expenses	1,082.4	970.7
Property related expenses offset against property income	91.2	85.0
Interest and loan amortisation costs	3.3	11.1
Management fees	46.1	46.8
Adjustment for non-controlling interests and other items	10.7	10.8
Difference between management view of investment experience and statutory recognition		
Actual capital growth ¹	566.6	(1,373.4)
Normalised capital growth	(34.1)	213.0
Annuity valuation experience	(84.7)	90.7
Statutory revenue (refer Note 1 Revenue)	2,564.4	936.6

¹ Actual capital growth represents net realised and unrealised capital gains or losses and includes the attribution of interest rate, inflation and foreign exchange derivatives that are used to hedge exposures.

Note 4 Income tax

	Consolidated		Parent	
	30 June 2021	30 June 2020	30 June 2021	30 June 2020
	\$m	\$m	\$m	\$m
Analysis of income tax (expense)/benefit				
Current income tax (expense)/benefit	(230.8)	52.0	(223.7)	10.7
Current income tax benefit prior year adjustment	1.1	4.7	1.3	11.8
Deferred income tax (expense)/benefit	(25.0)	100.7	(8.0)	62.3
Deferred income tax benefit prior year adjustment	1.7	0.2	1.2	0.2
Income tax (expense)/benefit	(253.0)	157.6	(229.2)	85.0
Income tax benefit on translation of foreign entities	17.4	5.0	—	—
Income tax (expense) on hedge of net investment in foreign entities	(20.1)	(0.2)	—	—
Income tax (expense)/benefit from other comprehensive income	(2.7)	4.8	—	—
Analysis of income tax (expense)/benefit				
Profit / (Loss) before income tax	882.0	(498.6)	852.8	(421.9)
Prima facie income tax based on the Australian company tax rate of 30%	(264.6)	149.6	(255.8)	126.6
Tax effect of amounts not assessable/deductible in calculating taxable income:				
- non-assessable and non-deductible items	—	(7.3)	21.0	(66.2)
- rate differential on offshore income	12.2	13.0	6.1	12.0
- tax adjustment in respect of non-controlling interest	0.4	(1.3)	—	—
- other items	(1.0)	3.6	(0.5)	12.6
Income tax (expense)/benefit	(253.0)	157.6	(229.2)	85.0
Underlying effective tax rate¹	28.7%	31.9%	26.9%	20.1%

¹ The calculation of the underlying effective tax rate excludes the non-controlling interests' profit of \$1.3 million (30 June 2020: \$4.4 million loss).

	Statement of financial position		Statement of comprehensive income	
	30 June 2021	30 June 2020	30 June 2021	30 June 2020
	\$m	\$m	\$m	\$m
Consolidated				
Analysis of deferred tax				
Deferred tax assets				
Accruals and provisions	1.4	2.0	(0.6)	(0.8)
Losses	108.0	151.8	(43.8)	(8.2)
Other	4.4	16.0	(11.6)	2.4
Setting off deferred tax assets by jurisdiction	(113.0)	(168.2)	—	—
Total deferred tax assets¹	0.8	1.6	(56.0)	(6.6)
Deferred tax liabilities				
Unrealised foreign exchange movements	(7.7)	(1.9)	(5.9)	24.5
Unrealised movements on investments	(222.0)	(249.7)	30.2	76.1
Other	—	(8.4)	8.4	6.9
Setting off deferred tax assets by jurisdiction	113.0	168.2	—	—
Total deferred tax liabilities	(116.7)	(91.8)	32.7	107.5
Net deferred tax liabilities (statement of financial position)	(115.9)	(90.2)	—	—
Deferred income tax (expense)/benefit (statement of comprehensive income)			(23.3)	100.9

¹ Deferred tax assets of \$2.5 million (30 June 2020: \$2.4 million) have not been recognised in respect of non-tax consolidated group entities' revenue losses.

Note 4 Income tax (continued)

	30 June 2021 \$m	30 June 2020 \$m	Change \$m
Australian and overseas tax (expense) / benefit			
Australian operations	(243.2)	161.0	(404.2)
Overseas operations	(9.8)	(3.4)	(6.4)
Income tax (expense)/benefit	(253.0)	157.6	(410.6)

Parent	Statement of financial position		Statement of comprehensive income	
	30 June 2021 \$m	30 June 2020 \$m	30 June 2021 \$m	30 June 2020 \$m
Analysis of deferred tax				
Deferred tax assets				
Accruals and provisions	1.4	2.0	(0.6)	(1.6)
Other	0.8	0.9	(0.1)	0.9
Total deferred tax assets	2.2	2.9	(0.7)	(0.7)
Deferred tax liabilities				
Unrealised foreign exchange movements	(7.7)	(1.9)	(5.9)	2.9
Unrealised gains on investments	(123.8)	(123.5)	(0.2)	60.1
Other	—	—	—	0.1
Total deferred tax liabilities	(131.5)	(125.4)	(6.1)	63.1
Net deferred tax liabilities (statement of financial position)	(129.3)	(122.5)	—	—
Deferred income tax (expense)/benefit (statement of comprehensive income)			(6.8)	62.4

Accounting policy

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 period are measured at the amounts 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 assets and liabilities

Deferred income tax assets and liabilities are recognised for deductible or taxable temporary differences and are measured at the tax rates that are expected to apply to the year the asset is realised or the liability is settled, based on the tax rates (and tax laws) that have been enacted or substantially enacted as at the statement of financial position date. Deferred income tax assets and liabilities are offset only if a legally enforceable right exists to set off.

Tax consolidation

Challenger Limited and its eligible 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.

Note 4 Income tax (continued)

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 Shareholder 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 2020: \$207.0 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.

Key estimates and assumptions

Deferred tax assets are recognised for deductible temporary differences and unused tax losses only if it is probable that future taxable amounts will be available to utilise those temporary differences and losses.

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 2021	30 June 2020	30 June 2021	30 June 2020
	\$m	\$m	\$m	\$m
Fixed income securities				
Domestic sovereign bonds and semi-government bonds	6,054.8	8,610.3	5,760.5	7,809.6
Floating rate notes and corporate bonds	6,566.3	4,915.6	4,620.9	4,735.7
Residential mortgage and asset-backed securities	7,653.6	5,809.2	6,245.0	4,046.6
Non-SPV mortgage assets	112.2	139.8	—	—
Controlled entities	—	—	3,033.0	2,767.5
	20,386.9	19,474.9	19,659.4	19,359.4
Equity securities				
Controlled entities	—	—	347.2	631.2
Shares in listed and unlisted corporations	142.4	97.1	32.9	99.2
Unit trusts, managed funds and other	1,201.3	804.9	1,186.0	313.7
	1,343.7	902.0	1,566.1	1,044.1
Infrastructure investments				
Units in unlisted infrastructure trusts	48.8	55.9	18.4	11.6
Other infrastructure investments	296.6	324.2	—	—
	345.4	380.1	18.4	11.6
Property securities				
Indirect property investments in unlisted trusts	88.0	76.3	—	—
Controlled trusts				
Infrastructure	—	—	173.7	181.8
Property	—	—	1,139.2	1,052.4
Other	—	—	388.0	168.8
	—	—	1,700.9	1,403.0
Total financial assets – fair value through profit and loss	22,164.0	20,833.3	22,944.8	21,818.1
Current	11,900.4	8,338.5	12,984.3	7,834.0
Non-current	10,263.6	12,494.8	9,960.5	13,984.1
	22,164.0	20,833.3	22,944.8	21,818.1

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

Accounting policy

The Group categorises its financial assets as financial assets - fair value through profit and loss (being initially designated as such). 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.

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;
- option 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

	30 June 2021 \$m	30 June 2020 \$m
Consolidated		
Investment property held for sale ¹	388.0	—
Investment property in use	3,389.7	3,679.7
Investment property under development	—	6.2
Development property held for sale ^{2,3}	8.0	—
Total investment and development property⁴	3,785.7	3,685.9

¹ Investment property held for sale: County Court (30 June 2020: Nil).

² Development property held for sale: Maitland (30 June 2020: Nil).

³ Development property held for sale is recognised at fair value.

⁴ Investment and development property held for sale is considered current. All other investment property is considered non-current.

Note 6 Investment and development property (continued)

Consolidated	Investment property held for sale		Investment property in use		Investment property under development		Development property held for sale	
	30 June 2021	30 June 2020	30 June 2021	30 June 2020	30 June 2021	30 June 2020	30 June 2021	30 June 2020
Reconciliation of carrying amounts	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Balance at the beginning of the year	—	166.5	3,679.7	3,384.3	6.2	178.4	—	—
Movements for the year								
- acquisitions ¹	—	—	—	105.1	—	—	—	—
- disposals	—	(155.9)	—	—	—	—	—	—
- net transfers to/(from) investment property held for sale	326.0	(10.7)	(326.0)	10.7	—	—	—	—
- transfers to/(from) investment property under development	—	—	—	173.7	(6.2)	(173.7)	6.2	—
- capital expenditure	0.7	0.1	50.3	72.8	—	0.2	0.1	—
- net revaluation gain/(loss)	61.3	—	75.8	(78.4)	—	1.3	1.7	—
- foreign exchange gain/(loss)	—	—	(90.1)	11.5	—	—	—	—
Balance at the end of the year	388.0	—	3,389.7	3,679.7	—	6.2	8.0	—

¹ Investment property acquisitions: Nil (30 June 2020: Acquisition of remaining 50% of Lennox, NSW \$33.5m, Aeon Matsusaka XD, Japan \$14.7m, Kotesashi Towers, Japan \$25.2m and Yorktown Toride, Japan \$31.7m).

Accounting policy

Investment and development property

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.

Investment and development 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 to occur in the next 12 months. Investment and development 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 and development properties are derecognised when they have either been disposed of or when the investment and development property is permanently withdrawn from use and no future benefit is expected from its disposal. Any gain or loss on the retirement or disposal of an investment or development property is 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.

Impact of COVID-19

Across all sectors, particularly retail, some tenants have sought rent relief due to the impact the COVID-19 pandemic has had on their ability to meet rental obligations. Rent relief is granted after considering various factors and individual tenant circumstances. Rent amounts will fall into the following categories: (i) current rent due and payable now; (ii) deferred rent, payable at a later date; or (iii) waived rent, not payable.

If relief is given for current and deferred rent, income will continue to be recognised on a straight line basis over the term of the lease. The resulting rent receivable assets recognised in the statement of financial position as at 30 June 2021 have been assessed for impairment.

The methodology adopted for determining whether these rent receivable assets should be impaired is aligned to the requirements of AASB 9 *Financial Instruments*.

When an agreement is made between the landlord and tenant to waive rent:

- rent waived relating to future occupancy is spread over the remaining lease term and recognised on a straight line basis;
- rent waived relating to past occupancy is expensed immediately, except to the extent of a pre-existing provision for expected credit losses relating to unpaid rent.

