



Challenger Limited
Annual Report 2011



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Award-winning annuities

In 2011 Challenger was again named winner of the AFA/Plan for Life 'Annuity Provider of the Year', further reinforcing our strength in the annuity market.

Challenger today

Challenger Limited is an ASX-listed investment management firm established in 1985. We are the leading issuer of annuities in Australia and provider of alternative retirement income solutions. Through our Boutique Partnership and Aligned Investment Funds Management teams, we are a leading provider of investment products in Australia.

Life

Challenger is a leading provider of annuities and alternative retirement income solutions in Australia. Via an Australian Prudential Regulation Authority ('APRA') regulated life company, we offer attractive returns and capital protection for our customers, making our annuities well suited to retirement income planning. Annuity premia, along with shareholder and other capital, are invested in a diversified portfolio of assets to deliver predictable, long-term cash flows to meet commitments to our annuitants while providing attractive returns for shareholders.

Funds Management

As one of Australia's established and fast growing funds management businesses, Challenger offers a wide range of fiduciary investment choices across a variety of asset classes and investment styles. Through Aligned Investment teams, we manage assets for Challenger Life and third party investors. Through our Boutique Partnership platform, we partner with a diverse array of independent fund managers in which we own equity stakes and provide distribution and administration support.

Results at a glance

‘Record retail Life sales and growing funds under management in 2011 delivered strong financial performance, with increased profit and earnings per share, a solid capital position and greater returns for shareholders.’

Key financial highlights during the year:

- Normalised net profit after tax (NPAT) up 7% to \$248m
- Normalised earnings per share (EPS) up 14% to 51.7 cents per share
- Cost to income ratio down a further four percentage points to 37%
- Record sales of Life products of \$1.96bn, more than double the 2010 sales
- Total funds under management of \$27.9bn up 17%
- Final dividend of 9.5 cents per share declared, bringing full year dividend to 16.5 cents per share (unfranked), up 14%.

Financial performance	2011	2010
Net income	\$494m	\$448m
Expenses	\$180m	\$182m
Normalised NPAT	\$248m	\$233m
Statutory NPAT	\$261m	\$283m
EPS (normalised basic) – cents per share	51.7	45.5
EPS (statutory basic) – cents per share	54.5	55.3

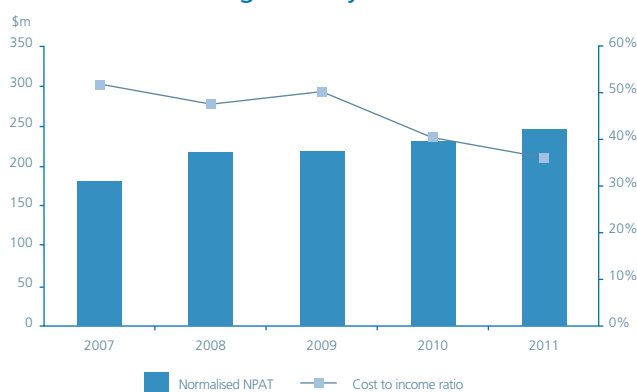
Normalised profit explained

Challenger is required by accounting standards to value all assets and liabilities supporting the life insurance business at fair value. This can give rise to fluctuating valuation movements being recognised in the income statement. As Challenger is fundamentally a long-term holder of assets, due to them being held to match the term of Challenger's annuity and life contract obligations, a large proportion of the gains and losses recognised in the income statement in any one period are unrealised and are expected to reverse over time.

Investment experience is a mechanism employed to remove the volatility arising from asset and liability valuation from the results so as to reflect more accurately the underlying performance of Challenger. The difference between the actual investment gains/losses (both realised and unrealised) and the normalised gains/losses (being Challenger's expected long-term return) plus any actuarial assumption changes for the period is referred to as 'investment experience'.

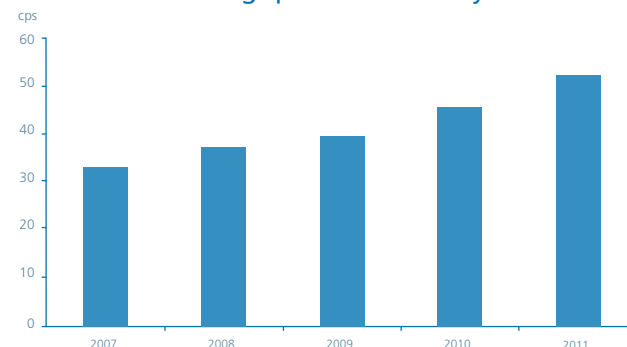
The investment experience is reported separately from normalised profit in order to provide a better understanding of Challenger's normalised financial results for the period. It is this normalised profit that underpins distributions to shareholders in the form of cash dividends.

Normalised earnings – five years



Normalised NPAT has continued its upward trajectory. We have successfully grown our net income while keeping expenses down, resulting in our cost to income ratio falling to 37% in 2011, within our 35-40% targeted range.

Normalised earnings per share – five years



Since 2007, we have continued our growth profile. Normalised earnings per share have consistently grown over 5 years.

Sources of income

Life derives its income by achieving a higher rate of return from its diversified portfolio of investments than the returns it has committed to pay to annuity policy holders. Total income is a factor of the size of the portfolio managed multiplied by the income received from those invested assets. Income has risen across the year as the size of the portfolio of assets grew in line with increased sales of annuities and increased yields on investment assets.

Funds Management is a fiduciary manager of third party capital, so its income is calculated as a margin or percentage of total funds under management (FUM). Additional income is earned from certain assets in the form of performance and transaction fees. From its co-ownership in boutique funds, it earns distribution and administration fees, as well as a share of profits from the boutique partnership.

Chairman's report

'This year saw continued growth and momentum in Challenger's business, delivering quality products for customers and strong returns for shareholders.'

After establishing a strong base for the business and a clear strategy during the last few years, 2011 saw us continue to deliver on this well-defined strategic focus in the retirement income market. All of the tailwinds that I spoke of last year are continuing through increased retirement flows and growing demand from retirees seeking simpler, secure investment products that provide a balance in their superannuation savings.

To further take advantage of our position, we created a new corporate division: Distribution, Product and Marketing. It is designed to provide a more cohesive support platform for our growing businesses. We have launched a major consumer advertising campaign and expanded the number of employees in our sales and distribution team.

Your Board and management are confident in our abilities to participate in the retirement income market, organically grow our share and increase returns for shareholders.

Full year result to 30 June 2011

During the year, Challenger again saw a continued rise in its normalised net profit after tax to \$248m, up 7% on 2010 and backed by an underlying operating cash flow of \$276m. Normalised earnings of 51.7 cents per share represented a 14% increase on 2010, reflecting stronger earnings, as well as accretion from the on-market share buy-back approved by shareholders at our 2010 Annual General Meeting.

Statutory net profit ended the year above normalised profit at \$261m. Statutory net profit was impacted by some negative investment experience due to periods of volatility in investment and financial markets, offset by a positive resolution of historical matters with the Australian Taxation Office in May 2011.

Consistent with prior years, we continue to direct shareholders to our normalised earnings, as this better represents the underlying operating performance of the Company. We have increased the disclosure around normalised and statutory earnings to provide a clearer explanation for shareholders. This can be found on pages 30 to 31 of the Directors' report.

In our regulated Life Company, capital levels remained strong, finishing the year with a surplus over regulatory minimums in excess of \$675m.

Dividend

Your Board has declared a final dividend of 9.5 cents per share, bringing the total dividend for shareholders to 16.5 cents per share across the year. This is an increase of 14% from 2010 and in line with our targeted dividend payout ratio of around 30% of normalised earnings.

Risk management

Risk management is a key area of our business. In providing guaranteed returns to our customers we need to ensure that not only do we have the appropriate risk frameworks and governance structures in place to manage the resulting market, interest rate, credit, liquidity and foreign exchange risk, but also the right people. It is a testament to our talented management team, and its strong risk management skills and experience, that our business has weathered some of the most testing financial environments in decades. As we continue to build and grow our retirement income franchise, the skills and experience we seek in management will not diminish. The management of risk within our regulatory framework will remain a key focus for your Board.

Board changes

During the year, we again reviewed the effectiveness of your Board and reflected on the skills, duties and obligations required of its members. Against this background, we decided that we would increase the number of Directors to ensure that we can continue to provide a high standard of strategic advice and corporate governance. We are pleased to welcome Brenda Shanahan, who joined the Board in April 2011. Brenda brings substantial skills and experience in the financial services sector and expands the diversity of your Board.

Outlook

After several years of change and refinement, Challenger is well placed through a leading and differentiated business model to participate in the growing retirement income market and the fast developing boutique funds management industry. We are positioned to expand our distribution footprint, broaden our product development, and importantly, continue to deliver value for shareholders.



Peter Polson

Chairman



CEO's report

'Challenger is well placed to execute its retirement income strategy via its growing annuity franchise, supported by structural market changes.'

Business performance

Consistent with the last few years, 2011 saw our business experience significant growth, which in turn has driven record financial results. Total assets under management rose 17% across the year as the momentum in sales of annuities and other retail products continued unabated. Sales in the last quarter of 2011 were our strongest organic flows in a number of years. At the same time, assets under management have been positively impacted by net inflows of \$3.9bn to our stable of Boutique Partnerships in our Funds Management business.

Normalised net profit after tax rose 7% to \$248m, but more importantly our normalised earnings per share rose 14% to 51.7 cents per share, reflecting ongoing accretion achieved via our on-market share buy-back approved by shareholders at last year's Annual General Meeting.

Expenses reduced slightly during the year and, coupled with strong revenue growth of 10%, the cost to income ratio reduced again by a further four percentage points to 37%. Over the medium term we expect to remain within a cost to income range of 35-40%.

The statutory net profit after tax was marginally higher than normalised net profit. Negative investment experience for the year was offset by the settlement with the Australian Taxation Office in relation to the tax treatment of certain matters from prior years. Interest and borrowing costs fell during the year. At year-end we had no group recourse debt outstanding and a net cash balance of \$93m.

Operational and financial highlights

- Record financial performance again allowed us to increase our dividend to 16.5 cents per share for the full year, up 14% on 2010.
- Sales of annuities and guaranteed income products by our Life business increased to \$1.96bn, more than double the sales achieved in 2010.

- We launched our first major consumer advertising campaign across television, newspapers and online, labelled 'Real Stories' to drive and support growth for our retirement income franchise.
- We experienced growth in funds under management for our Boutique Partnership business in Funds Management, reaching \$14.8bn at 30 June 2011, more than double the balance last year.
- Capital levels, surplus to our regulatory requirements in our Life company, remain solid at more than \$675m. As the sales momentum for annuities increases, the surplus offers significant headroom to support organic book growth.
- Our financial flexibility remains strong, with no recourse debt outstanding and a net cash position of \$93m. Operating cash flow also remained strong at \$276m, up 25% on 2010.

Capital management

At the Annual General Meeting in November 2010, shareholders approved a new on-market share buy-back. Under this approval, we acquired a further 9.1m shares at an average price of \$4.73. Since we initiated an on-market share buy-back in mid-2008, we have bought back and cancelled 123m shares at an average price of \$3.22. Acquiring these shares at a discount to the current market price has delivered significant accretion in earnings per share for shareholders.

Structural market changes and environment

Our business operates in a segment of the market, retirement income, which is supported by many structural changes. In the retirement income segment our targeted demographic, 65 years+, will grow almost four times faster than the pre-retirement demographic. 2010 was a pivotal year for retirees, as the first of the baby-boomers born since 1945 began to enter retirement phase. According to Rice Warner, in 2010 nearly \$48bn transferred from accumulation to retirement.

Today our market share of those flows is around 3% and growing. We believe we are at the beginning of a long-term structural shift in the demand for our products that has only just begun to emerge.

Strategy and outlook

Much of the work we have undertaken during the year has been operational to support our conviction of the importance of a focused strategy that leverages structural and regulatory tailwinds in the retirement income market. This saw the creation of a new corporate segment: Distribution, Product and Marketing, which is focused on improving the co-ordination in these key areas. This area is both driving and supporting our sales efforts, in retirement income and our Boutique Partnerships, and centralising data capture and analytics for our business. It has also been instrumental in the roll-out of our first major consumer advertising campaign, which launched in February 2011.

Our fiduciary Funds Management business continues on a strong trajectory, building out leading and differentiated Boutique Partnerships to target the growing superannuation pool, with funds under management for the Boutique Partners more than doubling this year to \$14.8bn. Within our Aligned Investment business, we have been awarded substantial mandates from industry funds and sovereign wealth funds during the year. Whilst investment markets have continued to see periods of volatility, which can be unsettling, the result is an increase in the risk premium and asset returns in the economy, ideal conditions for the reinvestment of assets backing our annuity portfolio.

The coming years will be an exciting time as we leverage structural market trends and continue to roll out our retirement income strategy in Australia.



Dominic Stevens
Chief Executive Officer



Life and Funds Management

Richard Howes

Chief Executive Life

Our APRA-regulated Life business is the pre-eminent provider of annuities in Australia, with our annuities capturing approximately 3% of the superannuation money that moves from accumulation to retirement each year. At 30 June 2011, the Life Company owned \$8.4bn of assets (up 11% over the last 12 months), supporting policy liabilities of \$5.6bn and institutional guaranteed return products of \$1.3bn.

The first of Australia's 'baby-boomers' reached retirement age during 2010. This, together with a growing realisation that Australia's equity-centric allocated pensions are too risky in isolation to deliver reliable retirement income, represents secular changes that are driving growth for our guaranteed retirement income products. We have seen an acceleration in demand for our core products of annuities, fixed rate allocated pensions and personal superannuation, with organic sales up 56% over the year to \$1,460m. New products such as our Guaranteed Income Fund, a unitised annuity sold via investment wrap platforms, our Liquid Lifetime annuity and our commission-free annuity accounted for 35% of this year's sales.

Along with this strong growth we were able to generate normalised cash operating earnings of \$401m, up \$63m or 19% on 2010. A contributor to this outcome has been the persistence of attractive asset returns.

Ongoing market volatility and increased regulatory pressure on banks lead us to expect that these returns will remain attractive for the foreseeable future.

In 2011, expenses rose just over \$18m as we continued to invest heavily in expanding our sales footprint with increased advertising and marketing, dedicated distribution teams, new product development and creating technology applications to assist financial planners in selling our product. Resulting EBIT of \$349m was up 15% on 2010.

Broader investment markets have experienced some volatility, particularly in equities, but in our core asset classes of fixed income, property and infrastructure we have benefited from an ongoing overall recovery.

Asset values increased across our fixed income and property assets, but a weaker outcome in infrastructure resulted in negative investment experience of \$29m post tax.

Our capital position continued to strengthen over the year, ending with surplus capital to regulatory minimums in excess of \$675m, up from a surplus position of approximately \$630m at June 2010.

In early 2011, the Life Company made an offer to acquire 100% of the units in the Challenger High Yield Fund (HYF). In return, existing HYF unit holders received a combination of cash and units in a new fund called the Challenger Guaranteed Income Fund, a registered managed investment scheme that invests in an annuity issued by the Life Company. The offer was accepted on 25 February 2011, and delivered an increase in investment assets of approximately \$550m and a broadening of our annuity client base.

Near the end of the financial year, the Life Company also acquired its first infrastructure asset in Australia via an interest in a wind farm in Victoria for a consideration of approximately \$40 million.

Rob Woods

Chief Executive Funds Management

Our Funds Management operations have developed significantly over the year, as we completed the transformation whereby all our investment activities now have a strong and tangible alignment with our clients. The business is well placed to benefit from the Government's decision to increase compulsory superannuation contributions from 9% to 12% over the next 10 years. Further, our strategy offers clients a broad offering, with investment management expertise in the equity, fixed income, property and infrastructure asset classes.

Total funds under management increased across the year to \$23.6bn, up 17%, while net flows for our Boutique Partnerships reached \$3.9bn, up significantly on 2010. Both net income and expenses fell during the year as we removed a number of our internally managed funds from our earnings and created new Boutique Partnerships. Pleasingly, the result was an improved EBIT contribution of \$20m, up 16% on 2010.

The Aligned Investment team develops and manages products under the Challenger brand for third party investors as well as for Challenger's Life business. This includes ASX-listed fund Challenger Diversified Property Group (CDI), as well as a number of large unlisted mandates with institutional investors.

CDI has performed strongly during the year, improving the quality of its portfolio with the acquisition of 31 Queen Street in Melbourne. Its net asset value (NAV) rose 2% versus June 2010 as property values increased. Challenger Infrastructure Fund (CIF) continues to focus on maximising value from its two core assets Inexus and LBC. It has a sound capital structure with no fund borrowings and a strong cash position to fund future growth and support refinancing of its core assets. Challenger Wine Trust (CWT) was privatised and delisted in early 2011, following an offer to acquire units by CK Life Sciences. Challenger Life remains an investor alongside CK Life Sciences in CWT and the Aligned Investment team continues to manage the now unlisted portfolio of properties for both investors.

On the unlisted mandate side, the fixed income and real estate teams worked closely to originate investments in the commercial property debt sector for major industry funds and sovereign wealth funds.

Our Boutique Partnership operations comprise co-owned, separately branded investment managers, to which Challenger provides administration and distribution services. In 2010, four new managers were added to the stable, taking the total number of Boutique Partnerships to 10. 2011 saw us focus on our distribution efforts across all boutiques, with the total funds under management doubling over the year to just under \$15bn by year-end.

We see the Boutique Partnership offering growing more quickly than the broader funds management market, providing scale synergies and therefore playing a strategic role in our business.



Rob Woods and Richard Howes

Chief Executive Funds Management
and Chief Executive Life

Distribution, Product and Marketing

Paul Rogan

Chief Executive Distribution, Product and Marketing

As we have continued to develop our organic growth we have combined Challenger's Distribution, Product and Marketing capability into its own separate group reporting to the CEO to improve the co-ordination and focus in these key areas. This focus is both driving and supporting our sales efforts, in retirement income and our Boutique Partnerships, and centralising client and adviser data capture and analytics for our business.



Distribution

2010/2011 saw the initiation and completion of some major distribution initiatives.

- Project Welcome Back successfully reconnected us with around 200 financial planners who had written annuity business historically.
- Project 10,000 was focused on targeting 10,000 contacts with the financial planners who sell our products. By June 2011, we had materially outstripped our original targets, and we continue to build on this momentum.
- We also increased focus on the retention of maturing annuity policies, leading to reinvestment rates now averaging around 80%, a solid improvement from 24 months ago.

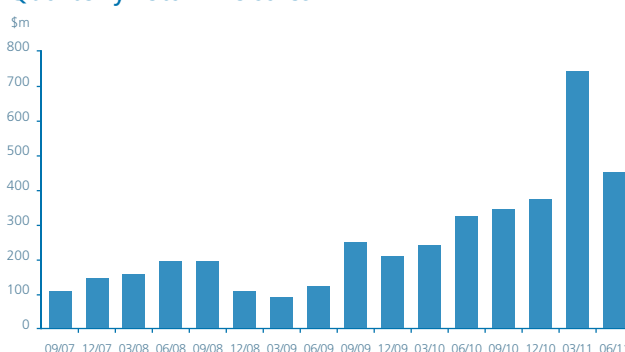
Building on these, we have also commenced new initiatives: Project Multiply, which will see us drive increased productivity from our distribution teams and lift sales per planner, and Project Footprint, which is focused on broadening our sales reach into planner groups across Australia.

Combined, all of this work is designed to increase the number of annuities written by financial planners, whilst increasing the number of financial planners who sell our products and further diversifying our distribution footprint.

Through the creation of specialist distribution teams for Life and Funds Management, focused either on annuity sales, Boutique Partnerships or Aligned Investments, we have driven greater penetration for our business. At the same time we have significantly increased the number of Business Development Managers to support the growth and demand in our Life and Funds Management operations.

Our roadshows for financial planners are now occurring twice a year. In February 2011 nearly 2,000 planners attended venues in Sydney, Melbourne, Brisbane, Adelaide, Hobart and Perth, to listen to our Chief Executive Life Richard Howes and our new Chairman of Retirement Income, Jeremy Cooper. The number of attendees was almost double those who attended in 2010.

Quarterly retail life sales



The year has seen a continued material uplift in retail life sales, with underlying sales in the June 2011 quarter our strongest ever. We also generated in excess of \$3.9bn in Boutique Partnership net flows via our institutional team.

Product

At our February roadshow, we officially launched our new Liquid Lifetime annuity product with planners. This new product won the Rainmaker 'Best innovation of the year' award. The product is a lifetime annuity

designed to give investors the security of income payments for life, but with an option to withdraw principal during the first 15 years.

We are looking at developing new retirement income products over the coming year, including solutions for sectors of the market that are traditionally unadvised, such as Self-Managed Superannuation Funds.

We continue to advocate for regulatory change that will enable greater innovation in the retirement income market, for example changes to facilitate a market for deferred annuities.

Marketing

The beginning of 2011 was an exciting time for the Company, as it launched Challenger's first major consumer advertising campaign.

Labelled 'Real Stories', the national campaign has been the largest consumer advertising programme in the Company's history. It portrays the impact of the global financial crisis on four individuals' retirement plans and has been running on free-to-air and subscription television, in cinema, on radio, in print and online. Our intent is to bring balance to a discussion that for too long has focused on the benefits of share market investing while rarely mentioning the risks. The campaign was recognised, winning the Rainmaker 'Best advertising campaign trade' and 'Best advertising campaign consumer awards'. Challenger also won the Money Management 'Marketing team of the year' award.

Supporting this campaign, we have revamped our internet site providing research material, case studies and other information applicable to retirees.

We have also responded to feedback from financial planners and created new web based tools such as our retirement calculator, assisting financial planners to model retirement income portfolios and the impact of various market scenarios on those portfolios.

Going forward, we intend to invest in improving the investor and adviser experience when interacting with Challenger.



Paul Rogan

Chief Executive

Distribution, Product and Marketing

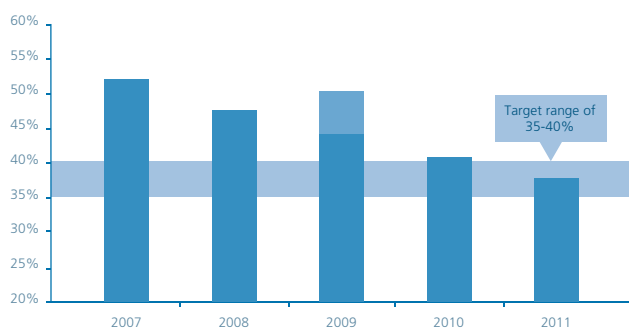
Corporate

Brian Benari

Group Chief Financial Officer and Chief Operating Officer

Finance and Tax, Treasury, Investor and Government Relations, Legal, Information Technology and Operations all form part of Business Services, headed up by the Group Chief Financial Officer and Chief Operating Officer. Bringing together all of the core functions of the organisation has led to significant cost savings and synergies whilst providing enhanced co-ordination and control. These synergies were again evident this year as the cost to income ratio across the Group fell four percentage points. This prudent cost control has been achieved while still investing in people and systems critical to support the work undertaken during the year in our Distribution, Product and Marketing division.

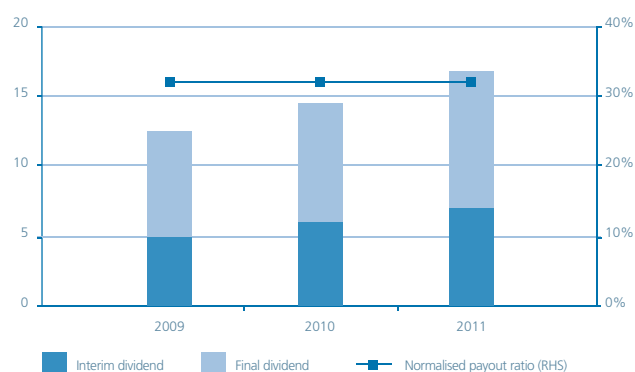
Group cost to income ratio



Note: \$22m of one-off restructuring costs incurred in 2009.

Expenses have continued to fall each year, and the Group cost to income ratio is targeted to remain within a 35-40% range over the medium term.

Dividend – cents per share (cps)



Dividends have been steadily increasing since 2009, in line with earnings. In addition to dividends, shareholders continue to benefit from the active share buy-back programme, which has provided material accretion for shareholders.

In addition to the share buy-back programme, shares that are required to satisfy the vesting of grants of either Performance Options or Performance Share Rights have been sourced from the Challenger Performance Plan Trust (CPP). The CPP looks to acquire shares around the date of PSR issuance. As a result of this, any impact of increase in the Challenger share price is not incurred by the Company to satisfy vested awards. As such Challenger has issued no new equity to satisfy vested awards since the Challenger Performance Plan was established in 2007.

The year saw further focus on minimising our impact on the environment by raising awareness with our people, employing technologies that minimise our use of resources and occupying sustainable places of work. We seek to accommodate our people in buildings which are National Australian Built Environment Rating System (NABERS) energy-accredited to a rating of 3.5 stars or higher. We also seek to maximise the NABERS energy accreditation of our tenancies, and our Head Office workspace at 255 Pitt Street, Sydney has an occupancy NABERS rating of 3.5 stars.

Blair Beaton

Head of Strategy and M&A

In the last few years, the importance of Strategy and Mergers & Acquisitions (M&A) to our Corporate Strategy has increased. Reflecting this, the role of Head of Strategy and M&A was elevated to a direct reporting line to the Chief Executive Officer.

The Strategy and M&A team has also been responsible for some of the key transactions that have occurred in recent years, including the acquisition of annuity books from MetLife and AXA, the sale of Mortgage Distribution and Financial Planning Operations, as well as the establishment of Boutique Partnerships for our Funds Management business.

Working closely with the Board and the Chief Executive Officer in regular planning workshops and off-sites, the team has assisted in establishing the strategic direction for our business over the medium term, including our retirement income strategy.



Blair Beaton and Brian Benari

Head of Strategy and M&A and
Group Chief Financial Officer
and Chief Operating Officer

Risk and Human Resources

Richard Willis

Chief Risk Officer

The 2011 financial year has seen continued industry focus on risk management and compliance practices and processes as market participants and regulators respond to the lessons of the global financial crisis and deal with ongoing macroeconomic challenges. Challenger has continued to evolve its risk management framework during the year to ensure that risk management and our compliance obligations remain a key focus of all employees. This saw the creation of a new role during the year: Chief Risk Officer, reporting directly to the Chief Executive Officer.

The Chief Risk Officer is responsible for all independent risk management functions for the Company, including compliance. Risks are managed within a framework across the organisation that is structured to operate within the parameters set by the Board and its risk appetite. The Board's Risk Appetite Statement outlines the level of risk that is acceptable for our business and for shareholders. This has a direct impact on culture within the organisation and provides clearly articulated boundaries on acceptable risk-taking activities across the Company.

The Chief Risk Officer is also responsible for oversight of regulatory engagement, including APRA and ASIC. In addition to regular liaison meetings with APRA during the year, additional meetings regarding APRA's Life and General Insurance Capital (LAGIC) project occurred. The project continues to gain momentum with strong parallels to Solvency II through the three-pillar regulatory approach, as well as local parallels to APRA's requirements for Authorised Deposit Taking Institutions (ADIs). New draft prudential capital standards for Life and General Insurers are expected by the end of the 2011 calendar year.

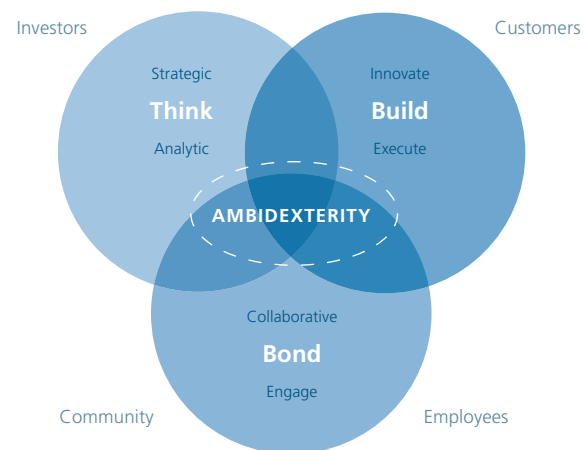
Jennifer Wheatley

Executive General Manager Human Resources

During the year, we have expanded on core people development initiatives such as a graduate recruitment programme, mentoring and our Leadership Perspectives programme in conjunction with the Australian Graduate School of Management (AGSM). The broad theme of 'applying leadership perspectives for better business outcomes' is central to this programme, and is explored within three subthemes:

- **THINK** – both strategically and analytically,
- **BUILD** – through innovation and execution, and
- **BOND** – through personal understanding of engagement and collaboration.

Leadership framework



Through our commitment to making a positive and meaningful contribution to the community, we have revitalised our Corporate Social Responsibility programme and have developed a number of community partnerships with charities that work across a range of causes. Current community partners include Alzheimer's Australia, Barnardos, Bear Cottage, Beyond Blue and National Seniors Foundation Trust.

With Challenger's Community Giving Programme, employees can also make regular donations to one of our community partners through their pre-tax salary. These contributions are then matched by the Company up to \$500 per employee per year. However, supporting these very worthwhile organisations requires more than just a financial contribution. Challenger also provides paid volunteer leave and actively encourages its employees to give their time and skills to help our community partners or another charity of their choice.



Jennifer Wheatley and Richard Willis
Executive General Manager Human Resources
and Chief Risk Officer

Directors' report

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The Company's approach to corporate governance

The Board of Directors and management of Challenger Limited (the Company) recognise their duties and obligations to stakeholders to implement and maintain a robust system of corporate governance. The Company believes that the adoption of good corporate governance adds value to stakeholders and enhances investor confidence.

The Board of Directors of the Company (the Board) determines the most appropriate corporate governance arrangements for the Company and its controlled entities (the Group), taking into consideration Australian and international standards and the prudential requirements of regulators such as the Australian Prudential Regulation Authority (APRA) and the Australian Securities and Investments Commission (ASIC). This statement reflects the Company's corporate governance arrangements as at the date of signing this report.

This statement reports against the ASX Corporate Governance Council's 'Corporate Governance Principles and Recommendations' as amended in 2010.

As required by the ASX Listing Rules, this statement sets out the extent to which the Group has followed the Principles or, where appropriate, indicates a departure from them with an explanation.

This report applies to the Group; however, some controlled entities have adopted additional policies and procedures to deal with specific issues relevant to their business, for instance Australian Financial Services Licence compliance. Where such policies and procedures have been adopted, they have been developed in line with the standards referred to throughout this report.

Principle 1 – Lay solid foundations for management and oversight

The role of the Board and delegations

The Board is accountable to shareholders for the activities and performance of the Company by overseeing the development of sustainable shareholder value within an appropriate framework of risk and regard for all stakeholder interests.

The Board has identified the key functions which it has reserved for itself. Full details are set out in the Board Charter, a copy of which is available on the Company's website. Duties of the Board include:

- establishment, promotion and maintenance of the strategic direction of the Company;
- approval of business plans, budgets and financial policies;
- consideration of management recommendations on strategic business matters;
- establishment, promotion and maintenance of proper processes and controls to maintain the integrity of accounting and financial records and reporting;
- fairly and responsibly rewarding executives, having regard to the interests of shareholders, the performance of executives, market conditions and the Company's performance;
- adoption and oversight of implementation of appropriate corporate governance practices;
- oversight of the establishment, promotion and maintenance of effective risk management policies and processes;
- determination and adoption of the Company's dividend policy;
- review of the Board's composition and performance;
- appointment, duration, evaluation and remuneration of the Chief Executive Officer (CEO) and approval of the appointment of the Chief Financial Officer (CFO), the Chief Risk Officer, the General Counsel and the Company Secretary; and
- determination of the extent of the CEO's delegated authority.

The Board has established Committees to assist in carrying out its responsibilities and to consider certain issues and functions in detail. The Board Committees are discussed in Principle 2.

Non-Executive Directors are issued with formal letters of appointment governing their roles and responsibilities. The responsibilities of the Chairman and the Directors are also set out in the Board Charter.

Management responsibility

The Board has delegated to the CEO the authority and powers necessary to implement the strategies approved by the Board and to manage the business affairs of the Company within the policies and specific delegation limits specified by the Board from time to time. The CEO may further delegate within those specific policies and delegation limits, but remains accountable for all authority delegated to management.

Executive performance assessment

The performance of senior executives is reviewed at least annually against appropriately agreed and documented performance objectives and measures, consistent with the Performance Management framework that applies to all Challenger employees. All employees at Challenger are also assessed against the Challenger Principles (refer to Principle 3).

The Remuneration Committee is responsible for reviewing the performance of the CEO at least annually; including setting the CEO goals for the coming year and reviewing progress in achieving those goals and making recommendations to the Board. The CEO is responsible for setting performance objectives and reviewing the performance of his direct reports.

Performance evaluations for the CEO and senior executives have taken place in respect of the 2011 reporting period in accordance with the above process.

Principle 2 – Structure the Board to add value

Membership of the Board

The Board comprises Directors who possess an appropriate range of skills, experience and expertise to:

- have a proper understanding of, and competence to deal with, the current and emerging issues of the business;
- exercise independent judgement;
- encourage enhanced performance by the Company; and
- effectively review and challenge the performance of management.

The Company's constitution provides for a minimum of three Directors and a maximum of 12 Directors. The table below summarises the current composition of the Board. Background details of each Director are set out on pages 27 to 29.

Name	Position	Independent	Appointed
Peter Polson	Chairman	Yes	2003
Dominic Stevens	Executive Director	No	2008
Graham Cubbin	Non-Executive Director	Yes	2004
Jonathan Grunzweig	Non-Executive Director	Yes	2010
Russell Hooper	Non-Executive Director	Yes	2003
Brenda Shanahan	Non-Executive Director	Yes	2011
Leon Zwier	Non-Executive Director	Yes	2006

The Chairman is selected by Non-Executive Directors of the Board. The roles of Chairman and CEO are not held by the same person.

As noted in the Directors' report, the composition of the Board of Directors has changed during the year. In April 2011, Ms Brenda Shanahan was appointed as an additional Non-Executive Director. Ms Shanahan is a Graduate of Melbourne University in Economics and Commerce and a Fellow of the Institute of Company Directors. Ms Shanahan has a long relationship with Challenger, having previously served as a Director of Challenger Boards and Committees. The appointment of Ms Shanahan increases the experience and the diversity of the Board.

Also during the year, in October 2010, Mr Jonathan Grunzweig of Colony Capital LLC (Colony Capital) was appointed as a new Non-Executive Director to replace Mr Tom Barrack, also of Colony Capital. Mr Barrack's increased commitments in the United States as founder, Chairman and Chief Executive Officer of Colony Capital led to his decision to step aside from the Challenger Board and to be replaced by Mr Grunzweig. Mr Grunzweig is Principal and Chief Investment Officer of Colony Capital, responsible for overseeing the sourcing, structuring, execution and management of all investments and divestments on a global basis.

Nominations and appointment of new Directors

The Board has established a Nomination Committee comprised of a majority of Independent Directors, having at least three members and chaired by an Independent Director.

Recommendations for nominations of new Directors are made by the Nomination Committee and considered by the Board as a whole. If a new Director is appointed during the year, that person will stand for election by shareholders at the next Annual General Meeting. Shareholders are provided with appropriate information to judge the adequacy of candidates. All new Directors are provided with an appropriate induction into Challenger's business. A copy of the Nomination Committee Charter can be found on the Company's website.

The Nomination Committee conducts periodic assessments of the Board's competencies. This assists the Nomination Committee in determining the appropriate composition of the Board and to consider the desirable depth and range of skills and diversity required for any new Board members. The Nomination Committee will draw on industry contacts and, where appropriate, will engage external consultants to assist with the identification and selection of a diverse range of candidates which meet the Nomination Committee's desired competencies. The Nomination Committee will also have regard to such criteria as independence, outstanding commercial capability, cultural fit and time availability to meet the commitment required.

The Nomination Committee makes an assessment of potential new Directors on the above criteria and makes recommendations to the Board for consideration and approval.

Retirement and re-election of Directors

The Company's constitution requires that, excluding the CEO, one third of the remaining Directors must retire each year. In addition, any Director who is appointed during the year must retire and be put up for re-election at the next Annual General Meeting.

Succession planning

In conjunction with the Nomination Committee, the Board considers the succession of its members, the CEO, the CFO, and the Chief Executives of each of the business divisions, as required.

Review of Board performance

The Board Charter sets out the requirement for a formal review of the Board's performance at least annually. A review of the Board's performance was conducted in June 2011.

The review of the Board's performance is conducted by the Chairman with all Board members. The review involves consideration of the effectiveness of the Board and its Committees having regard to the knowledge, skills and experience of the Directors. The review involves considering the weighting of attributes, culture and capabilities of the Board.

Director independence

The Board has adopted an Independence Policy that states that an Independent Director should be independent of management and free from any business or other relationship that could materially interfere with, or could reasonably be perceived to materially interfere with, the independent exercise of their judgement.

The Board regularly considers and assesses the independence of each Director in light of the interests and information that Directors disclose. In accordance with the *Corporations Act 2001*, Directors are required to advise the Company of any material personal interests they have in a matter.

In assessing independence, the Board will have regard to whether the Director has any of the following relationships with the Company or any Group company:

1. is a substantial shareholder (as defined by section 9 of the *Corporations Act 2001*) of the Company, or is a Director or officer of, or otherwise associated directly with, a substantial shareholder of the Company;
2. is employed, or has previously been employed, in an executive capacity by the Company or the Group, and there has not been a period of at least three years between ceasing such employment and serving on the Board;
3. has, within the last three years, been a principal of a material professional adviser or a material consultant to the Company or the Group, or an employee materially associated with the service provided;
4. is a material supplier or customer of the Company or the Group, or an officer of or otherwise associated directly or indirectly with a material supplier or customer; and
5. has a material contractual relationship with the Company or the Group other than as a Director.

The Board will state its reasons if it considers a Director to be independent notwithstanding the existence of a relationship of the kind referred to in points 1–5 above.

Determination of materiality in assessing independence

The materiality of a relationship is assessed on a case-by-case basis after having regard to each Director's individual circumstances. The Board has a majority of independent Directors.

Conflicts of interest

In accordance with the Board Charter and the *Corporations Act 2001*, any Director with a material personal interest in a matter being considered by the Board must declare such an interest and may only be present when the matter is being considered at the Board's discretion. Directors with a material interest may not vote on any matter in which they have declared a personal interest.

Meetings of the Board

The Board meets formally approximately every six weeks. In addition, the Board may meet whenever necessary to deal with specific matters needing attention between scheduled meetings.

The CEO, in consultation with the Chairman, establishes the meeting agendas to ensure adequate coverage of strategic, financial and material risk areas throughout the year. Senior executives are invited to attend Board meetings and are available for contact by Non-Executive Directors between meetings. The Non-Executive Directors often hold a private session without any executive involvement as part of Board meetings.

Board access to information and advice

All Directors have unrestricted access to the Company records and information. The Company Secretary provides Directors with guidance on corporate governance issues, developments and on all other matters reasonably requested by the Directors, and monitors compliance with the Board Charter.

The Board or each individual Director has the right to seek independent professional advice at the Company's expense to assist them in discharging their duties. Whilst the Chairman's prior approval is required, it may not be unreasonably withheld or delayed.

Board Committees

To assist it in undertaking its duties, the Board has established the following Committees:

- the Group Risk and Audit Committee (GRAC);
- the Remuneration Committee (RemCo); and
- the Nomination Committee (NomCo).

Each Committee has its own Charter, copies of which are available on the Company's website. The Charters specify the composition, responsibilities, duties, reporting obligations, meeting arrangements, authority and resources available to the Committees and the provisions for review of the Charter. Details of Directors' membership of each Committee and their attendance at meetings throughout the period from 1 July 2010 to 30 June 2011 are set out below.

Directors' meetings

Director	Board		Group Risk and Audit Committee		Remuneration Committee		Nomination Committee	
	Eligible to attend	Attended	Eligible to attend	Attended	Eligible to attend	Attended	Eligible to attend	Attended
P Polson	8	8	4	4	5	5	2	2
D Stevens	8	8	–	–	–	–	–	–
T Barrack Jr. ¹	1	1	–	–	–	–	1	1
G Cubbin	8	8	4	4	5	5	2	2
J Grunzweig	7	6	–	–	–	–	1	1
R Hooper	8	7	4	4	5	5	2	1
B Shanahan	3	3	–	–	–	–	–	–
L Zwier	8	6	–	–	–	–	2	1

¹ Director attended by personal attendance and through the attendance of his appointed alternate Directors.

Principle 3 – Promote ethical and responsible decision-making

The Board and the Company's commitment to ethical and responsible decision making is reflected in the internal policies and procedures, underpinned by the Challenger Principles of:

- Commercial Ownership;
- Compliance;
- Creative Customer Solutions;
- Working Together; and
- Integrity.

Code of Conduct

The Board has adopted a Code of Conduct which applies to all Directors, executives, management and employees of the Company and the Group. The Code articulates the standards of honest, ethical and law-abiding behaviour expected by the Company. Employees are actively encouraged to bring any problems to the attention of management or the Board, including activities or behaviour which may not comply with the Code of Conduct, other policies and procedures in place, or other regulatory requirements or laws. A copy of the Code can be found on the Company's website.

Political donations policy

The Board has adopted a policy of not making political donations in any country or jurisdiction in which it operates. Representatives of the Company may on occasion attend political functions. This attendance is strictly for commercial reasons and is predicated on the price charged not being in excess of commercial value (in terms of access) of the function.

Directors' and staff trading policy

The Board has approved Challenger's Staff Trading Policy which prescribes the manner in which Directors and staff can trade in the Company's shares. A copy of the policy is available on the Company's website.

Objectives for achieving gender diversity

The Board is committed to promoting a corporate culture that embraces diversity across the organisation. The Board has adopted a Diversity Policy, available on the Company's website, that has measurable objectives for achieving gender diversity. The Nomination Committee is responsible for the regular review of and reporting on the relative proportion of women employed at all levels of the Company and regular review of and reporting on the measurable objectives set on an annual basis pursuant to the Diversity Policy. The current objectives and progress towards achieving them, and the details of the proportion of women employed at all levels of the organisation are discussed in detail in the Sustainability section on page 25.

Principle 4 – Safeguard integrity in financial reporting

Integrity of financial reporting

The Board has the responsibility to ensure truthful and factual presentation of the Company's financial position. The Board has established a Group Risk and Audit Committee to assist the Board to focus on issues relevant to the integrity of the Company and the Group's financial reporting. In accordance with its Charter, the Group Risk and Audit Committee must have at least three members and is comprised of all Non-Executive Directors and a majority of independent members. The Committee is chaired by an Independent Director, who is not Chair of the Board.

The background details of the Group Risk and Audit Committee members are described in the Directors' report. The Committee typically meets four times a year and additional meetings are scheduled as required. The members' names and attendance at meetings are set out on page 20 of this report.

The Committee makes recommendations to the Board in relation to the appointment, review and removal of an external auditor, assessment of the external auditor's independence and the appropriateness of non-audit services that the external auditor may provide. A copy of the Group Risk and Audit Committee Charter is available on the Company's website.

Declaration by the Chief Executive Officer and the Chief Financial Officer

The CEO and CFO periodically provide formal assurance statements to the Board that:

- the Group's financial statements present a true and fair view of the Group's financial condition and operational results; and
- the risk management and internal compliance and control systems are sound, appropriate and operating efficiently and effectively.

Independent external audit

The Company requires its independent external auditor to:

- provide stakeholders with assurance as to whether the Group's financial reports are true and fair; and
- ensure Group accounting policies comply with applicable accounting standards and guidance.

The Company's independent external auditor is Ernst & Young (E&Y). E&Y was appointed upon constitution of the Company in November 2003, and this appointment was ratified by members at the Annual General Meeting held in November 2004.

External auditors are required to rotate the engagement partner assigned to the Company on a five year basis. Under this policy the lead audit engagement partner assigned to the Company rotated at the conclusion of the 2007 financial reporting period.

The Board has requested that E&Y attend the Company's Annual General Meeting, and that E&Y be available to answer any questions arising in relation to the conduct of its audit.

Principle 5 – Make timely and balanced disclosure

Continuous Disclosure Policy

The Company is committed to ensuring that all investors have equal and timely access to material information concerning the Company and that Company announcements are factual and presented in a clear and objective manner.

The Board has approved and implemented a Continuous Disclosure Policy. A copy of the policy can be found on the Company's website. The policy is designed to ensure compliance with the *Corporations Act 2001* and ASX Listing Rules continuous disclosure requirements. The Company has a Continuous Disclosure Committee which is responsible for:

- making decisions on what should be disclosed publicly under the Continuous Disclosure Policy;
- maintaining a watching brief on information; and
- ensuring that disclosure is made in a timely and efficient manner.

Principle 6 – Respect the rights of shareholders

The Company recognises the importance of enhancing its relationship with investors by:

- communicating effectively;
- providing ready access to clear and balanced information about the Company; and
- encouraging participation at general meetings.

As set out in Principle 5, it is Company policy that material information concerning the Company will be announced to the market in a timely and objective manner. Following release to the market, the Company publishes annual and half yearly reports, announcements, media releases and other relevant information on its website.

Internet webcasting and teleconferencing facilities are provided for market briefings to encourage participation from all stakeholders, regardless of their location. The Company also encourages greater use of electronic media by providing shareholders with greater access to the electronic receipt of reports and meeting notices.

The Company also provides a facility to ask questions about the Company and have them answered directly via electronic means.

All major and price sensitive announcements by the Company are lodged with the ASX and made publicly available via its website before being discussed or disseminated with members of the investment community.

Principle 7 – Recognise and manage risk

Risk management and compliance

The management of risks is fundamental to the Group's business and to building shareholder value. The Board recognises the broad range of risks that apply to the Group as a participant in the financial services industry, including, but not limited to, funding and liquidity risk, investment and pricing risk, counterparty risk, strategic, business and reputational risk, operational risk, licence and regulatory risk. The Board is responsible for determining the Group's risk management strategy and appetite. Management is responsible for implementing the Board's strategy and for developing policies and procedures to identify, manage and mitigate risks across the whole of the Group's operations in line with risk appetite.

The key design component of the Group's approach to risk management is that the heads of the business units have accountability for the risks within their divisions with oversight, analysis, monitoring and reporting of these risks by the Executive Risk Management Committee (ERMC) chaired by the Chief Risk Officer (CRO). The CRO is independent of the business units and responsible to the CEO and the Board and its Committees.

The framework and policies are developed by the CRO, reviewed and approved by the Group Risk and Audit Committee (GRAC), and then made available to all staff of the Group. The Group's risk management function has day to day responsibility for monitoring the implementation of the framework and policy, with regular reporting provided to the GRAC, via the ERMC, on the adequacy and effectiveness of management controls for material business risk.

The GRAC reports to the Board on the effectiveness of the framework, internal controls and policies, with a detailed review undertaken on an annual basis. A summary of Challenger's risk management framework can be found on the Company's website.

Internal audit

Internal audit services for the Group were provided by KPMG during the period. The GRAC oversees the scope of internal audit and monitors the progress of the internal audit work programme. The GRAC receives reports from internal audit at each meeting and monitors management's responsiveness to internal audit findings and recommendations. The internal audit function is independent of the external auditor. The internal audit function reports directly to the GRAC.

Assurance

In respect of the financial report for the year ended 30 June 2011, the Board has received formal assurance from the CEO and the CFO that:

- the Group's financial statements present a true and fair view of the Group's financial position and results for the period; and
- the risk management and internal compliance and control systems are sound, appropriate and operating efficiently and effectively.

This assurance forms part of the process by which the Board determines the effectiveness of its risk management and internal control systems in relation to financial reporting risks.

Principle 8 – Remunerate fairly and responsibly

The Board Remuneration Committee (RemCo)

The Board has established a RemCo comprised of a majority of Independent Directors, having at least three members and is chaired by an Independent Director.

The background details of the RemCo members are set out in the Directors' report. RemCo usually meets at least four times during the year, and additional meetings are scheduled as required. The members' names and attendance at meetings are set out in Principle 2 of this corporate governance statement.

RemCo is responsible for reviewing and recommending to the Board on:

- the Company's remuneration, recruitment, retention and termination policies and procedures for senior executives;
- senior executives' remuneration and incentives;
- superannuation arrangements;
- the remuneration framework for Directors; and
- remuneration by gender.

Remuneration

The remuneration details for key executives and Non-Executive Directors are reported in the Remuneration Report. Non-Executive Directors are not entitled to participate in incentive plans.

There are no termination payments to Non-Executive Directors on their retirement from office other than payments accruing from superannuation contributions comprising part of their remuneration.

Challenger policy, contained in the staff trading policy, prohibits any executive or staff member from entering into a transaction that is designed or intended to hedge that component of their unvested remuneration which is constituted by the Company's shares or options.

It is also Company policy to prohibit margin lending over Company shares by Directors, senior executives and staff members.

Sustainability commitment

Challenger fosters a strong culture of compliance, with a focus on ethics and corporate governance. People are critical to our success. We endeavour to create a work environment where diversity is embraced; people are promoted on their merits and treat each other with mutual respect and dignity.

We employ technologies and practices that enable us to minimise our carbon footprint, and we regard environmental, corporate governance and social issues as important considerations when making investment decisions.

Challenger Principles

We recognise that our people, and what they do on a daily basis, make a real difference to the culture at Challenger. The essence of Challenger is made up of five core principles that are linked to everything we do.

These principles are:

- Commercial Ownership – Achieving the best for the client, the business and employees
- Compliance – Being responsible for how and what we do
- Creative Customer Solutions – Superior customer service and providing innovative solutions to clients
- Working Together – True collaboration and embracing diversity
- Integrity – Being authentic and being accountable for what we say and do

We encourage our employees to champion our core principles and incorporate them into their daily work life. We believe that this will assist Challenger in achieving key business objectives.