Key estimates and assumptions

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. For the year ended 30 June 2021, all investment properties were valued by external valuers.

Note 6 Investment and development property (continued)

Key estimates and assumptions (continued)

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, and on the basis that they are engaged for no longer than two consecutive years on an individual property.

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.

Impact of COVID-19

As at 30 June 2021, the real estate markets to which the Group's investment properties belong were still being impacted by significant uncertainty caused by the COVID-19 pandemic. This has continued to create valuation uncertainty for the year ended 30 June 2021.

The valuation uncertainty has affected key inputs, assumptions and processes used in the valuation of the Group's investment properties, being:

- estimating and forecasting the net income that a property can produce; and
- converting that income to value by applying investment rates of return which are derived from analysis of recent market transactions.

Income uncertainty

The impact of COVID-19 on the income-earning potential of the Group's properties remains uncertain. The Group leases commercial space to a range of businesses from where they conduct their operations. Restrictions imposed by Government to combat COVID-19 has, in a majority of cases, impacted the ability for these businesses to operate effectively from their premises, or has affected their ability to operate in the usual manner prior to the onset of COVID-19.

In response to this and the Government's Code of Conduct for commercial tenancies, the Group is currently finalising the cost-sharing program introduced by the Code of Conduct for each tenant that has been affected. This involves the Group either deferring or waiving rent owed by the tenant depending on the individual circumstances. The legislative period for this relief has now ended across all states and there remains a small portion of rent relief negotiations in progress which are yet to be finalised. Since 30 June 2021, the NSW

and Victorian Governments have reintroduced restrictions to combat several COVID-19 outbreaks within each state. These restrictions will impact the operations of businesses across all sectors which the Group has property exposure. To assist businesses through these restrictions, the Government has announced business relief packages for those that are hardest hit. The Group will continue to monitor the Government's position on these business support packages and work with those tenants that have been severely impacted.

Rent receivable balances in respect of current and deferred rent recognised in the statement of financial position for the reporting period, have been assessed for impairment. An approach has been adopted which applies a lifetime expected credit loss and assesses all possible default events over the expected life of the receivables balance.

An appropriate loss rate has then been determined after considering the following factors:

- the asset sector in which the affected rent receivable is recognised. Each sector is affected differently by COVID-19 and this needs to be reflected in any loss assumption;
- the ranking of tenants by most to least affected by COVID-19; and
- the ageing of rent receivables.

After taking these factors into consideration and the cost-sharing program undertaken with tenants, an impairment of \$2.7 million was recognised in the Statement of comprehensive income for the year ended 30 June 2021 (30 June 2020: \$2.2 million) which includes an impairment for current and deferred rent, as well as waived rent impaired immediately. This assessment was conducted based on reasonable and supporting information readily available, and considering current and expected future economic conditions.

Valuation uncertainty

Valuation uncertainty has also arisen from a lack of transactional evidence from which to gauge current market pricing with strong conviction. Due to uncertainty relating to the impact of COVID-19, transaction volumes were low through the first half of the year ended 30 June 2021. Although activity has begun to improve, at this point in time, the repercussions of the pandemic on the property market remains uncertain and market pricing cannot be known with typical certainty until such time the market stabilises.

In response to this valuation uncertainty, the Group determined that all directly held investment properties would be independently valued by external valuers at 30 June 2021. The Group's independent valuers have accounted for this income and investment uncertainty by adjusting valuation inputs and estimates to acknowledge the potential impact of COVID-19 on investment property values. In addition to having regard to the available sales evidence to determine capitalisation and discount rates, they have also, where appropriate, adopted lower growth rates in the short to medium term, increased vacancy rates and letting up allowances and lower market rental levels. Notwithstanding the end of the legislated period for rent relief, valuers have continued to make deductions for the estimated cost of rent relief to tenants for occupancy disruption resulting from the COVID-19 pandemic.

Note 6 Investment and development property (continued)

Property valuations

Analysis of investment property as at 30 June	Acquisition date ¹	Total cost ² \$m	Carrying value 2021 \$m	Cap rate 2021 ³ %	Last external valuation date	Carrying value 2020 \$m	Cap rate 2020 ³ %
Investment property in use and held for sale							
Australia							
6 Chan Street (formerly DIBP Building), ACT	01-Dec-01	127.5	261.0	4.88	30-Jun-21	202.0	5.50
14 Childers Street, ACT	01-Dec-17	98.8	85.5	6.50	30-Jun-21	91.0	6.50
21 O'Sullivan Circuit, NT	27-Jan-16	47.8	31.4	7.75	30-Jun-21	32.1	8.50
31 O'Sullivan Circuit, NT	27-Jan-16	29.4	28.5	7.25	30-Jun-21	23.5	8.50
35 Clarence Street, NSW	15-Jan-15	154.0	229.0	5.13	30-Jun-21	235.0	5.00
45 Benjamin Way (formerly ABS Building), ACT	01-Jan-00	150.2	251.0	5.38	30-Jun-21	223.0	5.75
82 Northbourne Avenue, ACT	01-Jun-17	62.3	51.8	5.75	30-Jun-21	53.3	6.00
215 Adelaide Street, QLD	31-Jul-15	256.7	225.0	6.00	30-Jun-21	230.5	6.13
565 Bourke Street, VIC	28-Jan-15	109.1	148.0	5.00	30-Jun-21	147.5	5.00
839 Collins Street, VIC	22-Dec-16	212.0	246.5	4.75	30-Jun-21	238.5	4.75
Bunbury Forum, WA	03-Oct-13	158.2	78.1	7.25	30-Jun-21	82.0	7.50
Channel Court, TAS	21-Aug-15	87.8	80.0	7.25	30-Jun-21	76.0	7.75
Cosgrave Industrial Park, Enfield, NSW	31-Dec-08	91.4	139.4	4.50	30-Jun-21	131.9	5.00
County Court, VIC	30-Jun-00	219.1	388.0	n/a	30-Jun-21	326.0	n/a
Discovery House, ACT	28-Apr-98	104.6	164.0	5.13	30-Jun-21	152.5	5.63
Executive Building, TAS	30-Mar-01	35.1	49.0	5.75	30-Jun-21	46.5	7.00
Gateway, NT	01-Jul-15	124.1	102.9	6.34	30-Jun-21	105.1	6.34
Golden Grove, SA	31-Jul-14	159.9	148.0	6.25	30-Jun-21	147.0	6.25
Karratha, WA	28-Jun-13	57.1	45.4	7.50	30-Jun-21	44.3	7.50
Kings Langley, NSW	29-Jul-01	16.6	24.7	5.75	30-Jun-21	23.0	6.25
Lennox, NSW	27-Jul-13	64.2	65.0	6.75	30-Jun-21	61.0	6.75
North Rocks, NSW	18-Sep-15	187.0	179.0	6.00	30-Jun-21	171.1	6.25
Total Australia		2,552.9	3,021.2			2,842.8	

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 ² \$m	Carrying value 2021 \$m	Cap rate 2021 ³ %	Last external valuation date	Carrying value 2020 \$m	Cap rate 2020 ³ %
Europe							
Avenue de Savigny, Aulnay sous Bois	31-Dec-08	20.3	9.8	7.00	30-Jun-21	10.1	7.33
Japan							
Aeon Kushiro	31-Jan-10	30.5	34.2	5.40	30-Jun-21	38.5	5.40
Aeon Matsusaka XD	26-Sep-19	14.7	13.7	5.60	30-Jun-21	14.5	5.80
Carino Chitosedai	31-Jan-10	118.4	127.2	4.50	30-Jun-21	138.6	4.50
Carino Tokiwadai	31-Jan-10	77.6	75.5	4.60	30-Jun-21	85.9	4.70
DeoDeo Kure	31-Jan-10	32.2	31.2	5.50	30-Jun-21	35.3	5.60
Fitta Natalie Hatsukaichi	28-Aug-15	11.7	13.4	5.90	30-Jun-21	14.8	6.00
Izumiya Hakubaicho	31-Jan-10	69.6	71.4	4.80	30-Jun-21	78.0	5.00
Kansai Super Saigo	31-Jan-10	13.3	13.2	5.50	30-Jun-21	14.7	5.30
Kojima Nishiarai	31-Jan-10	12.2	14.6	4.10	30-Jun-21	16.4	4.40
Kotesashi Towers	28-Nov-19	25.2	21.5	5.07	30-Jun-21	24.3	5.10
Life Asakusa	31-Jan-10	27.9	35.1	4.20	30-Jun-21	38.6	4.30
Life Higashi Nakano	31-Jan-10	32.9	36.7	4.30	30-Jun-21	40.7	4.40
Life Nagata	31-Jan-10	25.2	27.7	4.90	30-Jun-21	30.3	4.20
MaxValu Tarumi	28-Aug-15	17.0	18.2	5.70	30-Jun-21	20.6	5.60
Seiyu Miyagino	31-Jan-10	9.8	10.6	5.20	30-Jun-21	12.0	5.20
TR Mall Ryugasaki	30-Mar-18	86.7	90.5	5.50	30-Jun-21	98.7	5.60
Valor Takinomizu	31-Jan-10	27.4	23.5	5.80	30-Jun-21	26.5	5.50
Valor Toda	31-Jan-10	42.5	41.7	5.20	30-Jun-21	46.3	5.10
Yaoko Sakato Chiyoda	31-Jan-10	19.8	20.9	4.70	30-Jun-21	22.8	4.90
Yorktown Toride	05-Mar-20	31.9	25.9	5.10	30-Jun-21	29.3	5.30
Total international		746.8	756.5			836.9	
Total investment property in use and held for sale⁴		3,299.7	3,777.7			3,679.7	
Investment property under development and development property held for sale							
Maitland, NSW	6-Dec-06	5.7	8.0	n/a	30-Jun-21	6.2	n/a
Total investment property under development and development property held for sale		5.7	8.0			6.2	

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 2021, the investment property portfolio occupancy rate for Australia was 90.3% (30 June 2020: 90.7%) with a weighted average lease expiry of 5.1 years (30 June 2020: 5.5 years), Europe 100.0% (30 June 2020: 100.0%) with a weighted average lease expiry of 0.1 years (30 June 2020: 0.1 years) and Japan 99.5% (30 June 2020: 99.5%) with a weighted average lease expiry of 9.4 years (30 June 2020: 9.7 years).

Note 7 Special Purpose Vehicles

	30 June 2021	30 June 2020
	\$m	\$m
Consolidated		
Cash and cash equivalents	60.8	58.0
Mortgage assets ¹	597.5	702.4
Derivative assets	—	0.4
Total assets	658.3	760.8
Payables ²	31.9	28.4
Derivative liabilities	0.5	0.3
Interest bearing financial liabilities ^{1,2}	595.0	686.9
Total liabilities	627.4	715.6
Net assets	30.9	45.2
Cash flow hedge reserve	0.4	(0.1)
Total equity attributable to residual income unit (RIU) holders	31.3	45.1

¹ \$145.6 million (30 June 2020: \$136.9 million) of the Mortgage assets balance is considered current, and \$116.0 million (30 June 2020: \$167.3 million) of the Interest bearing financial liabilities balance is considered current.

² Differs to the statement of financial position - Interest bearing liabilities – SPV and Payables - SPV due to the value of cumulative eliminations between the SPV and other members of the Group of \$215.3 million (30 June 2020: \$254.2 million) and \$4.2 million (30 June 2020: Nil) respectively.

Accounting policy

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 SPVs 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 SPVs 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 SPVs 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 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.

Key estimates and assumptions

The SPVs are valued making as much use of available and supportable market data as possible and keeping judgemental inputs to a minimum by using discounted cash flow analysis or other methods consistent with market best practice.

Note 8 Life contract liabilities

	Consolidated		Parent	
	30 June 2021 \$m	30 June 2020 \$m	30 June 2021 \$m	30 June 2020 \$m
Life investment contract liabilities – at fair value	6,230.4	5,867.8	8,677.7	7,408.7
Life insurance contract liabilities – at margin on services value	7,440.5	6,714.4	5,791.2	5,435.2
Reinsurance contract liabilities – at margin on services value	(1.0)	(1.0)	(28.2)	(30.9)
Total life contract liabilities	13,669.9	12,581.2	14,440.7	12,813.0

Consolidated	Life investment contract liabilities		Life insurance contract liabilities		Outward reinsurance contract liabilities		Total life contract liabilities	
	30 June 2021 \$m	30 June 2020 \$m	30 June 2021 \$m	30 June 2020 \$m	30 June 2021 \$m	30 June 2020 \$m	30 June 2021 \$m	30 June 2020 \$m
Movement in life contract liabilities								
Balance at the beginning of the year	5,867.8	6,757.7	6,714.4	6,113.1	(1.0)	(0.6)	12,581.2	12,870.2
Deposits and premium receipts	3,202.3	1,970.2	1,600.6	1,192.7	—	—	4,802.9	3,162.9
Payments and withdrawals	(2,935.5)	(2,997.4)	(852.4)	(749.6)	—	—	(3,787.9)	(3,747.0)
Revenue per Note 1	(29.8)	15.4	(978.6)	(690.6)	—	(0.4)	(1,008.4)	(675.6)
Expense per Note 2	125.6	121.9	956.5	848.8	—	—	1,082.1	970.7
Balance at the end of the year	6,230.4	5,867.8	7,440.5	6,714.4	(1.0)	(1.0)	13,669.9	12,581.2

Parent	Life investment contract liabilities		Life insurance contract liabilities		Outward reinsurance contract liabilities		Total life contract liabilities	
	30 June 2021 \$m	30 June 2020 \$m	30 June 2021 \$m	30 June 2020 \$m	30 June 2021 \$m	30 June 2020 \$m	30 June 2021 \$m	30 June 2020 \$m
Movement in life contract liabilities								
Balance at the beginning of the year	7,408.7	7,582.3	5,435.2	5,319.8	(30.9)	(31.9)	12,813.0	12,870.2
Deposits and premium receipts	4,657.5	2,914.5	835.8	479.4	—	—	5,493.3	3,393.9
Payments and withdrawals	(3,441.4)	(3,249.3)	(518.5)	(500.5)	2.3	1.7	(3,957.6)	(3,748.1)
Revenue per Note 1	(110.5)	27.9	(572.7)	(452.4)	2.2	(0.1)	(681.0)	(424.6)
Expense per Note 2	163.4	133.3	611.4	588.9	(1.8)	(0.6)	773.0	721.6
Balance at the end of the year	8,677.7	7,408.7	5,791.2	5,435.2	(28.2)	(30.9)	14,440.7	12,813.0

Note 8 Life contract liabilities (continued)

Consolidated	30 June 2021	30 June 2020
	\$m	\$m
Analysis of life insurance and reinsurance contract liability and expenses		
Best estimate liability		
Value of future life insurance contract benefits	6,928.6	6,435.1
Value of future expenses	196.6	171.3
Value of future acquisition expenses	175.1	166.9
Value of future premiums	(902.1)	(889.3)
Total best estimate liability	6,398.2	5,884.0
Value of future profit margins	1,041.3	829.4
Net life insurance and reinsurance contract liability	7,439.5	6,713.4
Life insurance and reinsurance contract operating expenses		
Maintenance expenses	61.6	54.9
Total life insurance and reinsurance contract operating expenses	61.6	54.9
Analysis of life contract profit		
Profit margin release on life insurance contracts	23.5	27.8
Loss recognition in respect of life insurance contracts ¹	(50.6)	(43.5)
Loss recognition in respect of life investment contracts	(88.7)	(54.2)
Difference in actual and assumed experience in respect of life insurance contracts	267.8	(74.5)
Difference in actual and assumed experience in respect of life investment contracts	278.5	(68.6)
Profit/(loss) arising from difference between actual and assumed experience	430.5	(213.0)
Investment earnings on assets in excess of life contract liabilities	197.3	(123.6)
Life contract profit/(loss) after tax²	627.8	(336.6)

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 \$627.7 million (30 June 2020: \$336.9 million loss)

Accounting policy

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 immediately. 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.

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

Note 8 Life contract liabilities (continued)

Life insurance premium revenue

Life insurance premiums are recognised as revenue when risk is transferred to the Group.

Life insurance claims expense

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

Inwards reinsurance

The Group has maintained inwards 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 and AASB 1038 *Life Insurance Contracts*, 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, longevity reinsurance and wholesale lifetime annuities. Annuity payments are used as the profit carrier for 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

Tax rates

The bases of taxation (including deductibility of expenses) are assumed to continue in accordance with legislation current at the reporting date.

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 9 *Financial Instruments*. 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 2020. Discount rates applied for Australian liabilities were between 0.3% - 2.8% per annum (30 June 2020: 0.9% - 2.4%).

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 2.0% per annum for short-term inflation and 2.3% per annum for long-term inflation (30 June 2020: -0.2% short-term, 1.8% long-term).

Surrenders

For life investment contracts, no surrenders or voluntary discontinuances are assumed. For Australian life insurance contracts where a surrender value is payable on withdrawal, a rate of surrenders is assumed in line with Challenger's own experience on these products, currently between 0.0% - 2.1% per annum (30 June 2020: 0.0% - 2.1%). 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 (30 June 2020: 3.5%).

Where policyholders have the option to commute a life insurance contract, the value of this option is included within the life contract liabilities. We also assume surrender rates based on past experience for this business which vary by product types and duration in-force for the contract.

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. For the age ranges and cash flow projection periods that contribute the majority of CLC's exposure, rates of future mortality improvement applied are between 0.3% - 2.5% per annum (30 June 2020: 0.3% - 2.5%).

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 SAPS3 tables mortality investigation developed by the Institute and Faculty of Actuaries (UK) using United Kingdom data collected between 2009–2016). Rates are adjusted for expected future mortality improvements based on observed and expected improvements. For the age ranges and cash flow projection periods that contribute the majority of CLC's exposure, rates of future mortality improvement applied are between 0.2% - 2.3% per annum (30 June 2020: 0.6% - 2.1%).

Base mortality rates for the inwards reinsurance of Japanese business are determined as a multiple of Japanese population mortality rates.

Note 8 Life contract liabilities (continued)

Valuation (continued)

Mortality (continued)

Mortality assumptions have been reviewed but not adjusted in light of the COVID-19 pandemic.

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

Financial assets held in the Group 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.

Statutory fund information

The life contract operations of CLC are conducted within four separate statutory funds. 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 outwards reinsurance, plus the wholesale mortality, wholesale morbidity and longevity inwards reinsurance. Fund 4 contains inwards reinsurance of annuity business written in Japan.

Life contract liabilities for Funds 1, 2, 3 and 4 are:

	30 June 2021	30 June 2020
Life contract liabilities	\$m	\$m
Statutory Fund 1	1.5	1.5
Statutory Fund 2	11,582.4	10,854.4
Statutory Fund 3	3.0	2.6
Statutory Fund 4	2,083.0	1,722.7
Total life contract liabilities	13,669.9	12,581.2

Current/non-current split for total life contracts

There is a fixed settlement date for the majority of life contract liabilities. Approximately \$3,099.3 million on a discounted basis (30 June 2020: \$2,596.5 million) of life contract liabilities have a contractual maturity within 12 months of the reporting date. Based on assumptions applied for the 30 June 2021 valuation of life contract liabilities, \$3,685.7 million of principal payments on fixed term and lifetime business are expected in the year to 30 June 2022 (expected in the year to 30 June 2021: \$3,327.7 million).

Life insurance risk

The Group is exposed to longevity risk on its individual lifetime annuities (both direct and reinsured) 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 reinsurance 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 maintains a reinsurance arrangement to manage longevity risk in respect of part of the closed book 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. The Company's insurance risk policy is approved by the Board and sets out the relevant risk limits for insurance exposures, to ensure the insurance risk portfolio is appropriately diversified and contains no significant concentrations of insurance risk.

Note 8 Life contract liabilities (continued)

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:

Insurance risk sensitivity analysis	Increase in life insurance contract liabilities				Loss after tax and equity impact			
	Gross		Net		Gross		Net	
	30 June 2021 \$m	30 June 2020 \$m	30 June 2021 \$m	30 June 2020 \$m	30 June 2021 \$m	30 June 2020 \$m	30 June 2021 \$m	30 June 2020 \$m
50% increase in the rate of mortality improvement	43.3	35.4	42.7	34.8	(30.3)	(24.8)	(29.9)	(24.4)
10% increase in maintenance expenses	18.3	16.3	18.3	16.3	(12.8)	(11.4)	(12.8)	(11.4)

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
2021	863.9	1,465.8	1,158.7	4,817.7	8,306.1
2020	775.4	1,272.1	1,014.4	4,574.9	7,636.8

Actuarial information

Mr A Kapel 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, APRA Prudential Standards, AASB 1038 *Life Insurance Contracts*, and AASB 9 *Financial Instruments*.

Note 9 External unit holders' liabilities

Consolidated	30 June 2021 \$m	30 June 2020 \$m
Current	3,090.1	1,587.3
Non-current	542.1	828.5
Total liabilities to external unit holders	3,632.2	2,415.8

Accounting policy

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 external unit holders' liabilities on the statement of financial position and represent the funds owing to third parties on these mandates. These funds are managed independently to CLC, with a separate Responsible Entity or Trustee and independent Board members. The liability is recognised at fair value.