Whistleblower policy

We strongly encourage all Challenger staff members with a concern to act on it. Integrity is a key Challenger principle and we actively foster an open culture where any issues can be raised and addressed. All policies at Challenger include a whistleblower provision and clear instructions on how staff can raise concerns in a confidential and non-threatening manner.

People/Human capital

In the past 12 months a number of initiatives have been developed for Challenger's people, with a particular focus on diversity, talent development, and health and wellbeing outlined below.

Diversity

At Challenger, diversity means recognising and embracing the contribution of people with different backgrounds, experiences and perspectives. It includes differences in gender, age, ethnicity, race, religion, language, sexual orientation, disability and cultural backgrounds.

Challenger believes that having a range of diverse employees better enables us to deliver quality products and services to our clients and strengthens organisational capability through increased morale, motivation and engagement.

For our people, this means attracting, recruiting, retaining and engaging diverse talent and embedding inclusive policies and practices. This means that diversity and inclusion are the responsibility of all Challenger employees and reflects how we interact with our stakeholders.

On 30 June 2010, the ASX Corporate Governance Council released amendments to the ASX Corporate Governance Principles and Recommendations in relation to diversity. Challenger has adopted a number of these provisions, including:

- The Board is ultimately responsible for diversity at all levels of the Group (including at Board level) and has delegated certain responsibilities in respect of diversity to the Nomination Committee as noted in the Nomination Committee Charter.
- A commitment that the Board has established measurable objectives for achieving diversity at all levels of Challenger. For the 2011 financial year, these included:
 1. the development of a formal policy concerning diversity (as summarised above). This policy includes the requirement for the Board to develop measurable objectives for achieving gender diversity, and for both these objectives and the progress made in achieving them, to be assessed annually;
 2. the identification of current and emerging talented women;
 3. the development and implementation of a coaching/mentoring programme for current and emerging talented women as a component of ongoing professional development; and
 4. providing access for talented women to internal networks and external professional women's networks.

Whilst these objectives were achieved, Challenger continues to further develop and refine its objectives to ensure that it achieves increased levels of diversity and inclusion, specifically in the areas of gender diversity and flexible work practices.

Gender diversity

At Challenger the gender diversity strategy is based on ensuring that gender is not a barrier to either participation or success. Detailed below is a comparison of the female representation at Challenger at the current and prior period end:

Role	2011		2010		Net movement	
	By number	By percentage	By number	By percentage	By number	By percentage
Board	1	14%	–	0%	1	14%
Senior management	10	26%	6	14%	4	12%
Management	21	22%	25	24%	(4)	(2%)
Non-management	148	46%	143	45%	5	1%

Leadership, mentoring and graduate recruitment

In conjunction with the Australian Graduate School of Management we have developed a senior leadership programme called Leadership Perspectives. The broad theme of ‘applying leadership perspectives for better business outcomes’ is central to this programme, and is explored within three sub-themes: Think, Build and Bond.

Our mentoring programme was successfully initiated as a pilot in 2010 and was expanded during 2011. The programme was developed to facilitate the professional and personal development of selected individuals by providing them with the opportunity to learn from senior managers within Challenger who have specific knowledge, skills and experience. The programme also provides a development opportunity for mentors, thereby building on the capability of senior managers in the Company.

Now also into its second year, our graduate recruitment programme provides an entry point for high-potential young talent, at a time when Australia faces an ageing workforce and a competitive employment market.

Our workplace

We recognise our place of work is more than an office space. The culture and community of a business is a key attribute for attracting and retaining valued employees. By providing flexible working environments we aim to facilitate a working style that promotes engagement and enables our people to grow and develop, to succeed and to feel connected with the Challenger community.

Challenger encourages our community to take ownership of the workplace. This is facilitated through the ‘Our Community’ committee made up of people from all over our business. This group of people is charged with building and maintaining the community spirit within Challenger and hosts annual events such as Kids to Work day and company-wide networking opportunities and initiates fundraising activities for our charity partners such as breakfasts and morning teas.

Recognising and rewarding our people is something we enjoy greatly. The annual ‘Stand Out’ awards celebrate those people who uphold the Challenger Principles on a daily basis and put in that extra effort in working positively with their peers. The award is a peer based programme with monthly nominations and an annual overall winner.

We also provide services and resources for our people to support their health and wellbeing, including free flu vaccinations, fitness club deals and discounts on private health insurance and optician services.

Parental leave

Challenger is committed to supporting our employees in balancing work and family commitments through its parental leave policy. Primary care givers can take up to 12 months leave, with 12 weeks at full pay. The policy also provides for two weeks of paid leave for secondary care givers.

Flexible work arrangements

Challenger recognises that there are times when a balance is needed between work and external responsibilities, especially for parents. Flexible working considers the way work is performed, to see whether it can be performed differently. Such flexibility may include:

- changes in hours of work (e.g. reduction in hours worked, changes to start/finish times);
- changes in patterns of work (e.g. different start/end times on different days or job sharing arrangements); and
- changes in work locations (e.g. working from home or another location).

Any permanent employee who has completed 12 months continuous service is eligible for flexible working arrangements.

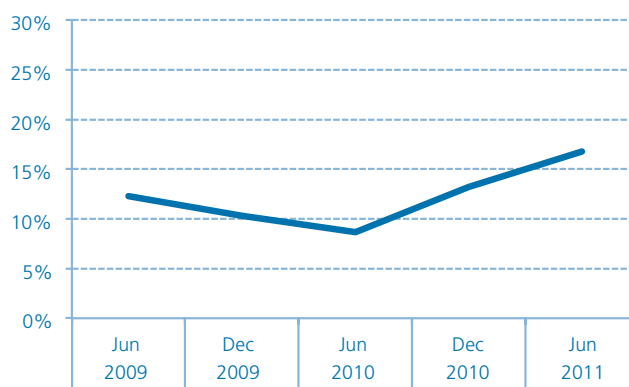
Absenteeism and turnover

In addition to measuring statistics relating to diversity, Challenger is committed to supporting a highly engaged workplace as part of a broader programme of initiatives designed to support engagement. The executive team and the Board monitor levels of employee turnover and absenteeism on a monthly basis (rolling yearly averages). Importantly, metrics are reviewed with the understanding that small movements can have a relatively large impact on overall percentages given our relatively small employee population of approximately 460 people.

Absenteeism (over and above annual leave taken) has remained constant at around 2.5 days per person annually. Turnover has increased to 16% in line with industry year on year increase, which has been expected given the tightening in the skilled labour market and resultant increased demand for talent.

Exit interview data are considered when developing strategies around engagement and people development over time.

Challenger voluntary turnover (rolling yearly average)



Community partnerships

Challenger is committed to making a positive and meaningful contribution to the community. We have revitalised our Corporate Social Responsibility programme and have developed a number of community partnerships with charities that work across a range of causes. Current community partners include Alzheimer's Australia, Barnardos, Bear Cottage, Beyond Blue and National Seniors Foundation Trust.

Through Challenger's Community Giving Programme, employees can make regular donations to one of our community partners through their pre-tax salary. These contributions are then matched by the Company up to \$500 per employee per year. However, supporting these very worthwhile organisations requires more than just a financial contribution. Challenger also provides paid volunteer leave and actively encourages its employees to give their time and skills to help our community partners or another charity of their choice.

Challenger's shareholders are also invited to support our community partners by donating some or all of their dividends through its dividend donation programme.

Environment

Property environmental performance

Challenger aims to minimise our impact on the environment by raising awareness with our people, employing technologies that minimise our use of resources and occupying sustainable places of work. When leasing premises, we seek accommodation in buildings which are National Australian Built Environment Rating System (NABERS) energy-accredited to a rating of 3.5 stars or higher. We also seek to maximise the NABERS energy accreditation of our tenancies.

Our workspace at 255 Pitt Street, Sydney has an occupancy NABERS rating of 3.5 stars and was designed for sustainable business practices and includes technology such as:

- energy efficient and computer-controlled lighting;
- time-controlled room heating, ventilation and air-conditioning;
- recycling facilities;
- multi-function devices utilising destination print; and
- LCD monitors.

Carbon price impact

On 10 July 2011, the Australian Government announced its Climate Change plan and the introduction of a price on carbon. The application of a carbon price applies to Scope 1 emitters who emit more than 25Kt of CO₂ or consume more than 100 terajoules from any one facility or property. Challenger has analysed the Climate Change plan and confirms that there is no direct impact of the introduction of a carbon price on Challenger.

Directors' report

The Directors of Challenger Limited (the Company) submit their report, together with the financial report of the Company and its controlled entities (the Group), for the year ended 30 June 2011.

Following shareholder approval at the 2010 Annual General Meeting, the Company changed its name from *Challenger Financial Services Group Limited* to *Challenger Limited* on 29 November 2010.

1. Directors

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

Peter L Polson

Independent Chairman

Experience/qualifications

Mr Polson holds a Bachelor of Commerce degree from the Witwatersrand University in South Africa and a Master of Business Leadership from the University of South Africa, and has completed the Harvard Management Development Programme.

Mr Polson retired from the Commonwealth Bank in October 2002, where he had held the position of Group Executive, Investment and Insurance Services. Mr Polson joined the Colonial group in 1994 prior to its acquisition by the Commonwealth Bank. Previously, Mr Polson was Managing Director of National Mutual Funds Management (International) Limited. Mr Polson has been a Director of the Company since 6 November 2003.

Special responsibilities

Mr Polson is Chairman of the Remuneration Committee, Chairman of the Nomination Committee and is a member of the Group Risk and Audit Committee.

Directorships of other listed companies

Mr Polson is Chairman of Customers Limited (appointed as a director on 23 November 2010). Mr Polson was previously the Chairman of AWB Limited (appointed 31 March 2003), he ceased to be Chairman and Director on 3 December 2010 following the acquisition of AWB Limited by Agrium Inc.

Dominic J Stevens

Chief Executive Officer and Managing Director

Experience/qualifications

Mr Stevens commenced in the role of Chief Executive Officer in September 2008 and was previously Deputy Managing Director of the Group. Mr Stevens joined the Group in September 2003; at which time he primarily held responsibility for overseeing Challenger's capital, risk management and strategy group.

Prior to joining Challenger, Mr Stevens led the foundation and was the Senior Managing Director of Zurich Capital Markets in the Asian region. Zurich Capital Markets Asia specialised in the areas of structured finance, derivative solutions and provision of risk management products to investors in alternative assets.

From 1987 to 1999 Mr Stevens held a number of senior roles at Bankers Trust. Mr Stevens was a Partner of Bankers Trust Company, where he headed the Bankers Trust commodity businesses globally (ex energy). In addition, Mr Stevens was responsible for the derivatives risk management business at Bankers Trust Australia. Mr Stevens was awarded a Bachelor of Commerce (Hons) Finance in 1986 from the University of New South Wales, Sydney, Australia.

Directorships of other listed companies

Mr Stevens was a director of Homeloans Limited from 3 May 2007 until 28 October 2008.

Graham A Cubbin

Non-Executive Director

Independent

Experience/qualifications

Mr Cubbin holds a Bachelor of Economics (Hons) from Monash University and is a Fellow of the Australian Institute of Company Directors.

Mr Cubbin was a Senior Executive with Consolidated Press Holdings Limited (CPH) from 1990 until September 2005, including Chief Financial Officer for 13 years. Prior to joining CPH, Mr Cubbin held senior finance positions with a number of major companies, including Capita Financial Group and Ford Motor Company. Mr Cubbin has been a Director of the Company since 6 January 2004.

Special responsibilities

Mr Cubbin is a member of the Group Risk and Audit Committee, the Remuneration Committee and the Nomination Committee.

Directorships of other listed companies

Mr Cubbin is a non-executive director of Bell Financial Group Limited (appointed 12 September 2007), STW Communications Limited (appointed 20 May 2008), White Energy Company Limited (appointed 17 February 2010) and McPherson's Limited (appointed 28 September 2010).

Jonathan Grunzweig

Non-Executive Director

Independent

Mr Grunzweig was appointed on 6 October 2010.

Experience/qualifications

Mr Grunzweig was appointed as a Director of the Company on 6 October 2010. Mr Grunzweig holds a Bachelor of Arts Degree from Cornell University, USA and a Juris Doctor in Law from Harvard University. Mr Grunzweig is Principal and Chief Investment Officer (CIO) of Colony Capital, LLC. As CIO, Mr Grunzweig oversees the sourcing, structuring, execution and management of all investments and divestments on a global basis. Prior to joining Colony in 1999, Mr Grunzweig was a Partner with the law firm of Skadden, Arps, Slate, Meagher & Flom LLP, where he specialised in corporate finance and mergers and acquisitions.

Special responsibilities

Mr Grunzweig is a member of the Nomination Committee.

Russell R Hooper

Non-Executive Director

Independent

Experience/qualifications

Mr Hooper is a Fellow of the Australian Institute of Company Directors, a Fellow of the Australian Society of Practising Accountants and a Fellow of the Financial Services Institute of Australasia, and has completed the Advanced Management Programme, Harvard Business School.

He has experience at chief executive level in life insurance, wealth management and listed investment trusts. Mr Hooper has been a Director of the Company since 6 November 2003.

Special responsibilities

Mr Hooper is the Chair of the Group Risk and Audit Committee, a member of the Remuneration Committee and the Nomination Committee.

Directorships of other listed companies

Mr Hooper is a director of Century Australia Investments Limited (appointed 12 September 2006).

Brenda M Shanahan

Non-Executive Director

Independent

Ms Shanahan was appointed on 1 April 2011.

Experience/qualifications

Ms Shanahan is a Graduate of Melbourne University in Economics and Commerce and a Fellow of the Australian Institute of Directors. Ms Shanahan has a research and institutional background in finance in Australia and overseas economies and equity markets. She has held executive positions in stock broking, investment management and an actuarial firm. Ms Shanahan was appointed as a Director of the Company on 1 April 2011.

Special responsibilities

Ms Shanahan is a member of the Group Risk and Audit Committee and the Nomination Committee.

Directorships of other listed companies

Ms Shanahan is a non-executive director of Clinuvet Pharmaceuticals Limited (appointed 6 February 2007).

Leon Zwier

Non-Executive Director

Independent

Experience/qualifications

Mr Zwier is a partner in the law firm Arnold Bloch Leibler. Mr Zwier holds a Bachelor of Laws from the University of Melbourne. Mr Zwier is a member of the External Advisory Committee of the Department of Business Law and Taxation (Monash University) and an Honorary Fellow of the same department. Mr Zwier has been a Director of the Company since 15 September 2006.

Special responsibilities

Mr Zwier is a member of the Nomination Committee.

Thomas Barrack Jr.

Non-Executive Director

Independent

Mr Barrack resigned on 6 October 2010.

Experience/qualifications

Mr Barrack received a Juris Doctor in Law from the University of San Diego and also holds a Bachelor of Arts degree from the University of Southern California.

Mr Barrack is the Founder, Chairman and Chief Executive Officer of Colony Capital, LLC and Colony Advisors, LLC. Prior to forming Colony, Mr Barrack was a principal with the Robert M. Bass Group, Inc. Mr Barrack also served in the Reagan Administration as Deputy Under Secretary of the Department of the Interior. Previously, Mr Barrack was a Senior Vice President at EF Hutton in New York City and President of Oxford Development Ventures, Inc. Mr Barrack was appointed as a Director on 22 November 2007 and resigned on 6 October 2010.

2. Company Secretary

Mr Michael Vardanega, B Comm LL.B, is a qualified solicitor and was appointed to the position of General Counsel and Group Company Secretary on 11 March 2011. In this role, he is responsible for the legal and company secretariat teams within Challenger. Since joining Challenger in 2006, he has been extensively involved in the general management of corporate actions, public entity compliance and governance matters for Challenger and its subsidiaries. Prior to joining Challenger, Mr Vardanega was a member of the corporate advisory practice at commercial law firm, Blake Dawson.

Ms Suzanne Koeppenkastrup, B Comm LL.M, was appointed to the position of Company Secretary in October 2006.

Ms Koeppenkastrup is a qualified solicitor and head of the company secretariat team at Challenger. She has over 15 years experience in legal and company secretarial roles in the financial services industry.

Christopher Robson resigned as Company Secretary on 11 March 2011.

3. Principal activities and changes in the state of affairs

The principal activities of the Group during the year were the provision of financial services. The following divisional units are responsible for delivering the Group's principal activities:

Life – the provision of a range of life insurance, annuity, superannuation and investment products in Australia, backed by a diverse portfolio of assets, to produce predictable over-the-cycle returns to shareholders.

Funds Management – manufactures and distributes quality investment products for both institutional and retail clients, including specialised funds. The Funds Management business model continues to transition from a traditional in-house portfolio manager structure to a boutique partnership structure. Further details of this are outlined in the operating and financial review section below.

There have been no significant changes in the nature of these principal activities or state of affairs of the Group during the year.

4. Operating and financial review

The Group's *statutory profit attributable to equity holders* of \$261.4 million for the year ended 30 June 2011 represents a \$21.1 million, or a 7.5%, fall compared to \$282.5 million for the year to 30 June 2010. The upward trend in underlying profit resulting from an increasing asset base, due to strong annuity cash inflows in the prior and current period, was offset by lower gains on the Group's debt investments compared to 2010 and losses on the Group's infrastructure assets over the year.

As described below, *normalised net profit after tax* removes the volatility arising from market movements on the Group's investments. As a result, the *normalised net profit after tax* of \$248.0 million represents a \$15.5 million, or a 6.7%, increase on the \$232.5 million for the year to 30 June 2010. The increase in *normalised profit after tax* was supported by an increase in *net income* of \$46.4 million (10.4%) primarily due to the Life division's increasing asset base arising from the continuing strong annuity sales described above. The average funds under management (FUM) for the Funds Management business rose significantly over the prior period with the Boutique Partnerships' FUM rising \$7.8 billion to \$14.8 billion at 30 June 2011.

The management view of *operating expenses* of \$180.2 million for the period was marginally lower than in the prior period, even with increased spend on distribution, product development and marketing during the period. The resulting cost to income ratio of 36.5% compares favourably to the 40.6% for the prior period.

The management view of *interest and borrowing costs* of \$2.7 million represents an \$11.4 million decrease compared to the prior period due to a combination of significantly lower levels of corporate recourse debt and a lower average cost of debt. The Group corporate debt facilities were undrawn at 30 June 2011.

Normalised profit and investment experience

The Group is required by accounting standards to value all assets and liabilities supporting the life insurance business at fair value. This can give rise to fluctuating valuation movements being recognised in the income statement. As the Group is fundamentally a long term holder of assets, due to them being held to match the term of the Group's life contract obligations, a large proportion of the gains and losses recognised in the income statement in any one period are unrealised and are expected to reverse over time.

Investment experience is a mechanism employed to remove the volatility arising from asset and liability valuation from the results so as to reflect more accurately the underlying performance of the Group. The difference between the actual investment gains/losses (both realised and unrealised) and the normalised gains/losses (being the Group's expected long term return) plus any actuarial assumption changes for the period is referred to as 'investment experience'.

The investment experience is reported separately from normalised profit in order to provide a better understanding of the Group's normalised financial results for the year.

The investment experience net loss after tax of \$28.7 million for the period compares to a net after tax gain of \$51.3 million for the year ended 30 June 2010. Global debt and equity markets have remained volatile and asset values still reflect a repricing of risk.

Significant items

The Group recognised a significant tax benefit of \$42.1 million in the year following confirmation from the Australian Taxation Office (ATO) that there were no further matters arising from the Group's tax treatment of specific items identified in a tax audit of prior years. This tax benefit has been reported separately from normalised profit after tax to provide a better understanding of the Group's normalised financial results for the year.

The following tables provide an overview of the Group's normalised results and components of investment experience:

	30 June 2011 \$M	30 June 2010 \$M	Change %
For the year ended			
Management analysis¹			
Normalised cash operating earnings	400.8	338.0	18.6
Net fee income	88.4	102.0	(13.3)
Other income	4.8	7.6	(36.8)
Net income	494.0	447.6	10.4
Operating expenses	(180.2)	(181.8)	(0.9)
Normalised EBIT	313.8	265.8	18.1
Interest and borrowing costs	(2.7)	(14.1)	(80.9)
Discontinued operations ²	–	39.1	Large
Normalised net profit before tax	311.1	290.8	7.0
Tax on normalised net profit	(63.1)	(58.3)	8.3
Normalised net profit after tax	248.0	232.5	6.7
Investment experience after tax	(28.7)	51.3	(155.9)
Significant items after tax ³	42.1	(1.3)	Large
Statutory profit attributable to equity holders	261.4	282.5	(7.5)

¹ 'Net income' and 'operating expenses' are internal classifications and are defined in Note 2 Segment information in the financial report. These differ from the statutory 'revenue' and 'expenses' classifications as certain direct costs (including commissions and management fees) are netted off against gross revenues and Special Purpose Vehicle revenues, expenses and finance costs are netted and included in aggregate for net income, or management view of revenue. These classifications have been made in the Directors' report, and the segment information note, as they reflect metrics used by management to measure the business performance of the Group. Whilst the allocation of amounts to the above items and investment experience differs to the statutory view, both approaches result in the same net after tax profit due to Challenger shareholders.

² Discontinued operations represent the results of the mortgage distribution business for the 4 months up to the date of sale to National Australia Bank Limited on 30 October 2009.

³ In May 2011 confirmation was received from the Australian Taxation Office (ATO) that there were no further matters arising from the Group's tax treatment of specific items identified in a tax audit of prior years. As a result, a legacy tax provision was released.

	30 June 2011 \$M	30 June 2010 \$M
For the year ended		
Components of investment experience		
Normalised capital growth¹		
Cash, fixed interest and debt	(19.6)	(14.6)
Infrastructure	19.7	24.9
Property (net of debt)	30.8	29.8
Equity and other investments	14.6	14.5
Total normalised capital growth	45.5	54.6
Actual capital growth²		
Cash, fixed interest and debt	20.4	155.3
Infrastructure	(52.9)	21.0
Property (net of debt)	18.8	52.7
Equity and other investments	14.8	5.1
Total actual capital growth	1.1	234.1
Investment experience		
Cash, fixed interest and debt	40.0	169.9
Infrastructure	(72.6)	(3.9)
Property (net of debt)	(12.0)	22.8
Equity and other investments	0.2	(9.4)
	(44.4)	179.5
Actuarial assumption changes³	3.4	(124.0)
Investment experience before tax	(41.0)	55.5
Tax benefit/(expense)	12.3	(4.2)
Investment experience after tax	(28.7)	51.3

¹ Normalised capital growth 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 long term capital growth expectations for each asset class over the investment cycle. The normalised growth rate for each asset class is 6.0% for Equity and other investments, 4.0% for Infrastructure, 2.0% for Property and (0.35%) for Cash, fixed interest and debt. The rates have been set with reference to market growth rates and are reviewed for appropriateness on an annual basis. For example, the normalised growth assumption for property was amended in January 2010 from 2.5% to 2.0%. This was as a result of the privatisation of CKT increasing the Group's exposure to Japanese property assets which have a lower expected long term capital growth rate than the rest of the property portfolio. No other changes have been made to the normalised capital growth rates since they were first introduced in June 2008.

² Actual capital growth represents net realised and unrealised capital gains or losses and includes the attribution of interest rate and foreign exchange derivatives that are used to hedge volatility.

³ Actuarial assumption changes represents the impact of changes in macro-economic variables, including bond yields and inflation factors, expense assumptions, losses on new business and other factors applied in the valuation of life contract liabilities. It also includes the attribution of interest rate derivatives used to hedge interest rate volatility.

Earnings per share

As shown in the table below, on a normalised basis, basic earnings per share (EPS) increased 13.6% to 51.7 cents and diluted EPS increased 12.6% to 48.1 cents. Both basic and diluted EPS figures were positively impacted by the 9.5 million shares purchased and cancelled as part of the Company's on-market buy-back over the year.

For the year ended	30 June 2011 cents	30 June 2010 cents	Change %
Basic – normalised	51.7	45.5	13.6
Diluted – normalised	48.1	42.7	12.6
Basic – statutory/(continuing)	54.5	53.8	1.3
Diluted – statutory/(continuing)	50.7	50.4	0.6

Key events during the period

The Life division recorded significant retail annuity sales of \$1,903.6 million for the year compared to total sales of \$933.1 million in the year to 30 June 2010. The increase in average investment assets of the Life division, from \$6.4 billion at 30 June 2010 to \$7.9 billion at 30 June 2011, was driven by the annuity sales noted above. The Group has continued to invest in product development, marketing and increased distribution capability during the year.

The Funds Management division, particularly through the Boutique Partnerships, experienced positive funds flow during the period. Boutique Partnerships now have \$14.8 billion funds under management (FUM) at 30 June 2011, up from \$7.0 billion at 30 June 2010. Total FUM of the Funds Management division totals \$23.6 billion at 30 June 2011, up from \$20.2 billion at 30 June 2010, representing growth of \$3.4 billion (16.8%) over the year.