Note 10 Derivative financial instruments

Consolidated Analysis of derivative financial instruments	30 June 2021			30 June 2020		
	Notional value \$m	Net fair value assets \$m	Net fair value liabilities \$m	Notional value \$m	Net fair value assets \$m	Net fair value liabilities \$m
Non-SPV						
Interest rate swaps						
Less than one year	5,069.0	8.8	(2.1)	7,495.7	7.1	(4.2)
One to three years	9,089.6	47.0	(40.8)	8,946.1	34.7	(32.7)
Three to five years	11,334.1	80.6	(71.6)	8,674.9	100.7	(62.3)
Greater than five years	41,913.7	307.1	(368.8)	36,600.7	511.1	(594.1)
Total interest rate swaps	67,406.4	443.5	(483.3)	61,717.4	653.6	(693.3)
Collateral securities¹	—	—	216.7	—	—	259.0
Inflation-linked swaps						
Less than one year	300.0	—	(2.3)	211.0	7.6	(1.4)
One to three years	243.0	2.5	—	243.0	10.1	—
Three to five years	387.0	10.0	(4.6)	72.0	3.0	(7.8)
Greater than five years	1,092.0	60.3	(28.0)	1,407.0	164.0	(43.0)
Total inflation-linked swaps	2,022.0	72.8	(34.9)	1,933.0	184.7	(52.2)
Futures contracts						
Less than one year	16,168.8	—	(1.0)	18,101.9	—	(0.6)
Total futures contracts	16,168.8	—	(1.0)	18,101.9	—	(0.6)
Forward currency contracts						
Less than one year	2,850.1	32.0	(22.5)	2,947.5	63.2	(46.9)
Total forward currency contracts	2,850.1	32.0	(22.5)	2,947.5	63.2	(46.9)
Cross-currency swaps						
Less than one year	1,397.7	17.8	(17.9)	1,268.7	29.2	(44.0)
One to three years	3,187.4	29.9	(40.5)	2,332.3	69.8	(15.3)
Three to five years	2,482.5	11.6	(29.2)	1,332.1	36.6	(10.5)
Greater than five years	765.0	7.5	(9.8)	825.4	25.3	(5.5)
Total cross-currency swaps	7,832.6	66.8	(97.4)	5,758.5	160.9	(75.3)
Equity swaps						
Less than one year	1,475.0	16.4	—	596.6	20.0	—
One to three years	308.9	2.1	(0.4)	—	—	—
Total equity swaps	1,783.9	18.5	(0.4)	596.6	20.0	—
Credit default swaps						
Less than one year	63.4	0.3	—	—	—	—
One to three years	—	—	—	67.9	1.2	(0.6)
Three to five years	1,218.8	96.4	—	—	—	—
Total credit default swaps	1,282.2	96.7	—	67.9	1.2	(0.6)
Options						
Less than one year	—	—	—	2.5	0.6	—
Total options	—	—	—	2.5	0.6	—
Total - Non-SPV	99,346.0	730.3	(422.8)	91,125.3	1,084.2	(609.9)
SPV						
Interest rate swaps – SPV						
Less than one year	7.2	—	(0.1)	5.1	—	(0.1)
One to three years	0.7	—	—	7.6	—	(0.1)
Three to five years	0.6	—	—	0.5	—	—
Total interest rate swaps – SPV	8.5	—	(0.1)	13.2	—	(0.2)
Cross-currency swaps – SPV						
Greater than five years	212.1	—	(0.4)	261.0	0.4	(0.1)
Total cross-currency swaps – SPV	212.1	—	(0.4)	261.0	0.4	(0.1)
Total – SPV	220.6	—	(0.5)	274.2	0.4	(0.3)
Total derivative financial instruments²	99,566.6	730.3	(423.4)	91,399.5	1,084.6	(610.2)

¹ Collateral securities relates to centrally cleared interest rate swaps.

² 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 decrease by \$284.9 million (30 June 2020: \$474.1 million) and the derivative liabilities would decrease by \$284.9 million (30 June 2020: \$474.1 million).

Note 10 Derivative financial instruments (continued)

Accounting policy

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:

- 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 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.

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 the statement of 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 2021, a post-tax gain of \$46.8 million (30 June 2020: post-tax gain \$0.5 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, SPVs 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 rates. Cross-currency swaps are also entered into to hedge currency movements on foreign denominated RMBS. The SPVs 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 2021, a post-tax loss of \$0.5 million (30 June 2020: post-tax gain nil) 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

Accounting policy

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. As at 30 June 2021 \$264.5 million (30 June 2020: \$471.8 million) cash received from third parties as collateral is recorded in payables and \$74.6 million (30 June 2020: \$221.4 million) of collateral assets received from counterparties were repledged by the Company to third parties. Except in the event of default, collateral received can

be called back by the counterparty in accordance with the financial arrangement.

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.

	30 June 2021	30 June 2020
Consolidated	\$m	\$m
Collateral pledged by CLC as security		
Cash	269.9	97.8
Other financial assets	6,675.5	7,730.9
Total collateral pledged	6,945.4	7,828.7

Note 12 Notes to the statements of cash flows

	Consolidated		Parent	
	30 June 2021	30 June 2020	30 June 2021	30 June 2020
	\$m	\$m	\$m	\$m
Reconciliation of profit to operating cash flows				
Profit/(loss) for the year	629.0	(341.0)	623.6	(336.9)
Adjusted for				
Net realised and unrealised (gains)/losses on investment assets	(539.5)	891.1	(399.7)	794.1
Change in life contract liabilities ¹	73.7	970.3	92.0	721.6
Change in operating assets and liabilities				
Decrease/(increase) in receivables	80.1	(104.4)	35.4	4.3
Decrease/(increase) in other assets	5.7	(3.6)	0.7	(1.0)
Increase/(decrease) in payables	46.2	91.2	8.6	(0.7)
Increase/(decrease) in life contract liabilities	1,015.0	(1,259.3)	1,535.7	(778.8)
Increase in external unit holders' liabilities	1,216.4	449.6	—	—
Increase/(decrease) in net tax liabilities	27.4	(148.6)	6.8	(132.0)
Net cash flows from operating activities	2,554.0	545.3	1,903.1	270.6

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

	Consolidated		Parent	
	30 June 2021	30 June 2020	30 June 2021	30 June 2020
	\$m	\$m	\$m	\$m
Reconciliation of cash				
Cash at bank	715.6	457.9	177.2	99.5
Cash at bank - SPV	60.8	58.0	—	—
Total cash and cash equivalents¹	776.4	515.9	177.2	99.5

¹ All cash and cash equivalents are considered current.

Accounting policy

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 2021		30 June 2020	
	No. of shares/notes m	Value of shares/notes \$m	No. of shares/notes m	Value of shares/notes \$m
Ordinary shares issued and fully paid				
Opening ordinary shares issued	1,966.5	1,966.5	1,696.5	1,696.5
New ordinary shares issued	30.0	30.0	270.0	270.0
Total ordinary shares issued and fully paid	1,996.5	1,996.5	1,966.5	1,966.5
Equity hybrid notes				
Opening equity hybrid notes	8.1	805.0	8.1	805.0
Hybrid notes issued	3.8	385.0	—	—
Hybrid notes repurchased	(3.2)	(317.2)	—	—
Total equity hybrid notes	8.7	872.8	8.1	805.0
Total contributed equity		2,869.3		2,771.5

Accounting policy

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.

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 the Australian Prudential Regulation Authority (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' (outlook stable) (30 June 2020: 'A' (outlook positive)).

Equity issue

In July 2020, CLC issued \$30.0 million of new fully paid ordinary shares as Common Equity Tier 1 capital.

In November 2020, CLC completed a new hybrid equity notes issue, raising \$385.0 million of funding, of which \$297.5 million was used to repurchase existing hybrid equity notes. The issue features similar structural characteristics to the existing notes. In May 2021, a further \$19.7 million of existing hybrid equity notes were repurchased.

The notes issuance was approved by APRA as qualifying as Additional Tier 1 capital of CLC and are classified as equity.

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.

CLC's internal capital models result in a target PCA ratio range under current circumstances of 1.3 to 1.7 times. This range can change over time and is dependent on numerous factors.

The PCA ratio at 30 June 2021 was 1.63 times (30 June 2020: 1.81 times), within this range of 1.3 to 1.7 times. The CET1 ratio was 1.14 times at 30 June 2021 down from 1.20 times at 30 June 2020.

Subordinated debt

CLC's total regulatory capital base includes \$405.4 million (30 June 2020: \$396.7 million) of admissible subordinated debt with a call date in November 2022.

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 2021 \$m	30 June 2020 \$m
CLC's excess capital under prudential standards		
Common Equity Tier 1 regulatory capital	2,971.2	2,337.0
Additional Tier 1 regulatory capital	872.7	805.0
Tier 2 regulatory capital – subordinated debt ¹	405.4	396.7
CLC total regulatory capital base	4,249.3	3,538.7
CLC's prescribed capital amount		
Asset risk charge ²	2,481.8	1,842.8
Insurance risk charge	227.0	199.5
Operational risk charge	57.9	56.5
Aggregation benefit	(167.4)	(144.8)
CLC prescribed capital amount	2,599.3	1,954.0
CLC excess over prescribed capital amount	1,650.0	1,584.7
Capital adequacy ratio (times)	1.63	1.81
Common Equity Tier 1 ratio (times)	1.14	1.20

¹ Differs from \$404.5 million (30 June 2020: \$395.7 million) disclosed in Note 14 Interest bearing financial liabilities due to \$0.9 million (30 June 2020: \$1.0 million) of accrued interest.

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

Note 14 Interest bearing financial liabilities

	30 June 2020 Facility	Opening balance	Cash flows Proceeds/ (repayments) ³	Non-cash movements Foreign exchange	Fair value changes	Other	30 June 2021 Closing balance	Facility
Consolidated ¹	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Bank loans								
Controlled property trusts ²	451.9	451.9	(17.5)	(45.9)	0.5	1.4	390.4	390.4
Controlled infrastructure trusts	185.8	185.8	(6.5)	—	—	—	179.3	179.3
Repurchase agreements ⁴	5,393.4	5,393.4	(1,282.3)	—	—	—	4,111.1	4,111.1
Total bank loans	6,031.1	6,031.1	(1,306.3)	(45.9)	0.5	1.4	4,680.8	4,680.8
Non-bank loans								
Subordinated debt ⁴	400.0	395.7	—	—	8.8	—	404.5	400.0
Other finance	0.7	0.7	—	—	—	—	0.7	0.7
Total non-bank loans	400.7	396.4	—	—	8.8	—	405.2	400.7
Total interest bearing financial liabilities	6,431.8	6,427.5	(1,306.3)	(45.9)	9.3	1.4	5,086.0	5,081.5
Current		5,417.8					4,308.8	
Non-current		1,009.7					777.2	
		6,427.5					5,086.0	

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 non-redraw loan facilities limits totalling \$390.4 million (30 June 2020: \$451.9 million).

³ Differs to Statement of cash flows due to \$53.8 million (30 June 2020: \$136.8 million) net repayments relating to SPVs. Total net cash proceeds comprise nil proceeds from borrowings (30 June 2020: \$944.9 million) and \$1,359.7 million (30 June 2020: \$171.2 million) repayments of borrowings, inclusive of SPVs.

⁴ Held by parent.

	30 June 2019 Facility	Opening balance	Cash flows Proceeds/ (repayments) ³	Non-cash movements Foreign exchange	Fair value changes	Other	30 June 2020 Closing balance	Facility
Consolidated ¹	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Bank loans								
Controlled property trusts ²	457.9	457.9	(15.7)	6.8	0.2	2.7	451.9	451.9
Controlled infrastructure trusts	192.0	192.0	(6.2)	—	—	—	185.8	185.8
Repurchase agreements ⁴	4,448.5	4,448.5	944.9	—	—	—	5,393.4	5,393.4
Total bank loans	5,098.4	5,098.4	923.0	6.8	0.2	2.7	6,031.1	6,031.1
Non-bank loans								
Subordinated debt ⁴	400.0	403.8	—	—	(8.1)	—	395.7	400.0
Other finance	13.2	13.2	(12.5)	—	—	—	0.7	0.7
Total non-bank loans	413.2	417.0	(12.5)	—	(8.1)	—	396.4	400.7
Total interest bearing financial liabilities	5,511.6	5,515.4	910.5	6.8	(7.9)	2.7	6,427.5	6,431.8
Current		4,473.2					5,417.8	
Non-current		1,042.2					1,009.7	
		5,515.4					6,427.5	

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 non-redraw loan facilities limits totalling \$451.9 million (30 June 2019: \$457.9 million).

³ Differs to Statement of cash flows due to \$136.8 million (30 June 2019: \$186.9 million) net repayments relating to SPVs. Total net cash proceeds comprise \$944.9 million (30 June 2019: \$632.8 million) proceeds from borrowings and \$171.2 million (30 June 2019: \$313.3 million) repayments of borrowings, inclusive of SPVs.

⁴ Held by parent.

Accounting policy

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 with movements on fair value recognised in the statement of comprehensive income. Repurchase agreements are all short-term in nature, and are therefore valued at amortised cost which approximates fair value.

Note 14 Interest bearing financial liabilities (continued)

Details of liabilities

Bank loans

Bank Loans	Type	Maturity	Rate type	Ranking/securitisation
Controlled property trusts ¹	Loan	June 2022 to October 2024	Variable	1) First ranking mortgages over Japanese investment properties: \$376.6 million (30 June 2020: \$424.7 million) 2) First ranking mortgage over County Court, VIC: \$13.7 million (30 June 2020: \$27.0 million)
Controlled infrastructure trusts ²	Facility	June 2022	Variable	First ranking mortgages over infrastructure assets

¹ Controlled property trusts consists of multiple loans with maturity dates from June 2022 to October 2024. At 30 June 2021 \$376.7 million (30 June 2020: \$424.9 million) of these loans are held at amortised cost. The fair value of these liabilities at 30 June 2021 is \$396.3 million (30 June 2020: \$474.9 million).

² These loans are held at amortised cost. The fair value of these liabilities at 30 June 2021 is \$182.3 million (30 June 2020: \$189.8 million).

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 2021 are current and all mature by August 2021. They will continue to be rolled into new agreements in the future.

Non-bank loans

Subordinated debt

The Group issued subordinated notes of \$400.0 million on 24 November 2017 with a call date on 24 November 2022. Holders of the subordinated notes have the option to convert their holding into ordinary shares of Challenger Limited on 24 November 2024 if CLC has not exercised its call option on 24 November 2022. If holders do not elect to convert the

subordinated notes to ordinary shares of Challenger Limited, the subordinated notes will be fully eligible as Tier 2 regulatory capital of CLC until 24 November 2038.

Other finance

Other finance included a limited recourse non-bank loan held for the financing of equipment of \$12.5 million that was repaid in December 2019.

Key estimates and assumptions

Subordinated debt valuation

Subordinated debt is recognised at fair value and is valued by reference to the ask price observable in the market at balance date.

The change recognised in the statement of comprehensive income in respect of valuation changes for the year ended 30 June 2021 was a loss of \$8.8 million (30 June 2020: gain of \$8.1 million).

Note 15 Reserves and retained earnings

	Consolidated		Parent	
	30 June 2021 \$m	30 June 2020 \$m	30 June 2021 \$m	30 June 2020 \$m
Foreign currency translation reserve¹				
Balance at the beginning of the year	1.3	(0.9)	—	—
(Loss)/gain on translation of foreign entities ²	(49.4)	1.7	—	—
Gain/(loss) on hedge of net investment in foreign entities ²	46.8	0.5	—	—
Balance at the end of the year	(1.3)	1.3	—	—
Adjusted controlling interests reserve¹				
Balance at the beginning of the year	5.7	7.8	—	—
Change in holdings in controlled entities	—	(2.1)	—	—
Balance at the end of the year	5.7	5.7	—	—
Cash flow hedge reserve – SPV¹				
Balance at the beginning of the year	0.1	0.1	—	—
Net loss on cash flow hedges	(0.5)	—	—	—
Balance at the end of the year	(0.4)	0.1	—	—
Other reserve				
Balance at the beginning of the year	132.3	132.3	137.8	137.8
Movement in distributable reserves	—	—	—	—
Balance at the end of the year	132.3	132.3	137.8	137.8
Total reserve	136.3	139.4	137.8	137.8
Retained earnings				
Balance at the beginning of the year	701.6	1,324.8	702.5	1,326.0
Profit attributable to equity holders	627.7	(336.6)	623.6	(336.9)
Dividends paid	(206.3)	(286.6)	(206.3)	(286.6)
Total retained earnings	1,123.0	701.6	1,119.8	702.5

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

² Net of tax

Accounting policy

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 2021	30 June 2020	30 June 2021	30 June 2020
	\$m	\$m	\$m	\$m
Interest expense	283.7	155.5	17.7	58.4
Interest expense – SPV	3.3	11.1	—	—
Interest expense – property trusts	5.3	6.1	—	—
Total finance costs	292.3	172.7	17.7	58.4

Accounting policy

Finance costs represent interest incurred on interest bearing financial liabilities (primarily external unit holders' liabilities distributions, repurchase agreements, 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 weighted average capitalisation rate to the expenditure on that asset.

Note 17 Dividends paid and proposed

	30 June 2021	30 June 2020
Parent	\$m	\$m
Unfranked dividends declared and paid during the year		
Ordinary shares:		
Final 30 June 2020 dividend: Nil (30 June 2019: 9.43 cents)	—	160.0
Interim 30 June 2021 dividend 8.51 cents (30 June 2020: 5.07 cents)	170.0	86.0
Equity hybrid notes	36.3	40.6
Total unfranked dividends declared and paid during the year	206.3	286.6
Unfranked dividends proposed (not recognised as a liability at 30 June)		
Ordinary shares	103.3	—
Total unfranked dividends proposed (not recognised as a liability at 30 June)	103.3	—

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 reasonably possible 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, inflation 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 Financial Risk Committee (FRC) and the Investment Committee (IC). The IC is a committee of investment professionals from within CLC and represents the first line. The FRC is a committee of professionals mainly from the Risk division that is independent of the investment team of CLC. The FRC represents the second line.

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, financial assets at fair value through profit and loss, payables, life 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 and other alternatives 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 shareholder 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 SPVs, the impact of a rising/falling bank bill swap rate (BBSW) 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 risk (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 point (1%) movements in interest rates would have a minimal impact on the Group's financial position.

	Change in variable	30 June 2021 Profit/(loss) \$m	30 June 2021 Change in equity \$m	30 June 2020 Profit/(loss) \$m	30 June 2020 Change in equity \$m
Non-SPV	+100 bps	1.7	1.7	0.8	0.8
	-100 bps	(1.7)	(1.7)	(0.8)	(0.8)
SPV	+100 bps	(0.2)	(0.2)	(0.3)	(0.3)
	-100 bps	0.2	0.2	0.3	0.3
Total	+100bps	1.5	1.5	0.5	0.5
	-100bps	(1.5)	(1.5)	(0.5)	(0.5)

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. Equity prices can be driven by a range of risk factors specific to an individual exposure including broad macroeconomic and instrument-specific factors which may be uncorrelated with broader equity markets. The Group's primary tools for managing investment price risks are the Internal Capital Adequacy Assessment Process (ICAAP) and the 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 small impact on the consolidated Group's financial position. It is assumed that the relevant change occurs as at the reporting date.

Equities and other alternatives	Change in variable	30 June 2021 Profit/(loss) \$m	30 June 2021 Change in equity \$m	30 June 2020 Profit/(loss) \$m	30 June 2020 Change in equity \$m
Property securities	+10%	6.2	6.2	5.3	5.3
	-10%	(6.2)	(6.2)	(5.3)	(5.3)
Infrastructure investments	+10%	7.8	7.8	3.9	3.9
	-10%	(7.8)	(7.8)	(3.9)	(3.9)
Other equities and alternative assets	+10%	108.7	108.7	55.5	55.5
	-10%	(108.7)	(108.7)	(55.5)	(55.5)
Total assets	+10%	122.7	122.7	64.7	64.7
	-10%	(122.7)	(122.7)	(64.7)	(64.7)

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) and policy liabilities. As at 30 June 2021, 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 \$146.9 million in respect of fixed income securities partially offset by an unrealised gain/loss of \$81.8 million in respect of policy liabilities (30 June 2020: \$102.9 million fixed income securities, \$77.8 million policy liabilities).

Currency risk

It is the Company's policy to minimise the exposure of 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 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 SPVs 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 2021					
Financial assets	765.3	1,997.8	1,164.2	385.6	574.6
Financial liabilities	(3.2)	(1,190.4)	(4.4)	—	—
Foreign currency contracts and cross currency swaps	(762.2)	(802.7)	(1,161.3)	(376.7)	(576.0)
Net exposure in Australian dollars	(0.1)	4.7	(1.5)	8.9	(1.4)
30 June 2020					
Financial assets	555.9	1,927.8	899.3	418.9	514.2
Financial liabilities	—	(648.8)	—	—	—
Foreign currency contracts and cross currency swaps	(555.5)	(1,248.0)	(896.9)	(405.5)	(513.6)
Net exposure in Australian dollars	0.4	31.0	2.4	13.4	0.6

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 continued to have been applied as it still reflects a reasonable measurement given the current level

of exchange rates and the volatility observed during the conditions created by the COVID-19 crisis. 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.