Capital position

The Group's capital position is managed at both the Group and the, prudentially regulated, Challenger Life Company Limited (CLC) level with the objective of maintaining the financial stability of the Group and CLC whilst ensuring that the shareholders earn an appropriate risk adjusted return. The Group corporate debt facilities are undrawn at 30 June 2011 (30 June 2010: undrawn) and there is \$93.0 million of Group available cash (30 June 2010: \$76.1 million).

Capital reserves above the regulatory minimum in CLC grew from in excess of \$630 million at 30 June 2010 to in excess of \$675 million at 30 June 2011, supported by CLC's increased underlying earnings during the period. The Company continued its on-market share buy-back activity during the period and received shareholder approval at the Annual General Meeting (AGM) on 18 November 2010 to buy back a further 50.3 million shares, effectively refreshing the ability of the Company to buy back up to 10% of its issued capital.

In total, the Company has bought back 9.5 million shares during the year at an average price of \$4.68 per share. From the commencement of the programme in July 2008 to the date of this report, a total of 122.8 million shares have been repurchased at an average price of \$3.22 per share.

5. Dividends

On 20 August 2010, the Directors of the Company declared a final dividend on ordinary shares in respect of the year ended 30 June 2010 of 8.5 cents per share. The final dividend, of \$41.8 million, unfranked, was paid on 15 October 2010.

On 18 February 2011, the Directors of the Company declared an interim unfranked dividend of 7.0 cents per share in respect of the half year ended 31 December 2010 (31 December 2009: 6.0 cents per share, unfranked). The interim dividend of \$34.1 million, unfranked, was paid on 31 March 2011.

On 19 August 2011, the Directors of the Company declared a final dividend on ordinary shares in respect of the year ended 30 June 2011 of 9.5 cents per share. The final dividend is estimated to be \$45.1 million, will be unfranked, is payable on 29 September 2011 and has not been provided for in the 30 June 2011 financial report.

The final unfranked dividend brings the total dividend per security for the 2011 financial year to 16.5 cents (2010: 14.5 cents – unfranked), an increase of 13.8% on the prior year. The total dividend represents a payout ratio of 31.9% of normalised net profit after tax and is consistent with the Group's policy of paying approximately 30% of normalised after tax profit.

6. Significant events after the balance date

At the date of this report and other than as disclosed in this report or the financial report, no other 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.

Global market volatility

Subsequent to 30 June 2011 there has been significant volatility in global equity and debt markets following the downgrade of the credit rating of US long term sovereign debt by Standard & Poor's and continued market uncertainty in relation to European sovereign debt.

A detailed sensitivity analysis of asset and liability valuations to market risk, credit risk and liquidity risk is provided in Note 27 to the Financial Report. The Group actively manages levels of capital, gearing and liquidity of the investment assets held to support the Group's obligations to the life contract holders of Challenger Life Company Limited (CLC), which is subject to prudential regulation. As at 19 August 2011, CLC held significant capital in excess of its prudential regulatory requirements.

7. Likely developments and expected results

The investment management market in which the Group operates has seen significant structural change and development in the last two years. In the retirement income segment our targeted demographic of 65 years and over is growing almost four times faster than the pre-retirement demographic, and in the pre-retirement sector the Government has announced its intention to lift superannuation contributions from 9% to 12% over the next 10 years via the superannuation guarantee charge. Legislation has yet to be passed to enact this increase.

When these changes are combined with an increased focus on risk and return, both at a consumer level and by regulatory review committees and government, we see material growth opportunities for our business to take advantage of these positive tailwinds.

The Group is well placed to participate in the growing Australian retirement income market and the fast developing boutique funds management business. We are directing our focus towards lifting product sales via expanded distribution and the introduction of new guaranteed income products. Subject to continued stability in global markets, we are confident we can increase value for shareholders over the coming years.

The Australian Prudential Regulation Authority (APRA) issues Prudential Standards that impose minimum statutory capital requirements on all regulated entities. APRA is currently reviewing these standards as part of its Life and General Insurance Capital (LAGIC) project. It is expected that this review will result in changes to the Prudential Standards and these are currently due to be effective from 1 January 2013.

8. Indemnification and insurance of officers and Directors

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

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 and its subsidiaries. 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. The Company has not given, nor agreed to give, any indemnity to an auditor of the Group and has not paid any premium for insurance against that auditor's liabilities for legal costs.

9. Environmental regulation and performance

The Group acts as a trustee or responsible entity for a number of trusts that own assets both in Australia and overseas. These assets are subject to environmental regulations under both Commonwealth and State legislation. The Directors are satisfied that adequate systems are in place for the management of its 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.

10. Remuneration report

Letter from the Chairman

Dear Shareholders,

At last year's annual general meeting in November 2010, Challenger received a substantial negative vote in relation to our remuneration report. I can assure you that your Board took this feedback very seriously and committed to significantly increase our interaction with key shareholders and stakeholders to better understand and address their concerns.

In February 2011, we commenced a six-month consultation process with our institutional shareholders, retail shareholder representative groups and proxy advisory firms. I personally attended 17 meetings and spoke with 31 parties about Challenger's current remuneration policies and the changes made to our practices during the year. This consultation process has led to improved disclosure and transparency in this year's remuneration report.

As a basic principle, your Board has always ensured that the remuneration paid to our staff and executive has been directly aligned to the value created for shareholders. Illustrated in the charts on page 36, through an extraordinarily difficult period for wealth managers, Challenger has recorded five years of sustained normalised NPAT and EPS growth, significantly outperforming its peers. Challenger has also delivered total shareholder returns many multiples above the broader market on a one, three and five year basis.

Although your company has performed very strongly over the last five years, following discussions with our shareholders we decided to make changes to both our remuneration practices and disclosures. These include:

- increasing the number of years over which hurdled Long Term Incentives (LTI) vest from 3 to 4, with the first third vesting on the second anniversary of grant;
- reducing LTI hurdles from two to one, such that only absolute Total Shareholder Return (TSR) targets must be met rather than TSR or EPS targets;
- granting Hurdled Performance Share Rights (HPSRs) instead of options;
- reducing employee ownership by way of unvested equity instruments below 10% of issued capital;
- in addition to disclosing statutory remuneration of key management personnel (KMP), publishing the total remuneration actually awarded to each KMP in the current year; and
- disclosing the basis on which executives are assessed and rewarded with Short Term Incentives (STI) and the manner in which that total pool is calculated.

This year's report, I am sure, provides greater insight into the rationale behind our remuneration decisions. Maintaining outperformance in returns for shareholders and delivering an aligned remuneration structure for executives has been, and continues to be, at the forefront of our decision-making.

Yours sincerely,



Peter Polson

Overview

In 2003, the Board decided to significantly improve the quality, expertise and experience of its Executive Management Team.

The Company operates in the Life, Wealth and Funds Management market. However, as the leading annuity provider in Australia, Challenger predominantly provides long term guaranteed returns to its customers.

Managing the risks associated with those guarantees required the recruitment of individuals with a depth of financial risk management skills typically found in Investment or Commercial Banking disciplines.

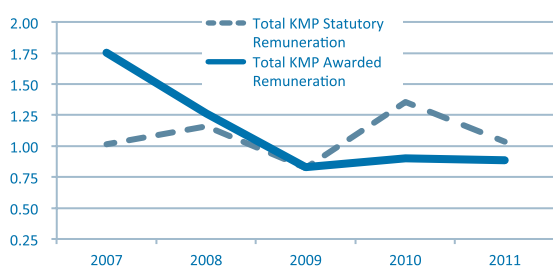
To attract and retain Executives with these skills, remuneration was structured to be more focused on longer term value creation. This resulted in a higher proportion of remuneration at risk in the form of equity than industry norms.

The statutory accounting expense for remuneration in the form of equity requires the cost to be amortised over the life of the grants. Therefore any reduction in awards will give rise to a lower accounting expense, however it will be reflected gradually and in future periods. This is illustrated in the chart below that highlights that while awarded remuneration to Executives has reduced over the last five years, the statutory accounting expense recorded has only now begun to reduce.

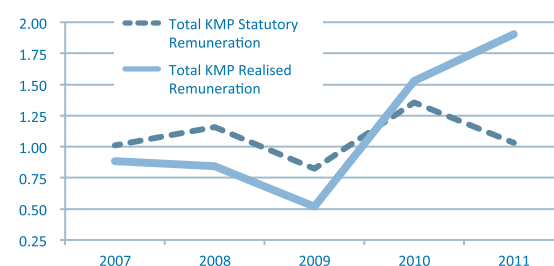
Additionally, the realised (or cash) view of the Key Management Personnel (KMP) remuneration shows the remuneration benefit only when it has been vested and realised. Given this, there will be variable outcomes depending on vesting dates of awards and share price movements. This is illustrated in the chart below on the right that shows realised remuneration had been below statutory remuneration (2007-2009) until historic LTI awards began vesting in 2010 and 2011, consistent with Challenger's shareholder returns over these periods.

A full description of all remuneration presentation (awarded, statutory and realised) can be found on page 49.

Statutory Remuneration/Awarded Remuneration



Statutory Remuneration/Realised Remuneration



The original goals set in 2003 by the Board have more than been achieved, and through even the most testing of times for financial services companies in the last 70 years. Challenger has evolved into a streamlined, focused and successful organisation with a leading position in the retirement income sector in Australia. Over the past five years, Challenger has grown earnings per share by 160%, which equates to a compound growth rate of 21%, and achieved a total shareholder return of 75%.

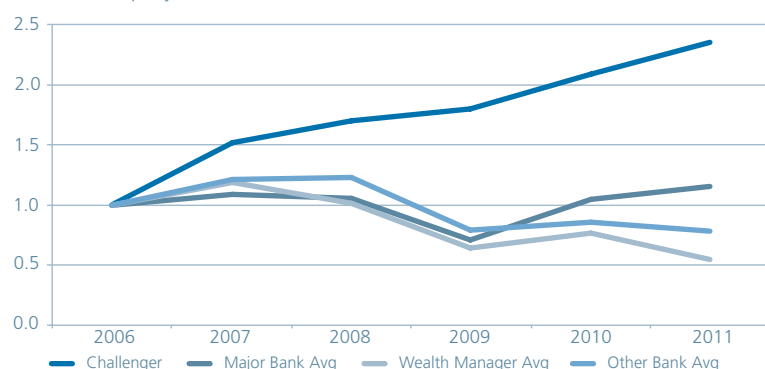
Outlined below is longer term trend data highlighting the performance of the Company and its controlled entities (the Group) since 2006. This performance has positively impacted both shareholder value and remuneration outcomes for Executives exposed to short-term incentives and long term incentive plans. As Challenger's business strategy has matured, so has its remuneration strategies. Challenger has reduced the level of long term incentive equity issuance to below 10% of issued capital whilst still retaining appropriate levels of alignment between Executives and shareholders.

Year ended 30 June	2006	2007	2008	2009	2010	2011
Normalised net profit after tax (NPAT) (\$m)	118.0	182.0	217.9	218.9	232.5	248.0
Normalised basic earnings per share (EPS) (cents)	20.0	33.0	37.1	39.2	45.5	51.7
Closing share price (\$)	3.16	5.83	1.89	2.24	3.52	4.89
Dividends per share (cents)	7.5	12.5	12.5	12.5	14.5	16.5

Normalised net profit after tax (NPAT) represents the underlying profit of the Group after adjusting the statutory profit/loss for any asset or liability valuation movements that are above or below our expected long term growth rates for each asset class held by Challenger Life Company Limited and any non-core or significant items that may positively or negatively impact the financial results. These principles have been consistently applied across current and prior reporting periods for the last six years. For a more fulsome disclosure on normalised earnings, refer to the *Operating and financial review* section of the Directors' report.

Normalised EPS Performance Versus Other Financials

(Source: Company Data/IRESS FY11 Estimates)

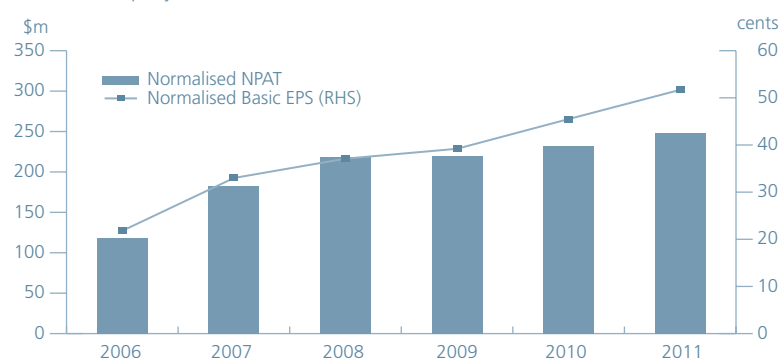


Significant outperformance in EPS growth

Major Bank Avg – Cash EPS (ANZ, CBA, NAB, WBC); Other Bank Avg – Cash EPS (BEN, BOQ, MQG, SUN), Wealth Manager Avg – Normalised EPS (AMP, IOOF, PPT)

Normalised Earnings/Normalised Basic EPS

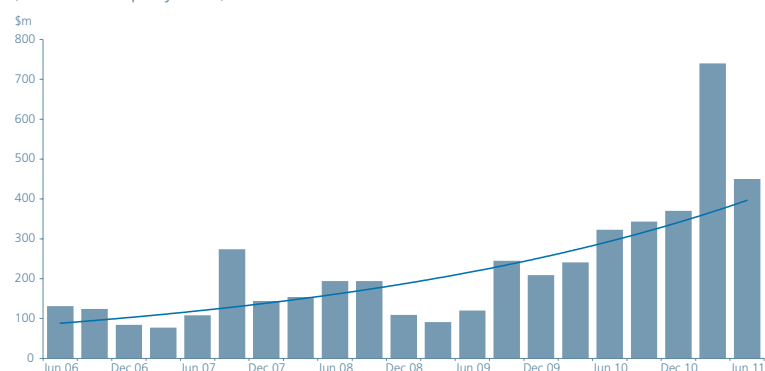
(Source: Company Data)



Sustained growth in Normalised NPAT and Normalised Basic EPS

Quarterly Growth in Annuity Sales

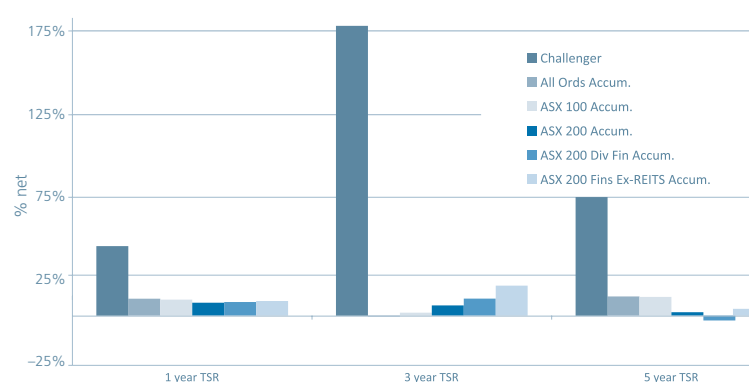
(Source: Company Data)



Accelerating growth in quarterly annuity sales

Total Shareholder Return (TSR)

(Source: IRESS – period ended 30 June 2011)



One, three and five year TSR consistently above market

2011 Remuneration Snapshot

The following table provides a summary of the action the Board has taken, or will be taking, in response to the concerns raised by shareholders about various aspects of the Company's remuneration arrangements.

	Board action/comment	More details (page)
Quantum of remuneration	<p>The Board recognises that executive remuneration is generally higher than companies in the ASX 75–125 with similar market capitalisation. This is because the Board looks to draw its executives from the specialist talent pool found in Investment and Commercial Banking disciplines that have remuneration structures significantly different to that of the ASX 75-125. The Board's approach and reasons for this are explained in more detail on page 42.</p> <p>For the 2011 year, the Board revisited the comparator companies and positions to determine the appropriateness of the remuneration structure for each executive position.</p>	41
Short Term Incentives (STI)		
Performance measures and how they were assessed	<p>The Board sets objectives for each individual on the basis of a balanced scorecard. For the 2011 year, the objectives were set and conveyed to executives in July 2010.</p> <p>In August 2011, the Board assessed the performance of each key executive against their scorecard and determined their STI award. The scorecard outcomes are shown in the table on page 46.</p> <p>Each key executive's 2011 awarded STI is shown in the table on page 48.</p> <p>The performance objectives that were set for the key executives at the beginning of the year are described in more detail on page 42.</p>	42, 46, 48
STI pool calculation	<p>The Board has continued to use a funding range for the STI pool of between 8% and 12% of Net Profit Before Bonus and Tax (NPBBT) as outlined on page 41.</p> <p>The Board reviews the Group performance at the end of the year and determines the limit of the STI pool. For the 2011 year the Board limited the STI pool to 10% of NPBBT.</p> <p>Specific details of the Group's performance are shown on page 36.</p>	36, 41
Deferral of STI	<p>The Board reserves the right to deliver the key executives' STI award in full as cash payment, partially deferred or wholly deferred. The deferred proportion is delivered as Performance Share Rights (PSR) and is subject to forfeiture if the employee terminates employment.</p> <p>50% of the STI awarded to executives in August 2011 was paid in cash, and 50% was deferred over two years.</p>	42
Long Term Incentives (LTI)		
Length of vesting period	<p>In previous years, one-third of the LTI vested in each of the first, second and third year after grant.</p> <p>In 2011, the Board changed the vesting period to extend it over four years. Provided the performance hurdle is met, one-third of the LTI may vest in the second year, one-third in the third year and one-third in the fourth year. In this way the Board has extended the vesting period.</p>	42, 43
Use of alternate performance hurdles/ absolute TSR hurdle	<p>In previous years, the LTI could vest if either a total shareholder return (TSR) hurdle or earnings per share hurdle were met. Some shareholders indicated concern with the use of multiple hurdles.</p> <p>Having a regard for these concerns, in August 2010 the Board changed the prior arrangements and has set only one hurdle as outlined below.</p> <p>Some shareholders have advised that they would prefer the Company to use a relative TSR hurdle. The Board has continued to review the appropriateness of the TSR hurdle and has explained in more detail on pages 43 and 44 why it determined that the LTI would be measured against an absolute TSR hurdle in the range of 8%-12% compounding.</p>	43, 44

	Board action/comment	More details (page)
Setting appropriate and consistent share valuation methodology	<p>In April 2009, the Board set a policy that all measurement of equity performance related to remuneration plans would be determined using a longer term volume-weighted average price (VWAP) calculation. The use of a 90 day VWAP will result in less risk of erroneous price movements or price manipulation that could advantage or disadvantage employees.</p> <p>The Board considers the 90 day VWAP to be the most appropriate way to value the equity instruments for these purposes and that it should be consistent in this regard.</p> <p>The 2010 and 2011 awards have therefore followed this methodology and the Board proposes to continue with this methodology.</p>	45
Equity instrument	In 2011, the Board changed from granting Options to granting Hurdled Performance Share Rights (HPSRs). HPSRs were considered to be the most appropriate equity instrument to motivate and reward employees without excessive dilution for shareholders, leverage or adverse tax outcomes for the employees.	43
Other		
Employee ownership	<p>While many shareholders have indicated they have no policy on minimum or maximum levels of employee ownership, others have indicated they prefer that employee ownership does not exceed 10% of issued capital. Generally, the Board encourages executive and employee ownership because it believes greater ownership increases the alignment of employee interests with those of the wider shareholder group.</p> <p>In 2011, employee ownership, by way of unvested equity instruments awarded, has reduced to approximately 7% of issued capital. The Board continues to monitor employee ownership and proposes to maintain the level below 10%.</p>	

Key Management Personnel

This audited Remuneration Report describes Challenger's director and executive remuneration arrangements as required by the *Corporations Act 2001*. The report covers Key Management Personnel (KMP). These personnel include the five highest remunerated executives of the Group and those who have authority and responsibility for planning, directing and controlling the major activities of the Company and the Group.

Name	Current role
Dominic Stevens	CEO and Managing Director
Rob Adams	Joint Chief Executive, Funds Management*
Brian Benari	Group Chief Financial Officer/Chief Operating Officer
Richard Howes	Chief Executive, Life
Paul Rogan	Chief Executive, Distribution Product & Marketing
Robert Woods	Chief Executive, Funds Management

*KMP until 25 February 2011.

Remuneration Principles – Key Management Personnel

Challenger aims to provide remuneration that is market competitive and linked to long term shareholder value creation. It is made up of the following components:

Instrument	Link to business strategy
Fixed remuneration including: <ul style="list-style-type: none">• base salary (which is guaranteed and comprises salary, including salary sacrifice benefits and applicable fringe benefits tax); and• employer superannuation contributions	Fixed remuneration reflects a competitive base relative to market data for comparable roles and skills.
Short term incentive which is at risk and may include cash or equity, and is dependent on company, business unit and individual performance: <ul style="list-style-type: none">• 50% paid in current year• 50% deferred for 24 months	Short term incentives are awarded to reflect performance over the previous 12 months. For KMP's these incentives are paid 50% in cash and 50% are awarded in Challenger shares (PSR) and deferred for up to two years. Deferred STI is subject to claw back provisions – refer page 42.
Long term incentive: <ul style="list-style-type: none">• four-year performance period• total shareholder return hurdle	<p>Longer term incentives are awarded annually based on a range of criteria reflecting, in addition to current year performance, the longer term ability for an employee to add significant value to the Company and KMP retention. LTI ensures longer term alignment of interests between Challenger and the KMP.</p> <p>These incentives are awarded in Challenger shares that vest over a period of four years subject to meeting certain performance hurdles. If those performance hurdles are not met, no awards will vest to the employee. In addition, there are clawback mechanisms within the Challenger Performance Plan (CPP) to allow the Board discretion under certain circumstances to void awards.</p>

Together, these components make up an executive's total remuneration. When setting Challenger's total remuneration levels, the Board consider the size of the role and its responsibilities and also considers the market for similar skills. To support this, we participate in a number of executive remuneration surveys. Challenger's goal is always to remain competitive, and we aim to set total remuneration at levels for similar roles and skill base.

Governance Structure and Risk Management

The Board convenes a Remuneration Committee comprised of Independent Directors that has at least three members and is chaired by an Independent Director.

The background details of the Remuneration Committee members are contained in the Directors' report. The Committee meets at least four times a year, with additional meetings scheduled as required. The Committee met five times during the year to 30 June 2011.

	Role
Board	<ul style="list-style-type: none"> Has the ultimate responsibility for approving Remuneration principles and structures, ensuring that they are competitive, equitable and support the long term interests of the Company Receives recommendations from the Remuneration Committee as set out below and approves these recommendations where appropriate
Remuneration Committee	<p>Determines and recommends to the Board for approval:</p> <ul style="list-style-type: none"> The reward principles and policies including: <ul style="list-style-type: none"> remuneration, recruitment, retention and termination policies; and diversity as it relates to remuneration CEO and senior executives' remuneration and incentives Superannuation and life insurance arrangements The remuneration framework for Directors
External consultants	<p>Engaged by the Board and Remuneration Committee to provide remuneration and market practice advice and information to the Board. In February 2011, the Board Remuneration Committee engaged KPMG independently of management to advise the Board in its review of the Group's remuneration arrangements.</p> <p>Prior to engaging KPMG as independent remuneration adviser to the Remuneration Committee, independent advice was provided by Guerdon Associates.</p> <p>Although the <i>Corporations Amendment (Improving Accountability on Director and Executive Remuneration) Act 2011</i> was introduced with effect only for contracts entered into on or after 1 July 2011, the Board has sought to implement the underlying principles of the legislation for the year ended 30 June 2011.</p> <p>The engagement of KPMG by the Remuneration Committee was based on an agreed set of protocols that would be followed by KPMG, members of the Remuneration Committee and members of the key management personnel for the way in which remuneration recommendations would be developed by KPMG and provided to the Board.</p> <p>These arrangements were implemented to ensure that KPMG would be able to carry out its work, including information capture and the formation of its recommendations, free from undue influence by members of the key management personnel about whom the recommendations may relate.</p> <p>The Board undertook its own enquiries and review of the processes and procedures followed by KPMG and is satisfied that its remuneration recommendations were made free from such undue influence.</p>

Implementing Remuneration Policy

How fixed remuneration is determined

Fixed remuneration is comprised of base salary and employer superannuation. It is aimed at, or around the market median for similar skills and for those companies against which Challenger competes for talent.

Key to Challenger's business strategy and success has been the attraction, retention and motivation of its executives; recognising that key skills it seeks attract a premium. Therefore, remuneration needs to be positioned against relevant external benchmarks.

As highlighted on page 35, Challenger competes for executives from a narrow and specialist pool of talent. Challenger looks for executives who have had deep experience in capital markets and financial risk management and may come from investment banks or the institutional or commercial arms of major trading banks. Whilst these organisations may have a different business mix to Challenger, they compete for the same executives and form part of the relevant peer group for remuneration comparison purposes.

During 2011, remuneration data from the companies against which Challenger competes for talent was considered and formed a key input into the remuneration outcomes, along with individual and Group performance and assessment of retention risks.