	Movement in variable against \$	30 June 2021 Profit/(loss) \$m	30 June 2021 Change in equity \$m	30 June 2020 Profit/(loss) \$m	30 June 2020 Change in equity \$m
British pound (GBP)	+10%	—	—	—	—
	-10%	—	—	—	—
US dollar (USD)	+10%	0.3	0.3	2.2	2.2
	-10%	(0.3)	(0.3)	(2.2)	(2.2)
Euro (EUR)	+10%	(0.1)	(0.1)	0.1	0.1
	-10%	0.1	0.1	(0.1)	(0.1)
Japanese yen (JPY)	+10%	—	0.6	—	0.9
	-10%	—	(0.6)	—	(0.9)
Other	+10%	(0.1)	(0.1)	—	—
	-10%	0.1	0.1	—	—
Total	+10%	0.1	0.7	2.3	3.2
	-10%	(0.1)	(0.7)	(2.3)	(3.2)

Note 18 Financial risk management (continued)

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. 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.

COVID-19 has led to a number of external and internal ratings downgrades and loan restructures and amendments.

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. grade	Other	Total
	AAA \$m	AA \$m	A \$m	BBB \$m			
30 June 2021							
Cash and cash equivalents	715.6	—	—	—	—	—	715.6
Cash and cash equivalents – SPV	60.8	—	—	—	—	—	60.8
Receivables	15.4	106.0	127.3	24.0	3.7	712.8	989.2
Mortgage assets – SPV	287.4	61.5	181.5	66.1	—	1.0	597.5
Finance leases	—	—	5.8	9.7	11.3	—	26.8
Fixed income securities	9,162.3	3,549.8	1,984.7	3,023.4	2,427.1	239.6	20,386.9
Derivative assets	—	582.2	51.6	96.5	—	—	730.3
Total assets with credit exposures	10,241.5	4,299.5	2,350.9	3,219.7	2,442.1	953.4	23,507.1
30 June 2020							
Cash and cash equivalents	457.9	—	—	—	—	—	457.9
Cash and cash equivalents – SPV	58.0	—	—	—	—	—	58.0
Receivables	27.7	41.7	58.2	21.6	5.9	637.5	792.6
Mortgage assets – SPV	349.9	67.2	123.4	161.7	—	—	702.2
Finance leases	—	—	11.4	7.3	13.0	—	31.7
Fixed income securities	11,308.4	1,189.9	2,113.0	2,474.7	2,114.5	274.4	19,474.9
Derivative assets	—	1,005.6	78.3	0.1	0.6	—	1,084.6
Total assets with credit exposures	12,201.9	2,304.4	2,384.3	2,665.4	2,134.0	911.9	22,601.9

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 the mortgage loans as this is borne by the RMBS holder.

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 primary risks and rewards associated with ownership of the property are held by the trustee on behalf of the RMBS holder.

Ageing of amortised cost financial assets

The table below gives information regarding the carrying value of the Group's financial assets measured at amortised cost. The analysis splits these assets by those that are not past due and those that are past due, including an ageing analysis at the statement of financial position date.

	Not past due \$m	Past due				Total \$m
		0-1 months \$m	1-3 months \$m	3-6 months \$m	6+ months \$m	
30 June 2021						
Receivables	983.9	0.8	0.4	0.3	3.8	989.2
Finance leases	26.8	—	—	—	—	26.8
30 June 2020						
Receivables	786.3	—	4.5	1.8	—	792.6
Finance leases	31.7	—	—	—	—	31.7

Note 18 Financial risk management (continued)

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 fair values, a counterparty failing on repayment of a contractual obligation, the inability to generate cash inflows as anticipated or an unexpected increase in cash outflows.

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 mandated actions depending on actual liquidity levels relative to those targets.

Detailed forecast cash positions are reported regularly to the Financial Risk Committee (FRC). The FRC and the Investment Committee (IC) replaced the CLC Asset Liability Committee (ALCo) from 1 July 2019. The IC is a committee of investment professionals from within CLC and represents the first line. The FRC is a committee of professionals mainly from the Risk division that is independent from the investment team of CLC. The FRC represents the second line for CLC. At the reporting date, all requirements of the liquidity management policy were satisfied.

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 2021					
Payables	1,688.6	5.1	27.4	—	1,721.1
Interest bearing financial liabilities	4,327.1	448.3	335.7	0.7	5,111.8
Interest bearing financial liabilities – SPV	166.6	214.0	120.1	133.4	634.1
External unit holders' liabilities	3,090.1	542.1	—	—	3,632.2
Life investment contract liabilities	3,356.7	2,948.9	459.6	372.2	7,137.4
Life insurance contract liabilities ¹	863.9	1,465.8	1,158.7	4,817.7	8,306.1
Derivative liabilities	46.0	58.3	96.4	222.8	423.5
Total undiscounted financial liabilities¹	13,539.0	5,682.5	2,197.9	5,546.8	26,966.2
30 June 2020					
Payables	1,519.6	5.1	20.1	27.9	1,572.7
Interest bearing financial liabilities	5,431.3	686.9	420.8	0.7	6,539.7
Interest bearing financial liabilities – SPV	139.9	260.6	147.1	170.2	717.8
External unit holders' liabilities	1,587.3	828.5	—	—	2,415.8
Life investment contract liabilities	2,966.4	2,325.5	542.5	427.0	6,261.4
Life insurance contract liabilities ¹	775.4	1,272.1	1,014.4	4,574.9	7,636.8
Derivative liabilities	97.1	48.7	80.7	383.7	610.2
Total undiscounted financial liabilities¹	12,517.0	5,427.4	2,225.6	5,584.4	25,754.4

¹ Disclosure of life insurance contract liabilities is not required under AASB7 *Financial Instruments: Disclosures*, 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 9 *Financial Instruments*.

- | | |
|---------|---|
| 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). |

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 and amount of cash flows, discount rates, earnings multiples and internal credit ratings.

Valuation techniques

The majority of the Group's listed and unlisted fixed income securities, over-the-counter derivative financial instruments and interest bearing liabilities including the new subordinated debt issuance are 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's derivative financial instruments are traded over-the-counter so, whilst they are not exchange traded, there is a market observable price. All of the listed fixed income 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 and are classified as Level 2. 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 generally 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.

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 set out below.

External unit holders' liabilities are valued at the face value of the amounts payable, being an approximation of fair value, 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 (classified as Level 3).

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 other short-term 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 carried at fair value 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)

Valuation process (continued)

	Consolidated			
	Level 1	Level 2	Level 3	Total
	\$m	\$m	\$m	\$m
30 June 2021				
Derivative assets	—	730.3	—	730.3
Fixed income securities ¹	—	18,512.1	1,874.8	20,386.9
Equities and other alternatives	1.2	1,187.5	155.0	1,343.7
Infrastructure investments ¹	—	—	345.4	345.4
Property securities	—	—	88.0	88.0
Investment and development property ²	—	396.0	3,389.7	3,785.7
Assets attributable to RIU - SPV ³	—	219.6	31.3	250.9
Total assets	1.2	21,045.5	5,884.2	26,930.9
Derivative liabilities	0.8	422.6	—	423.4
Interest bearing financial liabilities	—	418.2	—	418.2
External unit holders' liabilities	—	3,632.2	—	3,632.2
Life investment contract liabilities	—	47.2	6,183.2	6,230.4
Total liabilities	0.8	4,520.2	6,183.2	10,704.2
30 June 2020				
Derivative assets	—	1,084.0	0.6	1,084.6
Fixed income securities ¹	—	17,566.6	1,908.3	19,474.9
Equities and other alternatives	0.5	627.2	274.3	902.0
Infrastructure investments ¹	—	9.8	370.3	380.1
Property securities	—	—	76.3	76.3
Investment and development property ²	—	—	3,685.9	3,685.9
Assets attributable to RIU - SPV ³	—	254.2	45.1	299.3
Total assets	0.5	19,541.8	6,360.8	25,903.1
Derivative liabilities	—	610.2	—	610.2
Interest bearing financial liabilities	—	423.4	—	423.4
External unit holders' liabilities	—	2,415.8	—	2,415.8
Life investment contract liabilities	—	49.9	5,817.9	5,867.8
Total liabilities	—	3,499.3	5,817.9	9,317.2

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 Company assesses, at inception and at each reporting date, whether a structured entity should be consolidated based on the accounting policy. 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 2021, the carrying value of asset-backed financing assets was \$76.7 million (30 June 2020: \$91.1 million) with \$56.4 million undrawn commitments (30 June 2020: \$32.0 million) and securitisations were \$4,517.9 million (30 June 2020: \$5,386.5 million) with \$20.4 million undrawn commitments (30 June 2020: \$107.2 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.

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 2021		30 June 2020	
	Assets	Liabilities	Assets	Liabilities
	\$m	\$m	\$m	\$m
Balance at the beginning of the year	6,360.8	5,817.9	6,483.1	6,712.2
Fair value movements	(54.7)	95.2	(187.5)	135.7
Acquisitions	1,688.0	3,208.7	2,764.2	1,992.4
Maturities and disposals	(1,702.1)	(2,938.6)	(2,683.5)	(3,022.4)
Transfers to other categories ^{1,2}	(407.8)	—	(15.5)	—
Balance at the end of the year	5,884.2	6,183.2	6,360.8	5,817.9
Unrealised losses included in the statement of comprehensive income for assets and liabilities held at the statement of financial position date	(54.7)	(95.2)	(187.5)	(135.7)

¹ The Group transfers between levels of the fair value hierarchy when there is a change in the observability of the pricing inputs or a change to valuation methodology.

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. There were no transfers into Level 3 from Level 2 (30 June 2020: \$2.5 million) and \$407.8 million (30 June 2020: \$18.0 million) transfers out of Level 3 into Level 2 during the reporting period.

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 reasonably possible change in alternative assumptions in respect of the non-observable inputs into the fair value calculation.