How the bonus pool (or STI) is calculated

Based on Challenger's current business mix, a formula is used to link STI outcomes with Group performance. The formula ensures that the STI pool is correlated with performance and has been historically between 8% and 12% of Net Profit Before Bonus and Tax (NPBBT) and for the 2011 financial year was set at 10% of NPBBT. Whilst the funding formula sets a range for the size of the STI pool, the Board still has flexibility to move within the above range taking into consideration unforeseen circumstances.

How short term performance drives STI through the financial year

The Board believes that executive STI must align to Group, business unit and individual performance. This means that it will decrease or increase the amount of STI paid for either underperformance or outperformance versus key performance indicators (KPIs).

The table below provides a summary of the STI plan and its key features:

Plan feature	Detail
Performance targets	KPIs are designed to ensure a focus on the achievement of Challenger's business strategy.
Purpose	The STI arrangements support Challenger's remuneration strategy of rewards based on performance against annual KPIs.
Determining individual incentive targets	<p>STI performance objectives are managed through a balanced scorecard approach (refer page 42). The selection of financial and non-financial performance objectives are chosen in order to align performance with business strategy.</p> <p>These performance objectives are communicated to each executive at the beginning of the performance year. This effectively focuses each executive on key performance objectives given the STI that they will ultimately receive will depend on performance against those objectives.</p>
Rewarding performance	The STI plan rewards outstanding performance. The actual STI payment made at the end of each financial year is determined based on performance against individual KPIs and relative to peer KMPs in the Company.
Mandatory deferral	This year, 50% of the STI is paid in cash at the end of the financial year. The remaining 50% of KMPs STI is currently deferred over two years and is delivered to the executive as performance share rights to encourage sustainable shareholder outcomes and alignment. Forfeiture will occur under certain circumstances outlined below.
Number of rights	The plan uses the 90-day volume weighted average price (VWAP) in determining the number of share rights issued per dollar of awarded value of deferred STI.

Executives' performance evaluations are conducted following the end of each financial year. Performance evaluations for the 2011 financial year were conducted in July 2011. Similarly, performance evaluations for the 2010 financial year were conducted in July 2010.

How a balanced scorecard measures performance for KMP STI

The STI is paid on the achievement of specific objectives in the areas of financial outcomes, business growth, risk management and people development. These objectives are set at the beginning of the financial year and the Board assesses the performance of each executive against each of these objectives and the extent to which the executive's behaviours are supportive of the Company's principles and strategy. A summary of these objectives for 2011 is detailed below.

Objective	Performance measure	Measurement	Link to business strategy
Financial	Normalised NPAT and EPS	Delivery against budget	Growth in NPAT and EPS to deliver increased shareholder value
	Return on Net Assets (RONA)	Delivery against budget	Return on net assets to meet a hurdle of 18% pre-tax
Growth	Implementation of key growth initiatives and lift in advertising awareness	Net growth in FUM and annuities sales Increased advertising recognition and awareness	Growth in our target markets (wealth, superannuation and retirement), greater than underlying system growth
Risk	Effective risk management	Compliance with Board Risk Appetite Statement	Ensuring the Company manages risk within defined parameters and regulatory requirements
People development	Employee engagement, talent development and diversity	Employee turnover Diversity metrics	Engaged and developed staff retained

How KMP STI can be clawed back – delivery and forfeiture

Reflecting the emphasis on sustainable returns over the longer term, 50% of the STI is paid in cash at the end of the financial year. The remaining 50% is deferred over two years and is delivered to the KMP as performance share rights (on Challenger Limited shares). Both the cash and equity element of the STI may be forfeited if the KMP leaves employment prior to payment.

The STI may also be reduced or forfeited should the Board determine that the bonus outcome was achieved where an executive:

- commits an act of dishonesty;
- is ineligible to hold their office for the purposes of Part 2D.6 of the *Corporations Act 2001*; or
- is found to have acted in a manner that the Board considers to be gross misconduct or is dismissed with cause.

In addition, the Board may resolve that the bonus outcome (or part of the bonus outcome) should be reduced or forfeited in order to:

- protect the financial soundness of the Company; or
- respond to unexpected or unintended consequences that were significant and unforeseen by the Board (such as material risk management breaches, unexpected financial losses by the Company, reputational damage or regulatory non-compliance).

How longer term performance drives LTI over four years

Long term incentives focus executives on Challenger performance over the longer term. Performance hurdles for our long term incentive plan were specifically chosen to support our business strategy, and to drive the long term creation of shareholder value. Performance hurdles must be achieved before an executive can receive any value from this portion of their target remuneration.

LTI reward is linked to the long term performance of the Company and will only begin to vest once an 8% level of Total Shareholder Return (TSR) is reached. Full vesting occurs when a 12% level of TSR for shareholders is reached.

Hurdled Performance Share Rights (HPSRs) were granted under the LTI plan in September 2010 following the 2010 remuneration cycle. An overview of the plan is detailed below.

Plan feature	Detail	
Instrument	HPSRs are the right to receive a fully paid ordinary share for zero consideration. HPSRs do not provide an entitlement to vote or a right to dividends.	
Number of rights	The number of HPSRs granted to an executive is calculated by reference to the estimated fair value of the LTI award approved by the Board.	
Grant date	September 2010	
Maturity	September 2014	
Performance hurdle	Absolute Total Shareholder Return (TSR)	
	Compound annual growth rate of absolute TSR	Percentage of rights that vest
	Less than 8% per annum	0%
	8% or greater, but less than 12%	Pro-rata vesting between 33% and 100%
	Above 12% per annum	100%
Vesting schedule	<p>The performance rights will vest in windows if the relevant performance hurdles have been met over the following dates:</p> <ul style="list-style-type: none"> • One third commences vesting in September 2012 • One third commences vesting in September 2013 • One third commences vesting in September 2014 	

Equity instrument changes – move from options to hurdled performance share rights

In August 2010, the Board reviewed the type of equity instrument that should be granted under its LTI plans. This move followed regulatory and tax reform undertaken by the Australian Federal Government during 2010 and was reflective of a general trend by ASX listed entities towards the issuance of performance share rights.

While the instrument for LTI has changed, the awarded value of LTI has been determined under the same principles as in previous years and, as indicated earlier, has been reducing over time.

Use of an absolute TSR

TSR represents the change in share price plus dividends received over a given timeframe.

The Board believes that an absolute TSR is the only effective way to both incentivise and measure whether Challenger has delivered an increase in fundamental value to its shareholders. The Board decided an absolute rather than relative TSR was appropriate for the following reasons:

- There are no other listed companies in the Australian market with a retirement income business that are directly comparable to Challenger.
- Comparing Challenger's TSR to a broader index can provide outcomes that may not be indicative of the Company's performance given its differentiated position in the retirement sector.
- Key stakeholders, shareholders and proxy advisers have indicated a broader index is generally not considered an appropriate comparator group as the result can result in a misalignment of executive reward from shareholder value creation.
- Global regulators such as the Bank of International Settlement (BIS) through Basel Supervision prefer absolute measures for established rather than start-up firms. *"Relative benchmarks may result in sub-optimal absolute performance, if the only standard is that peers perform worse. It is also possible that relative performance measures may encourage 'herd mentality', in which firms and/or employees have an undue tendency to mirror peers' behaviour to stay close to their benchmark. If the same relative measures are widely used, this could have pro-cyclical consequences for the global financial system¹."*
- If the absolute TSR hurdle is set at a level that is above average market returns over the long term, then executives' reward will be directly linked to the superior returns achieved by all shareholders.

¹ Basel Report – Range of Methodologies for Risk and Performance Alignment of Remuneration – May 2011.

The Board has set the absolute TSR hurdle targets as outlined on page 44. These targets reflect expectations of what the Board considers to be appropriate long term hurdles for LTI remuneration to vest. These targets were set following significant research into:

- Long term returns of listed equities.
- Long term returns of listed financial services firms in general, and with reference to insurance companies and diversified financial firms.
- The importance of risk management and the negative consequences of a higher TSR hurdle that over the longer term could encourage imprudent risk taking.
- An objective to move from a cliff vesting hurdle into a hurdle that gradually vested over a range of outcomes.
- An objective to produce long term sustainable outcomes such that:
 - zero vesting would occur if the return was below a minimum level (8% TSR), an outcome lower than long term averages of a selection of equities indices (outlined in the chart below);
 - full vesting would occur if the return was above a level (12% TSR) being a significantly higher return than long term averages of a selection of equities indices (outlined in the chart below);
 - partial vesting between these two levels.

In setting these hurdles, the Board had regard for the longer time horizon in the last 10 years in Australia and noted that:

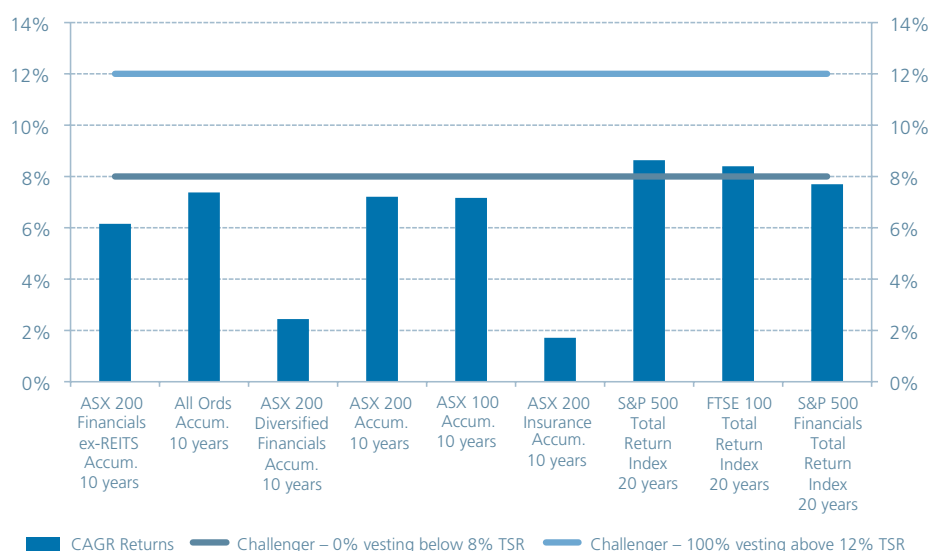
- the All Ordinaries Accumulation Index has achieved a compound annual growth in TSR of 7.4%;
- the ASX 100 Accumulation Index has achieved a compound annual growth in TSR of 7.2%;
- the ASX 200 Accumulation Index has achieved a compound annual growth in TSR of 7.2%;
- the ASX 200 Diversified Financials excluding REITS Accumulation Index has achieved a compound annual growth in TSR of 6.2%;
- the ASX 200 Diversified Financials Accumulation Index has achieved a compound annual growth in TSR of 2.4%; and
- the ASX 200 Insurance Accumulation Index has achieved a compound annual growth in TSR of 1.7%.

The Board also identified that over the longer time horizon of 20 years overseas indices have produced similar trends:

- the S&P 500 Total Return Index has achieved a compound annual growth in TSR of 8.6%;
- the S&P 500 Financials Total Return Index has achieved a compound annual growth in TSR of 7.7%; and
- the FTSE 100 Total Return Index has achieved a compound annual growth in TSR of 8.4%.

This information is summarised in the chart below.

Absolute TSR – Compound Average Growth Rates (CAGR) over 10 and 20 years
(growth rates measured to 30 June 2011)



As an example, a compound annual growth rate in TSR of 12% over four years means a share worth \$5.00 today and paying 15 cents dividend each year, would produce a total return of \$7.74 (or absolute growth of 55%) for the LTI to fully vest.

It is for these reasons that the Board determined the LTI grant would be measured against the absolute TSR range specified of 8%-12%. Notwithstanding this, the Board each year considers the most appropriate way of linking sustainable shareholder value creation and executive reward, and will again undertake a review of the performance hurdle in 2012.

Volume Weighted Average Price (VWAP) calculation

In April 2009, the Board set a policy that all measurement of equity performance related to remuneration plans be done via a longer term VWAP calculation.

The use of a 90 day VWAP results in less risk of erroneous price movements or price manipulation that could advantage or disadvantage employees. This was in line with the Australian Prudential Regulation Authority (APRA) guidelines that require Boards to ensure risk is appropriately mitigated within remuneration plans.

Since 2009 all issuance of equity via Performance Options or Performance Share Rights has been done with reference to a 90 day VWAP leading up to the award date. To be consistent, all calculations of TSR hurdles required to be met for vesting are also calculated using a consistent reference to a 90 day VWAP leading up to the final date of the relevant performance period.

Distributions from the Challenger Performance Plan (CPP) Trust

To maximise alignment with shareholders, Challenger has biased remuneration towards variable awards and long term incentives. Challenger shares held within the CPP Trust to satisfy future awards (either deferrals of STI into performance share rights or LTI in the form of options or hurdled performance share rights) receive income in the form of declared dividends. Income received by the CPP Trust cannot be paid back to the Company and to avoid adverse tax outcomes, the Trustee retains the right to distribute income from the Trust to potential beneficiaries.

The Board believes that distribution of dividends provides a further incentive for employees to drive alignment for shareholders.

Performance share rights received as a result of deferred remuneration receive preference in regard to any income for distribution. If a distribution is made, each performance share right relating to deferred STI will receive a maximum amount equal to Challenger's full year declared dividend.

If any residual income balance is available in the CPP Trust, the allocation to LTI holders is established by reference to a probability of vesting calculation for each series of issuances. The probability of vesting calculation is performed by an independent consultant.

Any income distributed to individuals from the CPP Trust is taken into account by the Remuneration Committee when considering STI determinations for the period and total remuneration awarded.

Employee share trading policy

All employees must comply with Challenger's employee share trading policy. All employees are required to obtain pre-approval from the Company Secretary if they wish to trade in Challenger shares. Employees are prohibited from trading during specified black-out periods, including prior to the release of the Group's financial results.

Under this policy, employees are also prohibited from hedging their unvested share awards including performance share rights and performance share options. In the Board's view, hedging unvested awards goes against the intention for which long term incentives are granted to employees. Where a person is found to have breached this requirement it will be regarded as serious misconduct and may be grounds for dismissal.

Challenger prohibits directors and employees from taking out margin loans on Challenger shares, with any exceptions to this rule requiring formal Board approval. There have been no exceptions to this prohibition in 2011.

Minimum shareholding for Non-Executive Directors and KMP

Challenger introduced equity holding guidelines that apply to KMP and Non-Executive Directors from 1 July 2010.

Under the guidelines, KMP are expected to maintain a minimum holding of 100,000 Challenger shares. Non-Executive Directors are expected to maintain a minimum holding of 20,000 Challenger shares. All will be expected to have achieved the minimum shareholding level by 1 July 2012.

The Board will retain the discretion to allow KMP and Non-Executive Directors to vary from this guideline policy.

In the Board's view, maintaining these significant levels of shareholdings in tandem with other alignment features of the remuneration mix reduces the potential for excessive risk taking and further strengthens alignment with shareholders.

2011 outcomes – performance against metrics and achievements for the year

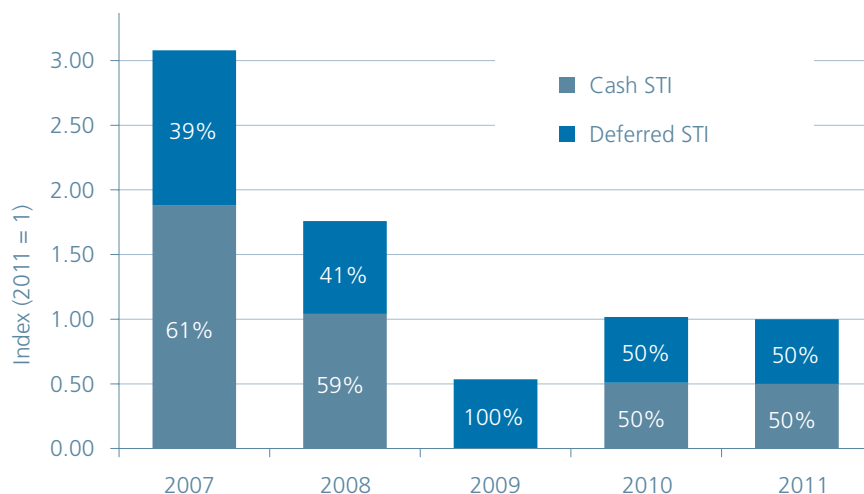
A formula is used to link STI outcomes with the Group's performance. The formula ensures that the STI pool is correlated with performance and has been historically between 8% and 12% of Net Profit Before Bonus and Tax (NPBBT). Whilst the funding formula sets a range for the size of the STI pool, the Board has flexibility to move within the above ranges taking into consideration under or outperformance. The STI and LTI outcomes for 2011 are included on page 47.

For financial year 2011 the Board limited the STI pool to 10% of NPBBT. Each executive's individual and business unit performance was then assessed by the Board with reference to the performance objectives set for them at the beginning of the year. The Group's outcome against each performance measure is shown below and the individual executive's award is shown on page 48:

Objective	Performance measure	Actual outcome	Actual outcome versus 2010	Outcome versus budget
Financial	Normalised NPAT	\$248m	up 6.4%	Exceeded budget by 4.5%
	Normalised EPS	51.7 cents	up 14%	Exceeded budget by 4.7%
	Return on Net Assets (RONA)	23.2%	up 220bps	Exceeded budget of 20.1% by 3.1 percentage points
Growth	Implementation of key growth initiatives and lift in advertising awareness	<p>Growth in Life retail annuity sales of 104% up from \$933.1 million to \$1,903.6 million.</p> <p>Growth in Boutique FUM of 111% up from \$7.0 billion to \$14.8 billion.</p> <p>44% of our target consumer audience, and 57% of advisers recall having seen our advertisements. Those advisers are 50% more likely to recommend Challenger annuities to their retired clients.</p>		
Risk	Effective risk management	<p>The scoreboard measure for risk involves the Board's assessment of performance against the Board Risk Appetite Statement. Performance for 2011 includes:</p> <ul style="list-style-type: none"> • maintenance of credit ratings; • a strengthened capital position for Challenger Life Company Limited; and • no material operational or compliance breaches. 		
People development	Employee engagement, talent development and diversity	<p>Employee turnover within industry averages of 16-18%.</p> <p>Percentage of women employed in senior roles at Challenger increased 12%.</p>		

STI outcomes

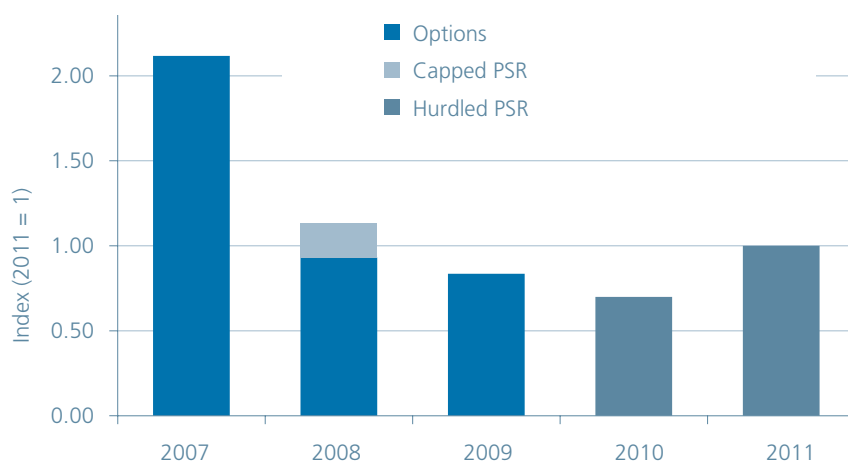
STI awarded to KMP over the past five years is outlined in the chart below.



- Consistent with 2010, 50% of short term incentives awarded in 2011 were deferred.
- The short term incentive pool has reduced since 2007 following changes in the business mix and in external market conditions.

LTI outcomes

Long term incentive awards are based on a range of criteria reflecting, in addition to current year performance, the longer term ability to add significant value to the Company and for retention purposes. LTI awarded to KMP over the past five years is outlined in the chart below.



- The Board has determined an award value of LTI for the current performance period. The terms and conditions of that LTI award are consistent with the information contained in the table on page 43.
- The amounts awarded to KMP are outlined in Table 1 on page 48.
- The chart outlines the trend of reducing awarded LTI instruments over the last five years.

2011 Remuneration Tables – Summary

Over the past 10 years the quantum and complexity of information required within Remuneration Reports has increased.

KMP have received a mix of remuneration, with a portion paid during the year, and a portion received between three to six years later, depending on service and performance. This can make it difficult for stakeholders to obtain a clear view of the actual amount of remuneration an executive received in the financial year in review.

Noting the above, the Board has undertaken to provide greater clarity and transparency around its remuneration. On pages 48 to 50 are three remuneration tables:

Table 1. Remuneration **awarded** to KMP (new for 2011).

- This table represents the value of remuneration that has been awarded for the annual performance period. This includes all base salary and superannuation, STI (both cash and the value of deferrals into PSR) and the award value of the current year LTI. This information is reflective of what the KMP receives in their annual remuneration statement.

Table 2. The **statutory** view of KMP remuneration

- This table reflects the accounting expense of KMP remuneration incurred in the year to 30 June 2011. As such, it includes amortisations of all current and historical remuneration plans, some of which were granted as far back as 2004. This results in an attribution of the accounting cost of equity issuance over the term of the plans and may bear little relation to the current award or business performance.

Table 3. The **realised** view of KMP remuneration

- This table reflects the actual benefit realised by the KMP during the year. This may be from base salary and STI, but also from vesting of STI and LTI awards issued in the past. Again, this may bear little relationship to current awards or business performance, and is driven instead by a greater correlation to vesting dates and historical share price movements.

These three measures can diverge significantly particularly given the market turbulence of the last five years. As mentioned above, the Board sees the most important metric as being the remuneration awarded during the year, which is in line with recent suggestions on the presentation of remuneration tables by the Corporations and Markets Advisory Committee (CAMAC).

Table 1 – Awarded Remuneration

Key points

Overall Awarded Remuneration has fallen significantly since 2007 as outlined on page 35.

The lower overall Awarded Remuneration has been combined with higher weighting to variable remuneration.

This strikes the appropriate balance between broader market expectations while maintaining incentives that encourage executives to strive for outperformance and increased shareholder returns.

	Year	Short term employee benefits			Post-employment super	Share based payments ² (LTI)	Other ³	Total awarded
		Salary ¹	Cash STI	Deferred STI				
		\$	\$	\$	\$	\$	\$	\$
Dominic Stevens	2011	992,606	1,050,000	1,050,000	15,199	1,462,500	1,016,904	5,587,209
	2010	990,795	1,100,000	1,100,000	14,461	1,417,500	1,285,143	5,907,899
Brian Benari	2011	639,405	875,000	875,000	15,199	1,170,000	678,779	4,253,383
	2010	639,750	925,000	925,000	14,461	661,500	1,182,979	4,348,690
Richard Howes	2011	635,887	750,000	750,000	15,199	1,170,000	648,175	3,969,261
	2010	636,414	750,000	750,000	14,461	661,500	1,128,880	3,941,255
Paul Rogan	2011	634,801	550,000	550,000	15,199	975,000	484,885	3,209,885
	2010	635,539	425,000	425,000	14,461	378,000	503,578	2,381,578
Robert Woods	2011	638,451	700,000	700,000	15,199	1,170,000	644,013	3,867,663
	2010	638,847	650,000	650,000	14,461	661,500	1,130,497	3,745,305

¹ Salary includes the cost of Death, TPD and Salary Continuance insurances.

² The Long Term Incentive (LTI) will be delivered in the form of Hurdled Performance Share Rights (HPSRs). The value of the HPSRs awarded to each KMP has been determined by reference to the estimated fair value of the number of HPSRs approved by the Board on 18 August 2011. The HPSRs will be formally granted in September 2011 and so the fair value of the awards is subject to change depending mainly on the Challenger share price at the date of grant.

³ Interest amounts accrued in the year on the loan taken out by individuals to acquire Challenger shares and dividend payments received from the Challenger Performance Plan Trust.

Table 2 – Statutory Remuneration

Key points

Statutory remuneration has significantly fallen from 2010 levels.

Amortisation over three or four years (term of long term incentive plans) results in a distortion between statutory share based payments versus awarded payments.

	Year	Short term employee benefits		Post-employment super \$	Share based payments ²		Cash settled shares and units \$	Other ³ \$	Total awarded \$
		Salary ¹ \$	Cash STI \$		Equity settled shares and units \$	Equity settled options and rights \$			
Dominic Stevens	2011	992,606	1,050,000	15,199	–	2,784,683	–	1,016,904	5,859,392
	2010	990,795	1,100,000	14,461	220,635	2,686,246	330,000	1,285,143	6,627,280
Brian Benari	2011	639,405	875,000	15,199	4,251	3,129,561	–	678,779	5,342,195
	2010	639,750	925,000	14,461	65,458	3,690,820	650,000	1,182,979	7,168,468
Richard Howes	2011	635,887	750,000	15,199	28,523	2,618,953	–	648,175	4,696,737
	2010	636,414	750,000	14,461	138,610	2,886,824	120,000	1,128,880	5,675,189
Paul Rogan	2011	634,801	550,000	15,199	369,751	1,188,739	–	484,885	3,243,375
	2010	635,539	425,000	14,461	778,759	1,421,670	–	503,578	3,779,007
Robert Woods	2011	638,451	700,000	15,199	4,251	2,563,840	–	644,013	4,565,754
	2010	638,847	650,000	14,461	53,306	2,914,393	–	1,130,497	5,401,504
Rob Adams⁴	2011	636,316	280,500	15,199	(227,367)	1,053,061	–	349,837	2,107,546
	2010	637,034	425,000	14,461	157,553	1,320,221	650,000	131,861	3,336,130
Drew Hall⁴	2011	–	–	–	–	–	–	–	–
	2010	211,846	–	4,820	(35,798)	1,730,759	–	–	1,911,627

¹ Salary includes the cost of Death, TPD and Salary Continuance insurances.

² The value of the equity settled shares and units and equity settled options and rights is calculated on the basis outlined in Note 1 (xxxiii) to the financial statements and reflects the fair value of the benefit derived at the date at which they were granted. The fair value is determined using an option pricing model. As the majority of the Company's equity settled share-based payment rewards are subject to share price based performance hurdles (e.g. TSR of the Company), no adjustment to the fair value after grant date is allowed to be made for the likelihood of the market performance conditions not being met. Therefore, the value of the reward included in the table may not necessarily have been vested to the Key Executives during the year.

³ Interest amounts accrued in the year on the loan taken out by individuals to acquire Challenger shares and dividend payments received from the Challenger Performance Plan Trust.

⁴ Mr Adams ceased to be a Key Executive on 25 February 2011. Mr Hall ceased to be a Key Executive on 31 October 2009. Disclosures for Mr Adams and Mr Hall cover the period when they were Key Executives.

Table 3 – Realised Remuneration

Key points

Statutory remuneration has fallen from 2010 levels; however, realised remuneration has risen.

Realised remuneration increased due to vesting of incentive plans from the prior four years, coupled with material outperformance of the Challenger share price.

	Year	Short term employee benefits		Post-employment super \$	Share-based payments		Other ⁴ \$	Total realised remuneration ⁵ \$
		Salary ¹ \$	Cash STI \$		Value of prior year's LTI tranches at issue ² \$	Value due to share price appreciation of prior year's LTI ³ \$		
Dominic Stevens	2011	992,606	1,050,000	15,199	2,059,993	2,181,161	1,016,904	7,315,863
	2010	990,795	1,100,000	14,461	1,259,996	3,874,674	1,285,143	8,525,069
Brian Benari	2011	639,405	875,000	15,199	1,906,646	6,773,519	678,799	10,888,568
	2010	639,750	925,000	14,461	1,206,658	4,105,330	1,182,979	8,074,178
Richard Howes	2011	635,887	750,000	15,199	1,354,166	6,297,007	648,175	9,700,434
	2010	636,414	750,000	14,461	1,004,161	2,843,934	1,128,880	6,377,850
Paul Rogan	2011	634,801	550,000	15,199	1,054,846	2,806,986	484,885	5,546,717
	2010	635,539	425,000	14,461	1,170,740	804,901	503,578	3,554,219
Robert Woods	2011	638,451	700,000	15,199	1,420,832	6,270,387	644,013	9,688,882
	2010	638,847	650,000	14,461	1,070,827	3,310,961	1,130,497	6,815,593

¹ Salary includes the cost of Death, TPD and Salary Continuance insurances.

² Represents the value of performance rights vesting during the period, at original grant price.

³ Represents the share appreciation on performance rights, options, cash LTI plan and other LTI that vested during the year based on the value at vesting date. The value is net of any exercise cost.

⁴ Interest amounts accrued in the year on the loan taken out by individuals to acquire Challenger shares and dividend payments received from the Challenger Performance Plan Trust.

⁵ Whilst there are no formal accounting standards that provide guidance as to the disclosure, measurement and classification of remuneration amounts to be included in a Realised Remuneration Table, the 2011 Share Based Payments and Other Award values have been prepared in consideration of announcements made by the Productivity Commission's inquiry into Executive Remuneration in Australia (released 4 January 2010) and the Corporations and Markets Advisory Committee Executive Remuneration Report (released 25 May 2011). The 2010 share based payments and other award values have been restated on a basis consistent with the 2011 disclosures. These restatements pertain to the measurement of option and performance rights awards based on the vesting date, regardless of whether the award was exercised by the KMP on that date and interest amounts paid in relation to Third Party Loan Facilities.

Terms and conditions of Performance Share Rights (PSR) and Hurdled Performance Share Rights (HPSRs) granted for the year

PSR were granted in September 2010 in relation to the 2010 deferred STI awards and will vest over two years subject to service conditions only. Participants realise the same growth as shareholders therefore sustainability of share price growth remains a key focus.

Performance Share Rights granted to the CEO and Key Executives during the year ended 30 June 2011

Executive	Compulsory deferral from 2010 \$	Deferred %	Allocation price \$	Number of rights granted	Date of grant	Vesting 15 September 2011		Vesting 15 September 2012	
						Number	Fair value at grant \$	Number	Fair value at grant \$
D Stevens	1,100,000	50	3.724	295,381	15 Sept 10	147,690	3.79	147,691	3.65
R Adams*	425,000	50	3.724	114,124	15 Sept 10	57,062	3.79	57,062	3.65
B Benari	925,000	50	3.724	248,388	15 Sept 10	124,194	3.79	124,194	3.65
R Howes	750,000	50	3.724	201,396	15 Sept 10	100,698	3.79	100,698	3.65
P Rogan	425,000	50	3.724	114,124	15 Sept 10	57,062	3.79	57,062	3.65
R Woods	650,000	50	3.724	174,543	15 Sept 10	87,271	3.79	87,272	3.65

*R Adams ceased to be a Key Executive on 25 February 2011.

The Company granted HPSRs to KMP in September 2010. The HPSRs ensure KMP make sound decisions driving shareholder value and company performance. As HPSRs have an absolute TSR hurdle of 8-12% they are designed to motivate long term sustainable share price growth.

Hurdled Performance Share Rights granted to Key Executives during the year ended 30 June 2011

Executive	Grant date	Allocation price \$	Number of rights granted	Tranche 1 15 September 2012		Tranche 2 15 September 2013		Tranche 3 15 September 2014	
				Number vesting	Fair value at grant \$	Number vesting	Fair value at grant \$	Number vesting	Fair value at grant \$
D Stevens	8 Sept 10	3.724	750,000	250,000	2.02	250,000	2.02	250,000	2.02
R Adams*	8 Sept 10	3.724	200,000	66,666	2.02	66,667	2.02	66,667	2.02
B Benari	8 Sept 10	3.724	350,000	116,666	2.02	116,667	2.02	116,667	2.02
R Howes	8 Sept 10	3.724	350,000	116,666	2.02	116,667	2.02	116,667	2.02
P Rogan	8 Sept 10	3.724	200,000	66,666	2.02	66,667	2.02	66,667	2.02
R Woods	8 Sept 10	3.724	350,000	116,666	2.02	116,667	2.02	116,667	2.02

*R Adams ceased to be a Key Executive on 25 February 2011.

Mr Stevens was not granted Share Options in this financial year. Mr Stevens' last grant of Share Options was upon his appointment as CEO and was approved by shareholders at the Annual General Meeting on 20 November 2008.

For full details of all new issues and awards vested from the Challenger Performance Plan during the period see Note 31 *Employee entitlements* in the Financial Report.

CEO employment agreement: notice periods

Mr Stevens is not on a fixed term contract. Mr Stevens was appointed CEO on 1 September 2008. The terms of his appointment as CEO were approved at the 2008 AGM, the key terms of which are set out below.

If Challenger terminates Mr Stevens' Service Agreement (other than for cause). Mr Stevens will be entitled to a payment equivalent to \$1,500,000 (Termination Payment). The Termination Payment is in addition to accrued statutory entitlements.

If Mr Stevens' employment is terminated for cause, all unvested PSR, HPSRs and all unvested Share Options will lapse at the termination date.

If his employment terminates for any other reason (including resignation with Board approval):

- unvested Performance Rights will vest in full at the termination date ('Accelerated Vesting Entitlement');
- unvested Share Options will continue to be held by Mr Stevens in accordance with, and subject to, the terms relating to the original issue ('Retained Option Arrangement').

Mr Stevens may terminate his service agreement by giving 26 weeks' notice, in which event he will receive accrued statutory and contractual entitlements, but he will not be entitled to any termination payment (unless Challenger makes a payment in lieu of notice). Unless Mr Stevens' resignation is with Board approval, Mr Stevens will not be entitled to any short term incentive payment.

KMP (excluding CEO) employment agreements: notice periods

KMP do not have fixed terms of employment. Notice period by the Company and the KMP is 26 weeks (unless terminated for cause).

Upon termination, if the KMP is considered a Good Leaver (such as cessation of employment due to redundancy), the KMP will be entitled to a pro rata short-term incentive payment. Board discretion will also apply in relation to awards under the Challenger Performance Plan.

Legacy Award Plans

Legacy plans are those which were offered to employees in prior years but which are no longer in operation. Corporations law regulations require these plans to continue to be disclosed until such time as each tranche relating to such plans has been fully vested or lapsed.

Long Term Incentive Plan (LTIP)

The LTIP was approved by Shareholders at the Annual General Meeting on 22 December 2003 and a more detailed description can be found in the 2006 and 2007 Annual Reports. The last commitments were made under the LTIP in September 2006 and, subject to participants' continued employment and the performance hurdle being satisfied, the plan will cease in September 2012.

The LTIP was suspended in December 2006.

Deferred Loan Plan

A small number of employees had outstanding future commitments under the Long Term Incentive Plan (LTIP) at the time it was suspended in December 2006.

To replace those commitments, an arrangement was entered into with a third party investment bank to provide the individuals with a loan over a similar number of Challenger shares as their prior LTIP commitment. This arrangement is known as the Deferred Loan Plan.

The last commitments were made under the Deferred Loan Plan in September 2007 and subject to participants' continued employment, the plan will cease in September 2011.

Other short term employee benefits: Third Party Loan Facilities

Challenger agreed to pay interest on loans taken out by certain KMP to acquire Challenger shares on market. The loans are fully secured against the underlying shares and are not margin loans. The last commitments were made under the Third Party Loan Facilities in June 2008 and, subject to participants' continued employment, the plan ceased in December 2010.

Capped Performance Rights

The grant of capped performance rights was a transitional arrangement introduced as a retention mechanism, with a cap put into place to moderate the risk-taking behaviour that might otherwise be encouraged by incentive plans that offer 'all or nothing' outcomes. This was reflective of the approaches advocated within emerging governance and regulatory initiatives. In addition, the design of the plan minimised dilution of shareholders by not having unlimited upside for participants.

The Capped Performance Rights vest subject to the achievement of certain service and performance conditions. The conditions are employment with Challenger at the time of vesting and a share price performance condition.

Commitments were made under the Capped Performance Rights plan only once in December 2008 and the plan ceased in September 2010.

Non-Executive Directors' Disclosures

The Non-Executive Directors holding office in the year ended 30 June 2011 were:

- Peter Polson (Chairman)
- Graham Cubbin
- Jonathan Grunzweig
- Russell Hooper
- Brenda Shanahan
- Leon Zwier.

Policy

The remuneration policy for Non-Executive Directors aims to ensure that the Company can attract and retain suitably skilled and experienced people to serve on the Board and to reward them appropriately for their time and expertise. The Board's focus is on strategic direction and the delivery of sustained long-term corporate performance. The maximum aggregate of annual Non-Executive Director fees is approved by shareholders in accordance with the requirements of the *Corporations Act 2001*.

Fee pool

The current fee pool of \$2 million was approved by shareholders in 2007. No increase to the Non-Executive Director fee pool will be sought for 2011.

Fee framework

The Board periodically reviews the fee framework. Under the current fee framework, Non-Executive Directors are remunerated by way of fees paid in recognition of membership of, and work in regard of, Boards and Committees (excluding the Nomination Committee) to reflect the position's accountabilities. The fees detailed below also cover service provided on subsidiary company Boards. Fees applicable to membership and chair of the main Board and Committees that applied in the year ended 30 June 2011 were as follows:

Board/Committee	Role	Annual fee
Board ¹	Chairman ^{1,2}	\$190,000
	Member	\$130,000
Group Risk Audit and Compliance	Chairman ²	\$15,000
	Member	\$20,000
Remuneration	Chairman ²	\$15,000
	Member	\$15,000

¹ Board fees include Nomination Committee fees.

² Chairman fees are in addition to Member fees.

Details of Non-Executive Director Remuneration for 2011 financial year

The remuneration of each Non-Executive Director of the Company and of the Group for the year ended 30 June 2011 is set out in the table below:

	Year	Short Term Benefits – Director Fees \$	Post-employment superannuation \$	Total \$
P Polson	2011	377,313	–	377,313
	2010	337,003	13,256	350,259
G Cubbin ²	2011	180,000	–	180,000
	2010	155,000	–	155,000
J Grunzweig ³	2011	–	–	–
	2010	–	–	–
R Hooper ²	2011	200,000	–	200,000
	2010	189,996	–	189,996
B Shanahan ⁴	2011	36,815	3,764	40,579
	2010	–	–	–
L Zwier ²	2011	130,000	–	130,000
	2010	120,000	–	120,000
T Barrack Jr ³	2011	–	–	–
	2010	–	–	–

¹ Includes the cost of Death, TPD and Salary Continuance insurance.

² These Directors provide their services to Challenger through service companies. Fees are shown exclusive of GST.

³ Acts as a Director in discharging his duties as an executive of Colony Capital LLC and consequently does not/did not accept fees for his service.

⁴ Excludes any amounts in relation to Challenger Listed Investments Limited Director fees.

Superannuation

The Non-Executive Directors also receive superannuation contributions where required by Superannuation Guarantee legislation.

Equity participation

The Non-Executive Directors do not receive shares, share options or share rights as part of their remuneration and do not participate in any equity-based incentive plans.

Key Shareholder Questions and Answers

Why is remuneration presented in three different ways?

Over the last 10 years the complexity and quantum of information required within the Remuneration Report has increased, but in many instances this has not increased the transparency or made it easier for shareholders to get a clear view of the actual amount of remuneration that was awarded in the year in review.

In order to improve disclosure, the Board decided to introduce an 'awarded' remuneration table. This aligns with the amount a KMP receives in their remuneration statement for the year in review and better reflects the intent of the Board in regard to remuneration. This differs from the statutory accounting expense and amortisation profile (Statutory Remuneration table) or what the outcome was in any one year (Realised Remuneration table) which has a greater correlation to vesting dates and historical share prices movements. Importantly, the Corporations and Markets Advisory Committee (CAMAC) has made recommendations around the inclusion of 'awarded' remuneration tables instead of statutory tables going forward to aid in increased transparency for shareholders. All three views can be found on pages 48 to 50.

Why do you use a 90-day VWAP calculation rather than a shorter time period?

The Board made a policy decision in 2009 to use a longer term VWAP calculation for the grant and measurement of vesting of equity. The Board believes that the use of a 90-day VWAP calculation will result in less risk of erroneous price movements or price manipulation in both setting and measuring long term performance hurdles.

Why do your LTI plans only have a single hurdle (absolute TSR)?

Prior to 2010, long term incentives had a dual hurdle of either 10% compound absolute TSR or 10% compound growth in earnings per share. In 2010, the either/or hurdle was removed based on shareholder feedback and a single hurdle (absolute TSR) was adopted. The new hurdle is absolute TSR in the range of 8-12% compounding.

Why do you use an absolute TSR rather than a relative TSR hurdle?

In 2010, the Board reviewed what the most appropriate hurdle for LTI should be. The Board believes that an absolute TSR is the only effective way to both incentivise and measure whether Challenger has delivered an increase in fundamental value to its shareholders. Some of the reasons for this decision include:

- there are no other listed companies in the Australian market with a retirement income business that are directly comparable to Challenger;
- comparing Challenger's TSR to a broader index can provide outcomes that may not be indicative of the Company's performance given its differentiated position in the retirement sector; and
- key stakeholders, shareholders and proxy advisers have indicated a broader index is generally not considered an appropriate comparator group as it may result in a misalignment of executive reward from shareholder value creation.

Further detail regarding the Board's choice of hurdle can be found on page 43.

How do you determine how much short term incentive to pay?

The funding of the STI pool is determined based on a percentage of net profit before bonus and tax. The Board reviews performance at the end of each financial year and determines the amount of the pool (within a pre-determined range). Details on the range and amount of the pool in 2011 can be found on page 41.

How do you determine the appropriate level of STI for KMP?

All KMP have a balanced scorecard that sets down their key performance metrics. Metrics for the year are conveyed at the start of the financial year in July. In August the following year, the Board assesses the performance of each KMP against their scorecard and determines their STI award. The 2011 balanced scorecard and performance against metrics can be found on page 47.

What are you doing about diversity at Challenger?


Challenger believes that having a diverse employee population better enables us to deliver quality products and services to our clients and strengthens organisational capability through increased morale, motivation and engagement. In our Sustainability Report (pages 24 to 26) this year we have outlined the key objectives set to address diversity at Challenger, both at a Company and a Board level.

11. Rounding

The amounts contained in this report and the financial report have been rounded off to the nearest \$100,000 under the option available to the Group under Australian Securities & Investments Commission (ASIC) Class Order 98/100. The Group is an entity to which the class order applies.

12. Auditor's independence declaration

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




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Auditor's Independence Declaration to the Directors of Challenger Limited

In relation to our audit of the financial report of Challenger Limited for the year ended 30 June 2011, to the best of my knowledge and belief, there have been no contraventions of the auditor independence requirements of the *Corporations Act 2001* or any applicable code of professional conduct.

Ernst & Young



S J Ferguson
Partner
19 August 2011

Liability limited by a scheme approved under Professional Standards Legislation.

13. Authorisation

Signed in accordance with a resolution of the Directors of Challenger Limited.



G A Cubbin
Director
Sydney
19 August 2011



D J Stevens
Director
Sydney
19 August 2011

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Financial report

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

Income statement

For the year ended 30 June	Notes	2011 \$M	2010 \$M
Continuing operations			
Revenue	3	1,526.5	1,634.7
Expenses	4	(673.2)	(651.5)
Finance costs	5	(563.4)	(640.9)
Share of profits of associates	36	289.9 7.9	342.3 3.7
Profit from continuing operations before income tax		297.8	346.0
Income tax expense from continuing operations	6	(5.3)	(60.2)
Profit after income tax from continuing operations		292.5	285.8
Profit after income tax from discontinued operations		–	8.0
Profit for the year		292.5	293.8
Profit attributable to non-controlling interests	26	31.1	11.3
Profit attributable to equity holders		261.4	282.5
		Cents	Cents
Earnings per share from continuing operations:			
Basic earnings per share	8	54.5	53.8
Diluted earnings per share	8	50.7	50.4
Earnings per share from all operations:			
Basic earnings per share	8	54.5	55.3
Diluted earnings per share	8	50.7	51.9

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

Statement of comprehensive income

For the year ended 30 June	Notes	2011 \$M	2010 \$M
Profit for the year		292.5	293.8
Other comprehensive income/(expense) net of tax from			
– translation of foreign entities	24	(41.3)	21.8
– hedge of net investment in foreign entities	24	23.8	(16.8)
– cash flow hedges	24	1.5	8.1
– available-for-sale assets	24	(1.4)	(5.6)
Other comprehensive (expense)/income, net of tax, for the year		(17.4)	7.5
Total comprehensive income for the year		275.1	301.3
Comprehensive income attributable to non-controlling interests		31.1	11.3
Comprehensive income attributable to equity holders		244.0	290.0

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

Balance sheet

As at 30 June	Notes	2011 \$M	2010 \$M
Assets			
Cash and cash equivalents	9	788.6	674.4
Cash and cash equivalents – SPV ¹	22	386.4	458.1
Receivables	10	118.3	113.0
Receivables – SPV	22	6,889.8	8,466.8
Current tax assets		–	4.8
Derivative assets	28	360.2	287.1
Other financial assets – fair value through profit and loss	11	6,012.7	5,050.2
Other financial assets – available-for-sale	11	9.5	11.8
Investment property held for sale	12	22.0	–
Investment and development property	12	2,551.9	2,610.1
Plant and equipment	13	85.7	63.1
Investments in associates	36	40.9	33.0
Other assets	14	51.4	77.0
Goodwill	15	505.4	509.7
Other intangible assets	15	13.4	16.8
Total assets		17,836.2	18,375.9
Liabilities			
Payables	17	354.0	317.2
Derivative liabilities	28	114.8	223.2
Interest bearing financial liabilities	18	1,568.5	1,387.6
Interest bearing financial liabilities – SPV	22	6,968.7	8,637.0
External unit holders' liabilities	19	1,316.7	1,259.0
Provisions	20	30.3	42.5
Current tax liability	6	3.7	–
Deferred tax liabilities	6	51.1	43.9
Life contract liabilities	21	5,629.0	4,745.8
Total liabilities		16,036.8	16,656.2
Net assets		1,799.4	1,719.7
Equity			
Contributed equity	23	1,101.1	1,106.6
Reserves	24	179.8	211.1
Retained earnings	25	207.4	21.9
Total equity attributable to equity holders		1,488.3	1,339.6
Non-controlling interests	26	311.1	380.1
Total equity		1,799.4	1,719.7

¹ SPV = Special Purpose Vehicles.

The balance sheet should be read in conjunction with the accompanying notes.

Statement of changes in equity

For the year ended 30 June	Notes	2011 \$M	2010 \$M
Contributed equity			
Issued share capital			
Opening balance		1,235.6	1,563.0
Shares purchased and cancelled under share buy-back		(44.5)	(310.1)
Net shares cancelled under share based payment plans		–	(17.3)
Closing balance	23	1,191.1	1,235.6
Treasury shares			
Opening balance		(129.0)	(161.6)
Long Term Incentive Plan shares forfeited and cancelled		–	17.3
Shares purchased and held in trust, net of forfeitures		(57.4)	(38.6)
Vested shares released from the CPP Trust		92.3	44.9
Vested shares released from the Long Term Incentive Plan		4.1	9.0
Closing balance		(90.0)	(129.0)
Total contributed equity	23	1,101.1	1,106.6
Reserves			
Opening balance		211.1	167.9
Change in equity option premium reserve		0.1	0.1
Change in foreign currency translation reserve		(17.5)	5.0
Change in cash flow hedge reserve		1.5	8.1
Change in available-for-sale asset revaluation reserve		(1.4)	(0.7)
Change in share based payments reserve		(17.5)	22.4
Change in adjusted controlling interest reserve		3.5	8.3
Closing balance	24	179.8	211.1
Retained earnings			
Opening balance		21.9	(187.4)
Profit for the year		261.4	282.5
Dividends paid		(75.9)	(73.2)
Closing balance	25	207.4	21.9
Total equity attributable to equity holders		1,488.3	1,339.6
Non-controlling interests			
Opening balance		380.1	307.5
Other non-controlling interest movements/distributions		(22.3)	69.3
Profit for the year		31.1	11.3
Deconsolidation of controlled entities		(77.8)	(8.0)
Closing balance	26	311.1	380.1
Total equity		1,799.4	1,719.7

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

Statement of cash flows

For the year ended 30 June	Notes	2011 \$M	2010 \$M
Operating activities			
Receipts from customers		1,025.5	1,278.5
Annuities received		1,903.6	933.1
Annuities paid		(1,257.8)	(1,152.9)
Receipts from external unit holders		59.3	–
Payments to vendors and employees		(820.4)	(1,121.4)
Dividends received		35.7	36.1
Interest received		387.1	338.1
Interest paid		(115.0)	(88.7)
Income tax refund		1.9	6.3
Net cash inflow from operating activities	32	1,219.9	229.1
Investing activities			
Net (payments)/proceeds on sale/purchase of investments		(1,183.9)	78.4
Mortgage loans – advanced and purchased		(3.9)	(645.6)
Mortgage loans – repaid and sold		1,633.9	7,554.6
Net proceeds from sale of controlled entities/significant transactions		59.5	495.2
Payments for purchase of plant and equipment		(36.8)	(19.4)
Net cash inflow from investing activities		468.8	7,463.2
Financing activities			
Proceeds from issue of interest bearing liabilities		278.3	1,285.9
Repayment of interest bearing liabilities		(1,777.1)	(9,291.8)
Payments made on buy-back of shares/treasury shares		(51.7)	(322.9)
Proceeds from rights issue		–	50.9
Dividends paid		(75.4)	(72.7)
Distributions paid to non-controlling interests		(20.3)	(17.9)
Net cash outflow from financing activities		(1,646.2)	(8,368.5)
Net increase/(decrease) in cash and cash equivalents		42.5	(676.2)
Cash and cash equivalents at the start of period		1,132.5	1,808.7
Cash and cash equivalents at the end of period		1,175.0	1,132.5
Cash	9	788.6	674.4
Cash – SPV	22	386.4	458.1
Cash and cash equivalents at the end of period		1,175.0	1,132.5

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

Notes to the financial statements

1. Basis of preparation and accounting policies

Challenger Limited (*the Company or the parent entity*) is a company limited by shares, incorporated in Australia, whose shares are publicly traded on the Australian Securities Exchange (ASX). The Company changed its name from Challenger Financial Services Group Limited on 29 November 2010 following shareholder approval at the 2010 Annual General Meeting.