	Level 3 value ¹	Positive impact	Negative impact		Reasonably possible change in non-observable input ^{2,3,4}
	\$m	\$m	\$m	Valuation technique	
30 June 2021					
Fixed income securities	1,874.8	13.5	(54.0)	Discounted cash flow	Primarily credit spreads
Equities and other alternatives	155.0	12.0	(13.0)	Discounted cash flow, external financial report	Mortality rate, 5% change in valuation
Infrastructure investments	345.4	4.3	(4.2)	Discounted cash flow, external financial report	Primarily discount rate on cash flow models
Property securities	88.0	4.4	(4.4)	External financial report	5% change in valuation
Life investment contract liabilities	(6,183.2)	2.4	(2.4)	Discounted cash flow	Primarily expense assumptions
Investment and development property	3,389.7	152.3	(124.9)	Market capitalisation, Discounted cash flow	Primarily capitalisation rate
Assets attributable to RIU – SPV	31.3	1.2	(1.3)	Discounted cash flow	Primarily prepayment rates
Total Level 3	(299.0)				
30 June 2020					
Derivative assets	0.6	—	—	Discounted cash flow	Primarily credit spreads
Fixed income securities	1,908.3	23.1	(74.9)	Discounted cash flow	Primarily credit spreads
Equities and other alternatives	274.3	18.8	(20.1)	Discounted cash flow, external financial report	Mortality rate, 5% change in valuation
Infrastructure investments	370.3	4.4	(4.3)	Discounted cash flow, external financial report	Primarily discount rate on cash flow models
Property securities	76.3	3.8	(3.8)	External financial report	5% change in valuation
Life investment contract liabilities	(5,817.9)	2.3	(2.3)	Discounted cash flow	Primarily expense assumptions
Investment and development property	3,685.9	165.3	(116.9)	Market capitalisation, Discounted cash flow	Primarily capitalisation rate
Assets attributable to RIU – SPV	45.1	1.7	(1.6)	Discounted cash flow	Primarily prepayment rates
Total Level 3	542.9				

¹ The fair value of the asset would increase/decrease if the credit spread, discount rate or expense assumptions decrease/increase or if other inputs increase/decrease. The fair value of the liability would increase/decrease if the discount rate decreases/increases or expense assumptions 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 reasonably possible alternative assumption was calculated by moving the credit band by one tier, adjusting the discount rates by between 50bps – 100bps, adjusting property capitalisation rates by 25bps (Australia) or 10bps (Japan), adjusting credit spreads by 50bps, changing the valuation of the unlisted schemes by 5% and adjusting the expense assumption allocation splits by 10%.

⁴ The changes in non-observable inputs at 30 June 2021 are unchanged from 30 June 2020.

Impact of COVID-19

The COVID-19 pandemic has had a significant impact on the economy and continues to drive uncertainty across the commercial property market. Independent valuers have noted these uncertainties in respect of the assumptions applied in the course of performing the independent valuation assessments for the direct property portfolio as at the reporting date. As a result of this uncertainty, a further sensitivity analysis has been undertaken to assess the impact on fair value when the significant non-observable input (capitalisation rates) experience a more material movement. Under this additional sensitivity scenario, the capitalisation rate is moved by 50bps (Australia) / 20bps (Japan), resulting in a positive impact of \$309.6 million and a negative impact of \$247.7 million across the direct property portfolio.

Fixed income also forms a material part of the Level 3 asset class held by the Group. This portfolio primarily consists of internally rated securities where the valuation is derived from applying the market observable comparable spread. The key non-observable inputs in these valuations are the internally derived credit ratings which are based upon credit assessments undertaken by the Risk division. The COVID-19 pandemic has impacted many businesses across various industries and the long-term effects are difficult to assess and not all industries and businesses have been impacted equally. An assessment of the current impact of COVID-19 on the performance of the Level 3 component of the fixed income portfolio has been undertaken and that performance has not changed sufficiently to warrant any additional sensitivity being included.

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 set out below.

Entity Name

839 Collins Trust	CLC Leveraged Loan Trust
Balloon Inflation Linked Bond Trust ²	Crown Domestic Sovereign Bond Trust ²
Challenger Adelaide Street Trust	GIR StatePlus Trust ²
Challenger Bourke Trust	Godo Kaisha Sub Tokumei Kumiai Two (Japan) ¹
Challenger Clarence Street Trust	Index Plus - Fiducian Enhanced Mandate Fund ²
Challenger Diversified Property Trust 1	Index Plus - IOOF Enhanced Mandate Fund ²
Challenger Golden Grove Trust	Index Plus - LGS Enhanced Mandate Fund ²
Challenger Index Plus Fund ²	Interstar Millennium Series 2006-1 Trust
Challenger Life OFI Trust	Kudu Investment Partners I, LP
Challenger Millennium Series 2013-1 Trust	Oaklands Hill Pty Ltd
Challenger North Rocks Trust	Specialised Finance Warehouse Tst 1 Series 2014-1
CLC Global High Yield Credit Trust	TLG Unit Trust

Unless otherwise stated, all material entities are incorporated in Australia, 100% owned and principal activity is to hold investments to support the life insurance business.

¹ Percentage holding is less than 100%.

² CLC consolidates the funds due to control over the trust and the existence of a total return swap. CLC has no percentage holding in the funds.

Accounting policy

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.

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. The Company assesses, at inception and at each reporting date, whether an entity should be consolidated based on the accounting policy.

All intercompany balances and transactions, including unrealised profits arising from intra-group transactions, are eliminated in full. Non-controlling interests represent the share in the net assets of subsidiaries attributable to equity interests not owned directly or indirectly by the Group.

The life 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.

Note 21 Related parties

Controlled entities and associates

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 and key executives

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

Directors

Peter Polson	Independent Chair
Richard Howes	Managing Director and Chief Executive Officer
John M Green	Independent Non-executive Director
Steven Gregg	Independent Non-executive Director
Heather Smith (appointed 20 January 2021)	Independent Non-executive Director
JoAnne Stephenson	Independent Non-executive Director
Duncan West	Independent Non-executive Director
Melanie Willis	Independent Non-executive Director

Key executives

Alexandra Bell (appointed 7 December 2020, retired 14 March 2021)	Acting Chief Financial Officer
Anthony Bofinger	Chief Risk Officer
Martin Considine (appointed 7 December 2020, retired 14 March 2021)	Appointed Actuary
Anton Kapel (retired 6 December 2020, reappointed 15 March 2021)	Chief Financial Officer and Appointed Actuary
Anton Kapel (appointed 7 December 2020, retired 14 March 2021)	Acting Principal Executive Officer
Anton Kapel (appointed 7 December 2020)	Acting Chief Investment Officer
Angela Murphy (appointed 15 March 2021)	Principal Executive Officer
Christopher Plater (retired 6 December 2020)	Principal Executive Officer and Chief Investment Officer

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.

	30 June 2021 \$	30 June 2020 \$
Consolidated and parent		
KMP compensation		
Short-term benefits	1,618,841	1,373,704
Post-employment benefits	50,055	38,544
Share-based payments	934,506	1,487,404
Total	2,603,402	2,899,652

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 reinsurance, investment management, transaction advisory, KMP compensation, 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 2021	30 June 2020	30 June 2021	30 June 2020
	\$m	\$m	\$m	\$m
Accounting and administrative services	101.3	96.6	101.3	96.6
Investment management and advisory fees	37.5	36.2	37.3	34.1
Realised hedge (receipts)/payments ¹	(13.4)	(9.7)	(13.4)	(9.7)

¹ The Company hedges certain foreign exchange and interest rate exposures with transactions with Challenger Treasury Limited. The fair value at 30 June 2021 was a loss of \$21.9 million (30 June 2020: gain of \$91.8 million).

At 30 June 2021, amounts recoverable from related entities were \$207.0 million (30 June 2020: \$265.9 million) and \$235.8 million (30 June 2020: \$282.6 million) for the consolidated group and parent respectively, and amounts payable to related entities were \$50.9 million (30 June 2020: nil) and \$179.2 million (30 June 2020: \$95.4 million) for the consolidated group and parent respectively.

Loans to Directors and key executives

There were no loans made to Directors or key executives as at 30 June 2021 (30 June 2020: nil).

Group products

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

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 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

	30 June 2021	30 June 2020
Consolidated	\$m	\$m
Goodwill¹	69.4	69.4

¹ All goodwill is considered non-current. The parent has \$69.4 million of goodwill (30 June 2020: \$69.4 million).

Accounting policy

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. Goodwill has an indefinite useful life.

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.

Key estimates and assumptions

Goodwill recoverable amounts

The Group assesses whether goodwill is impaired at least annually in accordance with its accounting policy. The recoverable amount of the cash-generating unit is determined based on value in use calculations, that utilise cash flow projections based on financial forecasts approved by senior management which cover an appropriate horizon. In determining these cash flow projections management considers:

- current and expected performance of the CGU;
- Board and management approved budgets and strategic plans; and

- changes in Australian and international economic and market environments.

The impact of COVID-19 has had a profound effect on economies and markets. In addition, the duration and extent of the pandemic together with government responses to it remains uncertain. Notwithstanding, management has made reasonable assumptions of the impact of COVID-19 when determining the cash flow projections to be used for the value in use calculations.

The cash flow projections determined by management are discounted using an appropriate discount rate. The determination of the discount rate is a matter of judgement and is based on a number of factors including a theoretical calculation, observation of third party reports and discount rates used by comparable financial services companies.

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

- the budgeted net profit after tax for the CGU for each year within the cash flow projection period;
- the discount rate; and
- growth rates, which are consistent with long-term trends in the industry segments in which the CGU operates.

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

Impairment testing of goodwill

The following represent the carrying amounts of goodwill.

CGU	Discount rate				Cash flow horizon (years)
	30 June 2021	30 June 2020	30 June 2021	30 June 2020	
	\$m	\$m	%	%	
CLC	69.4	69.4	10.2	10.0	5

The cash flow projections derived a value for the Group that was in excess of the net assets inclusive 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% or a change in projected cash flows of 5%, would not cause the respective recoverable amounts for the Group to fall below the carrying amounts as at 30 June 2021. All goodwill is non-current.

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 2021. 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 2021, there are potential future commitments totalling \$867.9 million (30 June 2020: \$419.7 million) in relation to these opportunities. Contractual obligations for future property repairs and maintenance are in place but cannot be quantified until required.

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 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 volumes.

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.

Other contracted commitments

This represents amounts payable in relation to fitout commitments and acquisition of investment properties that have exchanged prior to the balance date and will settle subsequent to the balance date.

	30 June 2021 \$m	30 June 2020 \$m
Analysis of credit commitments		
Contracted capital expenditure		
Amounts due in less than one year	2.6	18.7
Amounts due between one and two years	0.8	0.8
Amounts due between two and five years	2.9	—
Amounts due in greater than five years	7.3	—
Total capital expenditure commitments	13.6	19.5
Non-cancellable operating leases – Group as lessor		
Amounts due in less than one year	(219.8)	(221.0)
Amounts due between one and two years	(174.5)	(213.5)
Amounts due between two and five years	(412.8)	(511.3)
Amounts due in greater than five years	(784.3)	(954.3)
Total operating leases – Group as lessor	(1,591.4)	(1,900.1)
Other contracted commitments		
Amounts due in less than one year	—	6.2
Total other contracted commitments	—	6.2
Net commitments	(1,577.8)	(1,874.4)

Note 24 Statutory fund information

Life insurance funds

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
	Non-linked superannuation business	Performance annuity bonds ¹	Insurance contract
2	Non-linked superannuation business	Fixed-rate annuity	Investment contract
		Lifetime annuity	Insurance contract
		Allocated pension	Investment contract
		Personal super	Investment contract
	Non-linked ordinary business	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 ordinary business	Fixed-rate annuity	Investment contract ²
		Lifetime annuity	Insurance contract

¹ These products are non-investment linked per the Life Act definitions.

² 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	Statutory Fund No.2	Statutory Fund No.3	Statutory Fund No.4	Statutory Fund Total	Shareholder Fund	Total
2021	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Life insurance premiums	—	812.5	—	788.1	1,600.6	—	1,600.6
Change in contract liabilities and other revenue	—	(245.9)	(0.4)	(345.9)	(592.2)	—	(592.2)
Investment income ¹	0.1	1,198.7	0.6	0.9	1,200.3	367.1	1,567.4
Revenue¹	0.1	1,765.3	0.2	443.1	2,208.7	367.1	2,575.8
Life insurance claims	(0.1)	(494.0)	—	(358.3)	(852.4)	—	(852.4)
Policy liability related expenses	—	(216.7)	—	(13.0)	(229.7)	—	(229.7)
Other operating expenses ¹	—	(257.0)	—	(48.7)	(305.7)	(13.7)	(319.4)
Total Expenses¹	(0.1)	(967.7)	—	(420.0)	(1,387.8)	(13.7)	(1,401.5)
Finance costs	—	(21.8)	—	—	(21.8)	(270.5)	(292.3)
Profit before tax	—	775.8	0.2	23.1	799.1	82.9	882.0
Income tax (benefit)/expense	—	(221.7)	(0.1)	(7.1)	(228.9)	(24.1)	(253.0)
Profit for the year	—	554.1	0.1	16.0	570.2	58.8	629.0
Profit attributable to non-controlling interest	—	1.3	—	—	1.3	—	1.3
Profit attributable to equity holders	—	552.8	0.1	16.0	568.9	58.8	627.7
2020							
Life insurance premiums	—	450.1	—	742.6	1,192.7	—	1,192.7
Change in contract liabilities and other revenue	0.1	(20.7)	—	(496.5)	(517.1)	—	(517.1)
Investment income ¹	0.2	343.0	0.1	(26.8)	316.5	(38.4)	278.1
Revenue¹	0.3	772.4	0.1	219.3	992.1	(38.4)	953.7
Life insurance claims	—	(483.8)	—	(265.8)	(749.6)	—	(749.6)
Policy liability related expenses	—	(213.9)	—	(9.0)	(222.9)	—	(222.9)
Other operating expenses ¹	—	(263.2)	—	(40.9)	(304.1)	(3.0)	(307.1)
Total Expenses¹	—	(960.9)	—	(315.7)	(1,276.6)	(3.0)	(1,279.6)
Finance costs	—	(63.6)	—	—	(63.6)	(109.1)	(172.7)
Profit before tax	0.3	(252.1)	0.1	(96.4)	(348.1)	(150.5)	(498.6)
Income tax expense	(0.1)	83.4	—	28.9	112.2	45.4	157.6
Profit/(loss) for the year	0.2	(168.7)	0.1	(67.5)	(235.9)	(105.1)	(341.0)
Loss attributable to non-controlling interest	—	(4.4)	—	—	(4.4)	—	(4.4)
Profit attributable to equity holders	0.2	(164.3)	0.1	(67.5)	(231.5)	(105.1)	(336.6)

¹ Differs to consolidated amounts disclosed in the Statement of comprehensive income by \$11.4 million due to the elimination of inter-group transactions (30 June 2020: \$17.1 million).

Note 24 Statutory fund information (continued)

Disaggregated information by statutory fund (continued)

Abbreviated statement of financial position 30 June 2021	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	1.4	621.0	2.4	84.4	709.2	67.2	776.4
Investment assets ¹	4.1	20,033.1	3.8	2,360.9	22,401.9	5,646.2	28,048.1
Other assets	—	354.8	(0.6)	46.6	400.8	676.3	1,077.1
Total assets¹	5.5	21,008.9	5.6	2,491.9	23,511.9	6,389.7	29,901.6
Life contract liabilities ¹	1.5	12,352.9	3.0	2,083.1	14,440.5	—	14,440.5
Other liabilities	—	5,710.2	0.3	35.3	5,745.8	5,574.2	11,320.0
Total liabilities¹	1.5	18,063.1	3.3	2,118.4	20,186.3	5,574.2	25,760.5
Net assets	4.0	2,945.8	2.3	373.5	3,325.6	815.5	4,141.1
Contributed equity	—	—	—	—	—	2,869.3	2,869.3
Reserves	1.6	(144.1)	0.8	406.0	264.3	(128.0)	136.3
Retained earnings	2.4	3,077.4	1.5	(32.5)	3,048.8	(1,925.8)	1,123.0
Non-controlling interests	—	12.5	—	—	12.5	—	12.5
Total equity	4.0	2,945.8	2.3	373.5	3,325.6	815.5	4,141.1

Abbreviated statement of financial position 30 June 2020	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	1.6	438.5	2.3	29.6	472.0	43.9	515.9
Investment assets ¹	4.0	19,406.8	3.3	1,981.4	21,395.5	4,440.1	25,835.6
Other assets	—	1,329.3	(0.5)	144.2	1,473.0	168.0	1,641.0
Total assets¹	5.6	21,174.6	5.1	2,155.2	23,340.5	4,652.0	27,992.5
Life contract liabilities ¹	1.5	11,086.3	2.6	1,722.6	12,813.0	—	12,813.0
Other liabilities	0.1	7,522.9	0.3	125.0	7,648.3	3,906.9	11,555.2
Total liabilities¹	1.6	18,609.2	2.9	1,847.6	20,461.3	3,906.9	24,368.2
Net assets	4.0	2,565.4	2.2	307.6	2,879.2	745.1	3,624.3
Contributed equity	—	—	—	—	—	2,771.5	2,771.5
Reserves	1.6	29.2	0.8	356.0	387.6	(248.2)	139.4
Retained earnings	2.4	2,524.4	1.4	(48.4)	2,479.8	(1,778.2)	701.6
Non-controlling interests	—	11.8	—	—	11.8	—	11.8
Total equity	4.0	2,565.4	2.2	307.6	2,879.2	745.1	3,624.3

¹ Differs to consolidated amounts disclosed in the Statement of financial position by \$770.6 million due to the elimination of life contract liabilities and investment assets held within the Group (30 June 2020: \$231.8 million).

Note 24 Statutory fund information (continued)

Disaggregated information by statutory fund (continued)

Capital adequacy 30 June 2021	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	4.0	2,933.3	2.3	373.5	3,313.1	815.5	4,128.6
Regulatory adjustments	—	(201.4)	—	(14.7)	(216.1)	(68.6)	(284.7)
Tier 1 regulatory capital	4.0	2,731.9	2.3	358.8	3,097.0	746.9	3,843.9
Tier 2 capital ²	—	405.4	—	—	405.4	—	405.4
Capital base	4.0	3,137.3	2.3	358.8	3,502.4	746.9	4,249.3
Prescribed capital amounts components							
Insurance risk charge	0.1	221.2	—	5.6	226.9	0.1	227.0
Asset risk charge	0.3	1,607.6	0.2	61.4	1,669.5	142.3	1,811.8
Operational risk charge	—	51.6	—	6.3	57.9	—	57.9
Default stress	—	7.4	—	1.7	9.1	4.7	13.8
Aggregation benefit	(0.1)	(162.9)	—	(4.3)	(167.3)	(0.1)	(167.4)
Combined stress scenario adjustment	0.2	565.4	0.1	27.5	593.2	63.0	656.2
Prescribed capital amount	0.5	2,290.3	0.3	98.2	2,389.3	210.0	2,599.3
Capital adequacy multiple	8.0	1.4	7.7	3.7	1.5	3.6	1.6

Capital adequacy 30 June 2020	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	4.0	2,553.8	2.2	307.6	2,867.6	745.1	3,612.7
Regulatory adjustments	—	(385.3)	—	(22.7)	(408.0)	(62.7)	(470.7)
Tier 1 regulatory capital	4.0	2,168.5	2.2	284.9	2,459.6	682.4	3,142.0
Tier 2 capital ²	—	396.7	—	—	396.7	—	396.7
Capital base	4.0	2,565.2	2.2	284.9	2,856.3	682.4	3,538.7
Prescribed capital amounts components							
Insurance risk charge	0.2	189.8	—	9.5	199.4	0.1	199.5
Asset risk charge	0.3	1,208.8	0.1	32.9	1,242.1	66.2	1,308.3
Operational risk charge	—	50.8	—	5.7	56.5	—	56.5
Default stress	—	14.5	—	0.9	15.4	2.9	18.3
Aggregation benefit	(0.1)	(138.1)	—	(6.4)	(144.6)	(0.2)	(144.8)
Combined stress scenario adjustment	0.1	470.8	—	15.8	486.7	29.5	516.2
Prescribed capital amount	0.5	1,796.6	0.1	58.4	1,855.5	98.5	1,954.0
Capital adequacy multiple	8.0	1.4	22.0	4.9	1.5	6.9	1.8

¹ Net assets includes additional tier 1 capital.

² Differs from the \$404.5 million (30 June 2020: \$395.7 million) disclosed in Note 14 Interest bearing financial liabilities due to \$0.9 million (30 June 2020: \$1.0 million) accrued interest.

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

At the date of this report 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:

1. 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:
 - (a) giving a true and fair view of the Group's financial position as at 30 June 2021 and of its performance for the year ended on that date; and
 - (b) complying with Australian Accounting Standards (including the Australian Accounting Interpretations) and the **Corporations Regulations 2001**;
2. the financial statements and notes of the Group also comply with International Financial Reporting Standards as issued by the International Accounting Standards Board which is disclosed in Section 1(i) Basis of preparation and statement of compliance;
3. 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
4. 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 2021.

On behalf of the Board



P Polson
Independent Chair

Sydney
9 August 2021



R Howes
Managing Director and Chief Executive Officer

Sydney
9 August 2021



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 to the Shareholder 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 Group consolidated and Company statements of financial position as at 30 June 2021;
- the Group consolidated and Company statements of comprehensive income, statements of changes in equity and 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 is in accordance with the *Corporations Act 2001*, including:

- a) giving a true and fair view of the Company's and the Group's financial position as at 30 June 2021 and of their 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 (including Independence Standards)* (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.

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 2021 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 and Group'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 Group or to cease operations, or have no realistic alternative but to do so.

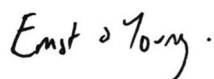
Auditor's Responsibilities for the Audit of the Financial Report

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 judgment 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 Company's or 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 Company's or 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 Company or 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.



Ernst & Young



Graeme McKenzie

Partner

Sydney

9 August 2021

Additional information

Principal place of business and registered office in Australia

Level 2
5 Martin Place
Sydney NSW 2000
Telephone: 02 9994 7000
Facsimile: 02 9994 7777

Directors

Peter Polson (Independent Chair)
Richard Howes (Managing Director and Chief Executive Officer)
John M Green
Steven Gregg
Heather Smith
JoAnne Stephenson
Duncan West
Melanie Willis

Company secretary

Linda Matthews

Website

› challenger.com.au

Auditor

Ernst & Young
200 George Street
Sydney NSW 2000