This financial report of Challenger Limited and its controlled entities (the Group) for the year ended 30 June 2011 was authorised for issue in accordance with a resolution of the Directors of the Company on 19 August 2011.

(i) Basis of preparation

This is a general purpose financial report that has been prepared in accordance with the requirements of the *Corporations Act 2001* and Australian Accounting Standards.

The *Corporations Amendment (Corporate Reporting Reform) Act 2010* was enacted in June 2010 and amended the *Corporations Act 2001* such that an entity required to present consolidated financial statements must disclose only the consolidated amounts in the primary statements and notes thereto. The Group therefore only discloses summarised parent entity information which is included in Note 37.

Unless stated otherwise, the financial report is presented in Australian dollars, has been prepared on the historical cost basis and amounts are rounded to the nearest one hundred thousand dollars.

The Group operates predominantly in the financial services industry. As such, the assets and liabilities disclosed in the consolidated balance sheet are grouped by nature and listed in an order that reflects their relative liquidity.

(ii) Statement of compliance

The financial report complies with Australian Accounting Standards and International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board.

(iii) New accounting standards and interpretations

Changes in accounting policy or disclosure

There were no changes in accounting policy applied during the period.

Accounting standards and interpretations issued but not yet effective

In addition to the changes specifically referred to below, there are a number of amendments to Australian Accounting Standards that are available for early adoption but that have not been applied in this financial report. The amendments would have resulted in only minor disclosure impacts if they had been early adopted.

AASB 9 Financial Instruments

AASB 9 *Financial Instruments* (AASB 9) was issued in December 2009 and is currently mandatory for annual reporting periods beginning on or after 1 January 2013. It provides revised guidance on the classification and measurement of financial instruments and permits more limited criteria for a financial instrument to be measured at amortised cost, with all other financial instruments being measured at fair value. The new standard also limits the ability to recognise fair value movements on financial assets directly in equity.

The Group is currently assessing the impact of this new standard. The classification of a financial instrument will be assessed on the facts at the date of initial application and it is possible that the classification of some financial assets may change upon adoption of the new standard.

IFRS 10, 11 and 12

IFRS 10 *Consolidated Financial Statements*, IFRS 11 *Joint Arrangements* and IFRS 12 *Disclosure of Interests in Other Entities* were issued in May 2011 and are mandatory for annual reporting periods beginning on or after 1 January 2013. IFRS 10 provides further clarity on the concept of control, IFRS 11 updates accounting for joint ventures and IFRS 12 enhances disclosure requirements for subsidiaries, joint arrangements, associates and unconsolidated structured entities. The AASB is yet to release Australian equivalent standards but the Group is in the process of assessing the impact based on the international standards.

IFRS 13

IFRS 13 *Fair Value Measurement* was issued in May 2011 and is mandatory for annual reporting periods beginning on or after 1 January 2013. It establishes a single source of guidance under IFRS for determining the fair value of assets and liabilities. The Group is currently assessing the impact of this new standard and, while it may result in some differences to the fair values determined, it is not expected to have a material impact on profit or equity upon adoption.

(iv) Basis of consolidation

The financial statements comprise the financial statements of the Company and its controlled entities. Interests in associates are equity accounted and are not part of the Group (see **Investments in associates** below).

Controlled entities are all those entities over which the Group has the power to govern the financial and operating policies so as to obtain benefits from their activities. The balance sheet date and the accounting policies of controlled entities are consistent with those of the Company.

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

The life insurance contract operations of Challenger Life Company Limited are conducted within separate statutory funds as required by the *Life Insurance Act 1995*. Both the shareholder and policyholders interests in these statutory funds are reported in aggregate in the financial report of the Group (see Note 1(xxx) **Life contract liabilities**).

Controlled entities are consolidated from the date on which control is transferred to the Company and cease to be consolidated from the date on which control is transferred out of the Company. 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 balance sheet, or a discount on acquisition, through the income statement.

Goodwill is subject to impairment testing as described in Note 1(xxiii).

Investments in associates

Associates are entities for which the Group has significant influence over the financial and operating policies, but not control. Investments in associates, other than those backing life contracts, are accounted for under the equity method whereby investments are carried at cost adjusted for post-acquisition changes in the Group's share of the net assets of the entity. Investments in associates that back life contracts are designated as financial assets at fair value through profit and loss.

The financial statements of associates are used to apply the equity method and both the financial year end and accounting policies of associated entities are consistent with those of the Group. After application of the equity method, the Group determines whether it is necessary to recognise any additional impairment loss in the carrying value of the net investment in associates.

The investments in associates are carried in the balance sheet at cost plus post-acquisition changes in the Group's share of net assets of the associate, less any impairment in value. The consolidated income statement reflects the share of the results of operations of the associate. Where there has been a change recognised directly in the associate's equity, the Group recognises its share of any changes and discloses this in the consolidated statement of changes in equity.

Special purpose vehicles

The Group manages and services trusts that hold residential mortgage assets and securitised financial liabilities. As the Group retains the right to the residual income of these trusts, it is deemed to control them and, as a result, they are consolidated.

(v) Comparatives

Where necessary, comparative figures have been reclassified to conform to the changes in presentation made in these financial statements.

(vi) Rounding of amounts

Amounts in this financial report are rounded to the nearest hundred thousand dollars (\$0.0M), unless otherwise stated, under the option available to the Company under ASIC Class Order 98/100.

(vii) Segment reporting

Operating segments are identified on the basis of internal reports to senior management and comprise component parts of the Group that are regularly reviewed by senior management in order to allocate resources and assess performance.

(viii) Revenue

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

- Management fee revenue is derived from the provision of investment management services to the Group's managed investment products and residential mortgage assets. Revenue is recognised when the services are deemed to have been earned using an effective interest rate method over the life of the contract.
- Interest revenue is recognised as it accrues using an effective interest rate, taking into account the effective yield of the financial asset.

1. Basis of preparation and accounting policies (continued)

(viii) Revenue (continued)

- Dividends on listed equity shares are recognised as income on the date the share is quoted ex-dividend. Dividends from unlisted companies are recognised when the dividend is declared.
- 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 income statement when the change in value is recognised on the balance sheet.
- Rental revenue from investment properties is accounted for on a straight-line basis over the lease term. Contingent rental income is recognised as income in the periods 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.
- The portion of the change in life contract liabilities recognised in the income statement that relates to changes in discount rates, inflation rates and other assumption changes is classified as revenue. The remaining change is classified as an expense. See Note 1(xxx) for more detail on the recognition and measurement of life contract liabilities.

(ix) Expenses

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

- See Note 1(xxi) for details of how the costs incurred in the establishment of special purpose vehicles and the origination of interest bearing liabilities are recognised in the income statement.
- Expenses incurred under an investment property operating lease are recognised on a straight-line basis over the term of the lease.
- Investment property expenditure, including rates, taxes, insurance and other costs associated with the upkeep of a building, are brought to account on an accrual basis. Repair costs are expensed when incurred. Other amounts that improve the condition of the investment are capitalised into the carrying value of the asset.
- Changes in life contract liabilities recognised as an expense consist of the interest expense on the liability, any loss on the initial recognition of new business less the release of expenses over the period. The interest on the liability represents the unwind of the discount on the opening liability over the period, whereas the impacts of the changes in discount rate applied for the current valuation are included in the change in the life contract liabilities disclosed in Revenue. See Note 1(xxx) for more detail on the recognition and measurement of life contract liabilities.

(x) Finance costs

Finance costs represent interest on interest bearing financial liabilities (primarily the securitised residential mortgage backed securities issued by the special purpose vehicles, 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 that asset. Revenue earned on the investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalisation.

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

(xi) Goods and Services Tax (GST)

Revenues, expenses and assets are recognised net of the 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 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 balance sheet.

Cash flows are included in the statement of cash flows on a gross 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.

(xii) Income tax

Income tax on the income statement for the year comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

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

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

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

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

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

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

The carrying amount of deferred income tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilised.

Unrecognised deferred income tax assets are reassessed at each balance sheet date and are recognised to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered. Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the balance sheet date.

Income taxes relating to items recognised directly in equity are recognised in equity and not in profit or loss in the income statement.

Deferred income tax assets and liabilities are offset only if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred tax assets and liabilities relate to the same taxable entity and the same taxation authority.

Tax consolidation

Challenger Limited and its 100% owned Australian 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 tax equivalent payments 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.

(xiii) 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

Transactions in foreign currency are translated into presentation currency, Australian dollars, 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 balance sheet 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 1(xvi).

1. Basis of preparation and accounting policies (continued)

(xiii) Foreign currency (continued)

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 balance sheet 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.

(xiv) Cash and cash equivalents

Cash and cash equivalents are financial assets and comprise cash at bank and in hand 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 the fair value. For the purposes of the cash flow statement, cash and cash equivalents are stated net of bank overdrafts.

(xv) Receivables

Receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They include mortgage assets, trade and other receivables and are recognised at their amortised cost less impairment losses.

Receivables are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated.

(xvi) Derivative financial instruments and hedging

The Group uses derivative financial instruments to hedge its risks associated with interest rate and foreign currency fluctuations but does not hold derivative financial instruments for trading purposes. 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 income statement.

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

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

At the inception of a hedge relationship to which the Group wishes to apply hedge accounting, the Group formally designates and documents the hedge relationship and the risk management objectives and strategies for undertaking the hedge. The documentation includes: identification of the hedging instrument; the hedged item or transaction; the nature of the risk being hedged; and how the entity will assess the effectiveness of the instrument in offsetting the exposure to changes in the hedged item.

Such hedges are expected to be highly effective in achieving offsetting changes in fair values, cash flows or foreign exchange difference and are assessed on an ongoing basis to determine that they actually have been highly effective over the period that they were designated.

Fair value hedges

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

For fair value hedges, the carrying amount of the hedged item is adjusted for gains and losses attributable to the risk being hedged and the derivative is remeasured to fair value. Gains and losses from both are recognised in the income statement.

When an unrecognised firm commitment is designated as a hedged item, the subsequent cumulative change in the fair value of the firm commitment attributable to the hedged risk is recognised as an asset or liability with a corresponding gain or loss recognised in the income statement. The changes in the fair value of the hedging instrument are also recognised in the income statement.

The Group discontinues fair value hedge accounting if the hedging instrument expires or is sold, terminated or exercised, the hedge no longer meets the criteria for hedge accounting or the Group revokes the designation. Any adjustment to the carrying amount of a hedged financial instrument for which the effective interest method is used is amortised to the income statement.

Amortisation may begin as soon as an adjustment exists and shall begin no later than when the hedged item ceases to be adjusted for changes in its fair value attributable to the risk being hedged.

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 income statement. 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 income statement.

Amounts taken to equity are transferred to the income statement 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 income statement. 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 income statement. The cumulative gain or loss previously recognised in equity is recognised in other comprehensive income on disposal or partial disposal of the foreign operation.

(xvii) Other financial assets

The Group classifies its other financial assets into the following categories: *financial assets at fair value through profit or loss* (being either held for the purposes of trading or initially designated as such); or *available-for-sale*. The classification depends on the definition and the purpose for which the investments were acquired. The classification of investments is determined at initial recognition and evaluated at each reporting date.

Purchases and sales of other financial assets are recognised on the date on which the Group commits to purchase or sell the asset. Other financial assets are initially recognised at fair value (plus transaction costs for available-for-sale assets). Other financial assets are derecognised when the right to receive cash flows from the asset has expired or when the risks and rewards of ownership have been substantially transferred.

The fair value of other 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 balance sheet date.

For assets for which no active market exists, fair values are determined using valuation techniques. Such techniques include: using recent arm's length market transactions; reference to the current market value of another instrument that is substantially the same; discounted cash flow analysis and option pricing models refined to reflect the issuer's specific circumstances, making as much use of available and supportable market data as possible and keeping judgemental inputs to a minimum.

Financial assets at fair value through profit and loss

Financial assets classified in this category are assets either held for the purposes of trading or designated as fair value through profit and loss on initial recognition. Held for trading assets consist of debt or equity securities. They are carried at fair value with unrealised gains and losses being recognised through the income statement. Assets designated as fair value through profit and loss consist of infrastructure and property securities. Assets backing life contract liabilities are required to be designated as fair value through profit and loss in accordance with AASB 1038 *Life Insurance Contracts*.

Available-for-sale financial assets

Available-for-sale financial assets are those non-derivative financial assets that are either designated into this category or are not classified as either receivables or financial assets through profit and loss.

After initial recognition, available-for-sale investments are measured at fair value with gains or losses being recognised as a separate component of equity. When the asset is derecognised, or is determined to be impaired, the cumulative gain or loss previously reported in equity is recognised in the income statement.

(xviii) Investment property

Investment property is initially recognised at cost, including transaction costs. Subsequent to initial recognition, investment property is recognised at fair value. Independent valuations for all investment properties are conducted at least annually, from suitably qualified valuers, and the Directors make reference to these independent valuations when determining fair value. When a sale price for a property has been agreed prior to the period end for a sale subsequent to the period end, the agreed sale price is taken as the fair value and the property is classified as investment property held for sale.

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

1. Basis of preparation and accounting policies (continued)

(xviii) Investment property (continued)

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

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.

Development property held for resale

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

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

(xix) Plant and equipment

Items of plant and equipment are stated at cost, or deemed cost, less accumulated depreciation and impairment losses. Depreciation is calculated on a straight-line basis to write off the net cost of each class of fixed assets over its expected useful life. Estimates of remaining useful lives are made on a regular basis for all assets, with annual reassessments for major items. The expected useful life of plant and equipment is three to five years.

Infrastructure fixed assets

Infrastructure fixed assets are stated at cost and amortised on a straight-line basis over their estimated useful life of 40 years. This is done on an asset by asset basis with amortisation commencing when the Group starts receiving income from the asset.

The carrying values of plant and equipment and infrastructure fixed assets are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. Impairment losses are recognised in the income statement.

(xx) Operating leases

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

Incentives received on entering into operating leases are recognised as liabilities and are amortised over the life of the lease.

Where the Group acquires, as part of a business combination, an operating lease over land, the fair value of the operating lease over land is recognised separately from goodwill. See Note 1(xxii) below. Other operating lease payments are charged to the income statement in the periods in which they are incurred.

Surplus lease space

The present value of future payments for surplus lease space under non-cancellable operating leases, net of sub-leasing revenue, is recognised as a provision in the period in which it is determined that the lease space will be of no future benefit to the Group. See Note 1(xxviii) below.

(xxi) Prepayments

Deferred portfolio costs

Portfolio costs represent the expenses incurred in establishing mortgage trusts. They are recognised as an asset when incurred and subsequently amortised in the income statement as the future economic benefits from the mortgage assets are expected to be received.

Deferred origination costs

Origination costs are expenses incurred as a direct result of the origination of mortgage loans to customers. These costs are recognised as an asset and subsequently amortised through the income statement in line with the pattern of expected future economic benefits arising from the related mortgage asset.

(xxii) Goodwill and other intangible assets

Goodwill

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

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

Each unit, or group of units, to which the goodwill is so allocated 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 (or group of cash-generating units), to which the goodwill relates. When the recoverable amount of the cash-generating unit (or group of cash-generating units) is less than the carrying amount, an impairment loss is recognised.

When goodwill forms part of a cash-generating unit (or group of cash-generating units) 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. Impairment losses recognised for goodwill are not subsequently reversed.

Other intangible assets

Other intangible assets acquired are recorded at cost less accumulated amortisation and impairment losses. The cost of an intangible asset acquired in a business combination is its fair value as at the date of acquisition.

As stated in Note 1(xx) above, where the Group acquires, as part of a business combination, an operating lease over land, the fair value of this lease is recognised separately from goodwill. This intangible asset is recorded at fair value less accumulated amortisation. Amortisation is calculated using the straight-line method over the effective life of the lease, being 25 years.

Certain internal and external software costs directly incurred in acquiring and developing software have been capitalised and are being amortised on a straight-line basis over their useful life, usually a period of five years. Useful lives are examined on an annual basis and where applicable, adjustments are made on a prospective basis. Costs incurred on software maintenance are expensed as incurred.

(xxiii) 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 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 time value of money and the risks specific to the asset.

When the carrying amount of an asset or cash-generating unit 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 income statement, 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 income statement.

Impairment losses recognised in respect of cash-generating units 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 income statement unless the asset is carried at revalued amount, in which case it is treated as a revaluation increase.

(xxiv) 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 costs.

1. Basis of preparation and accounting policies (continued)

(xxv) Interest bearing financial liabilities

Capital market issuances of interest bearing liabilities, including property debt issued by controlled property trusts and the subordinated debt issued by the Company, are recognised at fair value with unrealised gains and losses recognised through the income statement.

Other interest bearing financial liabilities are initially recognised at the fair value of the consideration received less directly attributable transaction costs. After initial recognition, other interest bearing financial liabilities are subsequently measured at amortised cost using the effective interest method.

(xxvi) Employee benefits

Superannuation funds

Obligations for contributions to superannuation funds are recognised as an expense in the income statement as incurred. The Group does not hold or pay into any defined benefit superannuation schemes on behalf of employees.

Wages, salaries, annual leave and non-monetary benefits

Liabilities for wages and salaries, including non-monetary benefits and annual leave expected to be settled within 12 months of the reporting date, are recognised in respect of employees' services up to the reporting date. They are measured at the amounts expected to be paid when the liabilities are settled. Liabilities for accumulated sick leave are recognised when the leave is taken and are measured at the rates paid or payable.

Long service leave

A liability for long service leave is recognised as the present value of estimated future cash outflows to be made in respect of services provided by employees up to the reporting date. The estimated future cash outflows are discounted using bond yields from Australian Commonwealth government bonds which have durations to match, as closely as possible, the estimated future cash outflows.

Factors which affect the estimated future cash outflows such as expected future salary increases, experience of employee departures and period of service, are included in the measurement.

(xxvii) External unit holders' liabilities

The Group controls a number of guaranteed index return trusts which contain funds pertaining to 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 controls these trusts and consolidates the financial performance and balance sheet of the trusts. The external unit holders' liabilities represent the balance owing to third parties on these mandates and are measured on a fair value basis.

(xxviii) Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

A provision for restructuring is recognised when the Group has approved a detailed and formal restructuring plan, and the restructuring has either commenced or has been announced publicly. Future operating costs are not provided for.

When the Group expects some or all of a provision to be reimbursed, for example, under an insurance contract, the reimbursement is recognised as a separate asset only when the reimbursement is virtually certain. The expense relating to any provision is presented in the income statement net of any reimbursement.

Provisions are measured at the present value of management's best estimate of the expenditure required to settle the present obligation at the balance sheet date. If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects the time value of money and the risks specific to the liability. The increase in the provision resulting from the passage of time is recognised in finance costs.

(xxix) Restrictions on assets

Financial assets held in Challenger Life Company Limited can only be used within the restrictions imposed under the *Life Insurance Act 1995*. 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 solvency and capital adequacy requirements are met.

(xxx) Life contract liabilities

The operations of the Group include the selling and administration of contracts through Challenger Life Company Limited. 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 term policies, the liability is based on the fair value of the income payments and associated expenses, being the net present value 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 premium 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. Any planned release of this margin is recognised in the income statement as part of the movement in life contract liabilities.

Life insurance contract liabilities are usually determined using a projection method, whereby estimates of policy cash flows (annuity payments, expenses etc) 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.

Reinsurance

The Margin on Services (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. The balance sheet therefore shows life insurance contract liabilities net of reinsurance and the change recognised in the income statement is also shown net of reinsurance.

(xxxi) Contributed equity

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.

Treasury shares are ordinary shares in the Company held by the employee share trust and those issued in respect of long term incentive plan awards to employees. Refer to Note 1(xxiii) for further details.

(xxxii) Earnings per share

Basic earnings per share is calculated by dividing the (total and continuing) profit for the year attributable to equity holders of the Company by the weighted average number of ordinary shares outstanding during the financial period. The number of ordinary shares outstanding includes any shares granted under the employee share incentive plan which have vested and settled.

Diluted earnings per share is calculated by dividing the (total and continuing) profit attributable to equity holders of the Company by the weighted average number of ordinary shares outstanding during the year (adjusted for the effects of dilutive options and shares granted under the Challenger Performance Plan).

(xxxiii) Share based payment transactions

Long term equity based incentive plan

The Group has an employee share incentive plan and an employee share trust for the granting of non-transferable options to executives and senior employees. Shares in the Company held by the employee share trust are classified as treasury shares and presented in the balance sheet as a deduction from equity.

Employees of the Group receive remuneration in the form of share based payment transactions, whereby employees render services in exchange for shares or rights over shares (equity-settled transactions).

The cost of equity-settled transactions with employees is measured by reference to the fair value at the date at which they are granted. The fair value is determined using an option pricing model. In valuing equity-settled transactions, no account is taken of any performance conditions, other than conditions linked to the price of the shares of the Company (market conditions).

In accordance with Australian Accounting Standards, the cost of equity-settled transactions is recognised in the income statement, together with a corresponding increase in equity, over the period in which the performance conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award (vesting date). At the Company level, the cost of the equity shares is recognised as an equity distribution, whereby the investment in subsidiary is increased with a corresponding increase in the share based equity reserve.

The cumulative expense or investment recognised for equity-settled transactions at each reporting date until the vesting date reflects the extent to which the vesting period has expired and the number of awards that, in the opinion of the directors of the Group at that date, based on the best available estimate of the number of equity instruments that will ultimately vest.

1. Basis of preparation and accounting policies (continued)

(xxxiii) Share based payment transactions (continued)

Long term equity based incentive plan (continued)

No adjustment is made for the likelihood of market performance conditions being met as the effect of these conditions is included in the determination of fair value at grant date.

Where the terms of an equity-settled award are modified, as a minimum an expense is recognised as if the terms had not been modified. In addition, an expense is recognised for any increase in the value of the transaction as a result of the modification, as measured at the date of modification.

Where an equity-settled award is cancelled during the vesting period (other than a grant cancelled forfeiture when the vesting conditions are not satisfied), it is treated as if it had vested on the date of cancellation, and any expense not yet recognised for the award is recognised immediately.

However, if a new award is substituted for the cancelled award, and designated as a replacement award on the date that it is granted, the cancelled and new awards are treated as if they were a modification of the original award, as described in the previous paragraph.

(xxxiv) Employee Share Acquisition Plan

Share based compensation benefits are provided to employees via the Challenger Performance Plan (CPP). The Group has formed a trust to administer the Group's employee share acquisition plan. This trust is consolidated, as the substance of the relationship is that the trust is controlled by the Group.

Through contributions to the trust, the Group purchases shares in the Company on market. Shares acquired are held by the Challenger Performance Plan Trust, are disclosed as Treasury Shares and deducted from contributed equity. The cost of the shares acquired by the CPP is recognised as an employee benefit expense with a corresponding increase in equity, being a share based payments reserve.

The fair value is measured at grant date and recognised over the period during which the employees become unconditionally entitled to the shares.

(xxxv) Significant accounting judgements, estimates and assumptions

The carrying values of amounts recognised on the balance sheet 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:

Share based payments

The Group measures the cost of equity-settled transactions with employees by reference to the fair value of the ordinary shares at the date at which they are granted. The fair value is determined using the Black-Scholes formula, taking into account the terms and conditions upon which the equity instruments were granted, as discussed in Note 31. The fair value calculation is performed by an external valuer.

Life insurance contract liabilities

Life insurance contract liabilities are recognised under the MoS methodology described in Note 1(xxx). Significant judgement is applied in the MoS liability valuation as it involves the application of actuarial assumptions.

The key areas of judgement in the determination of the actuarial assumptions are: the duration of claims/policy payments; acquisition and maintenance expense levels; and economic assumptions for discount and inflation rates. Additional information on the life insurance contract liabilities is set out in Note 21 *Life Contract Liabilities*.

Property valuations

Investment properties are stated at fair value based on valuations performed by independent valuers.

The independent valuer is authorised to practise under the law of the relevant jurisdiction where the valuation takes place and has at least five years of continuous experience in the valuation of property of a similar type to the property being valued. The valuer has no pecuniary interest that could conflict with the valuation of the property and complies with the Australian Property Institute (API) Code of Ethics and Rules of Conduct.

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 capitalisation and discounted cash flow approach.

Interest bearing financial liabilities

Subordinated debt is recognised at fair value. The determination of fair value includes the assessment of movements in interest rates, credit spreads and foreign exchange. These movements are reviewed at each reporting date to take into account market conditions.

Deferred tax assets

Deferred tax assets are recognised when it is considered probable that future taxable profits will be available to utilise those temporary differences. Factors considered include the ability to offset tax losses against taxable profits between members of the tax consolidated group within an appropriate future timeframe, and whether the levels of future taxable profits are expected to be sufficient to allow recovery of deferred tax assets.

Unlisted investment valuations

Investments for which there is no active market or an external valuation available are valued either by reference to the current market value of another instrument that is substantially the same; a discounted cash flow analysis or other methods consistent with market best practice. Refer Note 27 for further disclosure.

Impairment of goodwill

The Group assesses whether goodwill is impaired at least annually in accordance with the accounting policy in Note 1(xxiii). These calculations involve an estimation of the recoverable amount of the cash-generating units to which the goodwill is allocated.

2. Segment information

Business segments

The reporting segments of the Group have been identified as follows:

	Life		Funds Management	
For the year ended 30 June	2011 \$M	2010 \$M	2011 \$M	2010 \$M
Net income ¹	400.8	338.0	88.4	102.0
Operating expenses ¹	(52.0)	(33.9)	(68.3)	(84.7)
Normalised EBIT¹	348.8	304.1	20.1	17.3
Interest and borrowing costs ¹	–	–	–	–
Discontinued operations ²	–	–	–	–
Normalised net profit/(loss) before tax	348.8	304.1	20.1	17.3
Tax on normalised profit	(65.9)	(53.1)	(5.8)	(5.2)
Normalised net profit/(loss) after tax	282.9	251.0	14.3	12.1
Investment experience after tax ¹	(28.7)	51.3	–	–
Significant items after tax	–	–	–	–
Profit/(loss) attributable to equity holders	254.2	302.3	14.3	12.1
As at 30 June				
Segment assets	9,177.7	8,275.1	151.8	161.0
Segment liabilities	(7,627.8)	(6,822.6)	(15.9)	(28.2)
Net assets	1,549.9	1,452.5	135.9	132.8

¹ See following pages for definitions of the terms used in the management view of segments.

² The Mortgage Management division was disposed of on 30 October 2009 but remained as a reported segment during the period to 31 December 2009.

³ 'Corporate and other' includes corporate companies, corporate SPV, non-controlling interests and group eliminations.

	Discontinued operations ²		Total reporting segments		Corporate and other ³		Total	
	2011 \$M	2010 \$M	2011 \$M	2010 \$M	2011 \$M	2010 \$M	2011 \$M	2010 \$M
	–	–	489.2	440.0	4.8	7.6	494.0	447.6
	–	–	(120.3)	(118.6)	(59.9)	(63.2)	(180.2)	(181.8)
	–	–	368.9	321.4	(55.1)	(55.6)	313.8	265.8
	–	–	–	–	(2.7)	(14.1)	(2.7)	(14.1)
	–	39.1	–	39.1	–	–	–	39.1
	–	39.1	368.9	360.5	(57.8)	(69.7)	311.1	290.8
	–	–	(71.7)	(58.3)	8.6	–	(63.1)	(58.3)
	–	39.1	297.2	302.2	(49.2)	(69.7)	248.0	232.5
	–	–	(28.7)	51.3	–	–	(28.7)	51.3
	–	–	–	–	42.1	(1.3)	42.1	(1.3)
	–	39.1	268.5	353.5	(7.1)	(71.0)	261.4	282.5
	–	–	9,329.5	8,436.1	8,506.7	9,939.8	17,836.2	18,375.9
	–	–	(7,643.7)	(6,850.8)	(8,393.1)	(9,805.4)	(16,036.8)	(16,656.2)
	–	–	1,685.8	1,585.3	113.6	134.4	1,799.4	1,719.7

2. Segment information (continued)

Business segments (continued)

Definitions

Net income and **operating expenses** differ from revenue and expenses as disclosed in the income statement as certain direct costs (including commissions and management fees) included in expenses are netted off against gross revenues in deriving the management view of segment revenue above. 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 the management view of segment revenue.

Revenue also includes investment gains/losses which are excluded from the management view as they form part of investment experience (see below).

Normalised EBIT

Normalised earnings before interest and tax (EBIT) is the net of the management view of revenue and operating expenses, as defined above. It excludes investment experience, interest and borrowing costs, tax and significant items.

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

Investment experience after tax

The Group is required by accounting standards to value all assets and liabilities supporting the life insurance business at fair value. This can give rise to fluctuating valuation movements being recognised in the income statement, particularly during periods of market volatility. As the Group is generally a long-term holder of assets, due to them being held to match to 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) in any period and the normalised investment gains/losses (derived using calculations that estimate the expected capital growth of the portfolio, using stable, long-term growth assumptions). Investment experience after tax is investment experience net of tax at the prevailing income tax rate.

Operating segments

The format of the segment information is the same as that provided to the chief operating decision maker of the Group. The Group operates in the following segments:

Life – includes annuity and life insurance business carried out by Challenger Life Company Limited (CLC). CLC invests in assets providing long-term income streams for customers.

Funds Management – earns fees from its operations in the funds management and specialised funds fields, providing an end to end funds management business as well as managing two listed funds and a number of unlisted fund mandates.

Discontinued operations – represents the Mortgage Management segment which was a white label funding provider for the commercial and residential mortgage lending market. The segment also distributed mortgages through ownership of broker aggregation platforms. This segment ceased to operate after the sale of the mortgage distribution business and \$4.5 billion of mortgages on 30 October 2009.

Corporate and other

Corporate expenses consist of costs that fall outside the day-to-day operations of the reportable segments. These include the costs of the Group CEO and CFO, shared services across the Group, long-term incentive costs, Directors' fees, corporate borrowings and associated borrowing costs and shareholder registry services.

To reconcile to Group results, Corporate and other also includes eliminations and non-core activities of the Group.

Major customers

The Group does not rely on any major customer and so there is no concentration risk.

Products and services

The Group's divisional segment split represents the products that the Group supplies.

Life – offers fixed rate superannuation products and fixed rate retirement products that are both designed for investors who are seeking a low-risk investment for a known period of time and want to protect their capital.

Funds Management – offers a range of managed investments across the major asset classes with funds in:

- Fixed interest and mortgages;
- Australian shares;
- Property funds; and
- International shares.

Funds Management also has equity investments in a number of boutique fund managers.

Geographical areas

The Group operates predominantly in Australia and so no geographical split is provided to the chief operating decision maker.

	30 June 2011 \$M	30 June 2010 \$M
Reconciliation of management view of revenue to statutory revenue		
Reporting segments	489.2	440.0
Corporate and other	4.8	7.6
Net income – management view of revenue	494.0	447.6
Expenses and finance costs offset against management revenue		
SPV expenses and finance costs offset against SPV income	426.7	525.2
Commission expenses offset against commission income	56.9	70.0
Amortisation of deferred portfolio and origination costs offset against mortgage income	14.8	36.5
Change in life contract liabilities recognised in expenses offset against revenue	275.0	240.3
Property expenses offset against property income	63.2	55.9
Interest and loan amortisation costs	143.6	107.4
Infrastructure expenses	–	7.6
Management fees	53.6	31.9
Adjustment for non-controlling interests and other items	39.7	56.8
Difference between management view of investment experience and statutory recognition		
Total actual capital growth	1.1	234.1
Normalised capital growth	(45.5)	(54.6)
Actuarial assumption changes	3.4	(124.0)
Statutory view – revenue	1,526.5	1,634.7
Reconciliation of management to statutory view of pre-tax profit		
Reportable segment normalised net profit before tax	368.9	360.5
Corporate and other normalised loss before tax	(57.8)	(69.7)
Normalised net profit before tax – management view of pre-tax profit	311.1	290.8
Investment experience before tax	(41.0)	55.5
Difference between management and statutory view of discontinued operations	–	(11.4)
Profit attributable to non-controlling interests excluded from management view	31.1	11.3
Other	(3.4)	(0.2)
Statutory view – profit before tax	297.8	346.0

3. Revenue

	30 June 2011 \$M	30 June 2010 \$M
Fee revenue		
Management fee revenue	91.8	89.5
Fee revenue – SPV	10.4	25.9
Other fee revenue	4.4	11.0
Investment revenue		
Equity and infrastructure investments		
Dividend revenue	31.8	32.6
Net realised loss on equity investments	(1.2)	(6.3)
Net unrealised gain on equity investments	25.1	20.2
Net realised (loss)/gain on infrastructure investments	(0.2)	5.9
Net unrealised loss on infrastructure investments	(61.9)	(6.4)
Debt securities and cash		
Interest revenue	411.0	323.9
Net realised gain on debt securities	32.5	105.4
Net unrealised gain on debt securities	17.7	126.0
Investment property and property securities		
Dividend revenue	2.0	2.3
Property rental revenue	231.9	207.5
Net realised loss on investment property and property securities	(0.1)	(7.6)
Net unrealised gain/(loss) on investment property and property securities	5.4	(56.7)
Discount on acquisition of controlled entity ¹	–	112.4
Other		
Interest revenue – SPV	622.1	745.7
Impairment loss on available-for-sale financial assets	–	(4.9)
Net realised gain on foreign exchange translation and hedges	157.2	189.2
Net unrealised loss on foreign exchange translation and hedges	(67.0)	(113.9)
Net realised loss on interest rate derivatives	(4.5)	(8.4)
Net unrealised loss on interest rate derivatives	(19.5)	(7.1)
Other revenue		
Change in life contract liabilities ²	51.8	(138.8)
Change in reinsurance contract liabilities	(14.2)	(12.7)
	1,526.5	1,634.7

¹ On 31 January 2010, the Group acquired a controlling interest in Challenger Kenedix Japan Trust (CKT). The purchase of property assets is considered core to the operations of the Group.

² Changes in life contract liabilities arising from discount rates, inflation rates and other assumptions are recognised as revenue, with other movements being included in Note 4 *Expenses*.

4. Expenses

	30 June 2011 \$M	30 June 2010 \$M
Commission expenses	56.9	70.0
Amortisation of deferred portfolio and origination costs	14.8	36.5
Cost of life contract liabilities ¹	275.0	240.3
Property related expenses	63.2	55.9
Management fees	53.6	31.9
Fee expenses – SPV	9.6	4.3
Intangibles amortisation expense	1.3	2.4
Employee expenses	103.0	116.4
Employee share based payments	25.7	31.5
Superannuation	4.3	5.0
Occupancy expense – operating lease	4.5	4.5
Depreciation expense	6.4	6.9
Communications	12.8	7.6
IT maintenance	4.9	3.8
Professional fees	11.0	11.9
Other expenses	26.2	22.6
Total	673.2	651.5

¹ Cost of life contract liabilities recognised as an expense consists of the interest expense on the liability, any loss on the initial recognition of new business less the release of expenses incurred over the 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 3 *Revenue*.

5. Finance costs

	30 June 2011 \$M	30 June 2010 \$M
Interest and loan amortisation expenses incurred by:		
– SPV	417.1	520.9
– Property trusts	24.9	31.2
– Other entities	118.7	76.2
Other finance costs	2.7	12.6
	563.4	640.9

6. Income tax

	30 June 2011 \$M	30 June 2010 \$M
Analysis of income tax expense		
Current income tax benefit/(expense) for the period	21.3	(89.1)
Current income tax expense prior period adjustment	(2.3)	(8.5)
Deferred income tax (expense)/benefit	(24.3)	37.4
Income tax expense from continuing operations	(5.3)	(60.2)
Income tax (expense)/benefit on hedge of net investment in foreign entity	(10.2)	7.2
Income tax benefit on available-for-sale asset revaluations taken to equity	0.6	2.4
Income tax(expense)/benefit from other comprehensive income	(9.6)	9.6
Reconciliation of income tax expense from continuing operations:		
Profit from continuing operations before income tax	297.8	346.0
Prima facie income tax based on the Australian company tax rate of 30%	(89.3)	(103.8)
Tax effect of amounts not deductible/assessable in calculating taxable income:		
Non-assessable and non-deductible items	31.8	38.7
Rate differential on offshore income	0.7	(0.8)
Tax provision release ¹	42.1	–
Other items	9.4	5.7
Income tax expense from continuing operations	(5.3)	(60.2)

¹ In May 2011, confirmation was received from the ATO that there were no further matters arising from the Group's tax treatment of specific items identified in a tax audit of prior years. As a result, a legacy tax provision was released.

Current tax liability – The Group has recognised a current tax liability of \$3.7 million at 30 June 2011. This relates to controlled entities that are not part of the Challenger tax consolidated group and therefore cannot utilise Group losses.

	Balance sheet		Income statement	
	30 June 2011 \$M	30 June 2010 \$M	30 June 2011 \$M	30 June 2010 \$M
Analysis of deferred tax				
Deferred tax assets				
Accruals and provisions	32.5	34.3	4.5	24.8
Employee entitlements	2.1	2.4	(0.3)	0.8
Losses	80.2	124.2	(73.7)	(29.1)
Other	13.5	9.9	3.4	22.9
	128.3	170.8		
Deferred tax liabilities				
Deferred acquisition and origination costs	(3.7)	(7.9)	4.2	(17.5)
Fixed asset temporary differences	(0.7)	(1.6)	0.9	(14.4)
Unrealised foreign exchange movements	(0.7)	6.4	(7.1)	(14.1)
Unrealised gains on investment property	(146.9)	(156.0)	15.6	68.0
Other	(27.4)	(55.6)	28.2	(4.0)
	(179.4)	(214.7)		
Net deferred tax liability	(51.1)	(43.9)		
Deferred income tax (expense)/benefit			(24.3)	37.4

Unused capital losses – The Group has \$131.3 million (2010: \$134.4 million) of gross unused capital losses for which no deferred tax asset has been recognised. All available revenue losses have been recognised, see deferred tax table above for details.

Contingent tax asset

As a result of a retrospective amendment to the tax legislation in 2010, the Group has lodged a series of claims in relation to the Tax Consolidation treatment of rights to future income arising from the Group's entry into the tax consolidation regime in 2003. The amended legislation allows for deductions to be spread over 10 years from 2003. On 30 March 2011, the Assistant Treasurer announced a Board of Taxation review of the legislation surrounding these deductions. The Group's claims will not be processed until the findings of this review are communicated. If successful, the Group's tax claim, including prior year and future deductions, would be approximately \$45 million. No tax benefit or asset has been recognised in respect of this amount.

7. Dividends paid and proposed

	30 June 2011 \$M	30 June 2010 \$M
Dividends declared and paid during the year		
Final 30 June 2010 unfranked dividend: 8.5 cents (2009: 7.5 cents unfranked)	41.8	42.0
Interim 30 June 2011 unfranked dividend: 7.0 cents (2010: 6.0 cents unfranked)	34.1	31.2
	75.9	73.2
Dividend proposed (not recognised as a liability at 30 June)		
Final 30 June 2011 unfranked dividend: 9.5 cents (2010: 8.5 cents unfranked)	45.1	41.8

8. Earnings per share

	30 June 2011 Cents	30 June 2010 Cents
The following reflects the income and share data used in the basic and diluted earnings per share computations:		
Continuing operations:		
Basic earnings per share	54.5	53.8
Diluted earnings per share	50.7	50.4
All operations:		
Basic earnings per share	54.5	55.3
Diluted earnings per share	50.7	51.9
Profit used in the calculation of earnings per share	\$M	\$M
For basic earnings per share:		
Profit attributable to equity holders from continuing operations	261.4	274.5
Profit after income tax from discontinued operations	—	8.0
Profit attributable to equity holders	261.4	282.5
Adjustments for diluted earnings per share:		
Interest received on Long Term Incentive Plan loans	—	(0.1)
Adjusted profit attributable to equity holders from continuing operations	261.4	274.4
Adjusted profit attributable to equity holders	261.4	282.4

	Number	Number
Number of shares		
Weighted average ordinary shares for basic earnings per share	479,394,450	510,402,038
Effect of dilution	36,485,082	33,901,624
Weighted average ordinary shares for diluted earnings per share	515,879,532	544,303,662

In determining the weighted average number of ordinary shares used in the calculation of earnings per share, a reduction is made for the average number of treasury shares held. The weighted average number of treasury shares for the period was 25,152,356 (2010: 41,838,441).

There have been no material transactions involving ordinary shares or potential ordinary shares since the reporting date and before the completion of the financial report.

9. Cash and cash equivalents

	30 June 2011 \$M	30 June 2010 \$M
Cash at bank and on hand	312.9	317.0
Deposits at call	10.4	20.3
Other cash equivalents	465.3	337.1
	788.6	674.4

10. Receivables

	30 June 2011 \$M	30 June 2010 \$M
Interest receivable	62.3	48.2
Trade debtors	23.9	33.4
Amounts recoverable from managed trusts	6.1	8.1
Dividends and distributions receivable	9.8	10.1
Other debtors	16.2	13.2
Total receivables¹	118.3	113.0

¹ All receivables are current.**11. Other financial assets**

	30 June 2011 \$M	30 June 2010 \$M
Financial assets at fair value through profit and loss¹		
Debt securities		
Bonds	1,856.4	1,376.6
Fixed interest notes	265.1	154.7
Floating rate notes	2,768.6	2,535.7
	4,890.1	4,067.0
Equity securities		
Shares in listed and unlisted corporations	141.9	148.2
Unit trusts and managed funds	109.7	152.5
Shares in listed corporations held in relation to endowment warrants ²	41.5	38.4
	293.1	339.1
Infrastructure investments		
Units in listed and unlisted infrastructure trusts	416.2	489.6
Other infrastructure investments	239.9	–
	656.1	489.6
Property securities		
Indirect property investments in listed and unlisted trusts	173.4	154.5
Total financial assets at fair value through profit and loss	6,012.7	5,050.2
Available for sale equity securities ³	9.5	11.8
Total other financial assets	6,022.2	5,062.0
Current	3,139.8	1,366.5
Non-current	2,882.4	3,695.5
	6,022.2	5,062.0

¹ All financial assets at fair value through profit and loss are designated as such on initial recognition.² On 30 April 2004, the Group entered into a Deed of Assignment with Westpac Banking Corporation (WBC) whereby all legal and beneficial rights, title and interests in respect of these assets were assigned to WBC. See Note 17 for the corresponding liability.³ All available-for-sale financial assets are non-current.

12. Investment and development property

	30 June 2011 \$M	30 June 2010 \$M
Investment property held for sale ¹	22.0	–
Investment property in use	2,444.9	2,487.0
Investment property under development	27.0	25.0
Total investment property	2,493.9	2,512.0
Development property	80.0	98.1
Total investment and development property²	2,573.9	2,610.1
Held for sale	22.0	–
In use/under development	2,551.9	2,610.1
Reconciliation of carrying amounts		
Investment property in use		
Opening balance	2,487.0	1,892.4
Acquisitions ³	85.7	706.8
Sale of properties at cost	(14.6)	(97.7)
Transfer to investment property held for sale	(22.0)	–
Capital expenditure	10.4	9.1
Foreign currency exchange (loss)/gain	(106.6)	30.8
Net revaluation gain/(loss)	5.0	(54.4)
Closing balance	2,444.9	2,487.0
Investment property under development		
Opening balance	25.0	26.4
Capital expenditure	5.4	7.7
Net revaluation loss	(3.4)	(9.1)
Closing balance	27.0	25.0
Development property		
Opening balance	98.1	101.7
Sale of properties at cost	(30.5)	(18.1)
Development expenditure	12.4	14.5
Closing balance	80.0	98.1

¹ On 30 August 2010, contracts were exchanged for the sale of the Pacific Brands property. The carrying value at 30 June 2011 is based on the agreed sale price. The sale was settled in July 2011.

² Other than the amount described in 1 above, all investment and development property is considered to be non-current.

³ On 31 January 2010, the Group acquired a controlling interest in Challenger Kenedix Japan Trust (CKT).

12. Investment and development property (continued)

	Acquisition date	Total cost ¹⁰ additions \$M	Carrying value 2011 \$M	Cap ¹¹ rate 2011 %	Latest external valuation	Carrying value 2010 \$M	Cap ¹¹ rate 2010 %
Investment property in use/held for sale							
Australia							
Century City Walk, VIC ^{1,3}	16-Oct-06 30-Jun-08	30.0	30.0	8.50	30-Jun-11	30.0	8.50
Innaloo Cinema, WA ^{2,4}	17-Dec-01	34.2	41.0	8.00	30-Jun-11	35.5	8.00
Jam Factory, VIC ^{2,4}	4-Jul-00	104.0	104.0	8.25	30-Jun-11	104.5	8.50
Kings Langley, NSW ^{2,4}	29-Jul-01	15.3	15.7	8.75	30-Jun-11	16.0	8.25
County Court, VIC ⁴	30-Jun-00	201.9	276.1	7.25	31-Dec-10	273.0	7.00
CSIRO, NSW ⁵	27-Jun-01	150.7	159.1	8.00	30-Jun-11	159.0	8.00
Pacific Brands, Port Melbourne, VIC ^{2,4}	13-Nov-02	13.2	22.0	7.81	30-Jun-10	19.4	8.75
Goodman Fielder, North Ryde, NSW ^{2,4}	23-Feb-01	23.5	39.2	8.50	31-Dec-10	37.6	8.50
Kraft, Port Melbourne, VIC ^{2,4}	28-Jun-02	24.5	23.2	8.50	31-Dec-10	23.3	9.50
Rexel, North Ryde, NSW ^{1,4}	30-Nov-06 30-Jun-08	13.4	13.4	8.75	31-Dec-10	13.8	8.75
ABS Building, ACT ^{2,4}	1-Jan-00	122.4	148.0	7.75	30-Jun-11	148.0	7.50
DIAC Building, ACT ^{2,4}	1-Dec-01	105.1	113.2	7.75	30-Jun-11	112.0	7.75
Discovery House, ACT ^{2,4}	28-Apr-98	88.6	101.5	7.50	31-Dec-10	100.6	7.50
Elders House, SA ^{2,5}	21-Jun-02	45.6	47.5	8.75	30-Jun-11	47.3	8.75
Executive Building, Hobart, TAS ⁴	30-Mar-01	20.4	34.0	8.75	30-Jun-11	34.0	8.75
Makerston, QLD ^{2,9}	14-Dec-00	42.4	70.6	8.63	31-Dec-10	67.4	8.75
31 Queen Street, VIC ^{1,8}	31-Mar-11	86.5	86.5	8.00	30-Jun-11	n/a	n/a
417 St Kilda Rd, Melbourne, VIC ⁵	27-Jun-02	89.2	79.5	8.50	30-Jun-11	77.0	8.50
Taylor's Institute, Waterloo, NSW ^{2,4}	16-May-01	42.8	44.8	8.25	31-Dec-10	43.5	8.50
The Forum, Cisco, NSW ^{2,4}	5-Jan-01	61.9	103.2	8.35	31-Dec-10	102.9	8.35
The Forum, Verizon, NSW ^{2,4}	5-Jan-01	64.4	62.1	8.50	31-Dec-10	59.8	8.75
6 Foray St, Fairfield, NSW ^{1,3}	23-Oct-06	16.5	16.5	10.25	31-Dec-10	16.7	10.25
Cosgrove Industrial Park, Enfield, NSW ^{1,4}	31-Mar-07	20.7	20.8	8.25	31-Dec-10	20.5	8.25
Spotlight, Laverton North, VIC ^{1,4}	16-Oct-06	14.7	14.8	8.75	31-Dec-10	14.8	9.50
API Richlands, Richlands, QLD ^{1,4}	24-Oct-06	–	–	n/a	n/a	12.1	9.50
12-30 Toll Drive, Altona North, VIC ^{1,4}	16-Oct-06	13.4	13.4	8.75	30-Jun-11	13.0	9.25
2-10 Toll Drive, Altona North, VIC ^{1,4}	16-Oct-06	6.2	6.2	8.65	30-Jun-11	6.2	9.15
1-9 Toll Drive, Altona North, VIC ^{1,4}	16-Oct-06	3.6	3.6	8.50	30-Jun-11	3.6	9.00
Rendezvous Hotels ⁹	8-Dec-05	56.8	61.0	8.50	30-Jun-11	59.0	8.50
Total Australia		1,511.9	1,750.9			1,650.5	
Hungary³							
Mangro Kft	12-Apr-07	29.4	11.4	11.39	30-Jun-11	14.4	9.52
Namoc Kft	12-Apr-07	11.2	3.9	11.39	30-Jun-11	5.5	9.52
Rozalia Kft	12-Apr-07	11.9	4.4	11.39	30-Jun-11	6.4	9.52
Rozal Kft	12-Apr-07	7.0	2.5	11.39	30-Jun-11	3.5	9.52
Lazor Kft	12-Apr-07	7.1	2.5	11.39	30-Jun-11	3.3	9.52
Surplus Land	12-Apr-07	0.9	0.7	11.39	30-Jun-11	0.6	9.52
France^{1,6}							
Rue Charles Nicolle, Villeneuve les Beziers	06-Jun-07	11.9	12.1	7.98	30-Jun-11	12.4	8.25
Avenue de Savigny, Aulnay sous Bois	06-Jun-07	11.9	11.9	6.50	30-Jun-11	12.8	6.50
105 Route d'Orleans, Sully sur Loire	06-Jun-07	15.0	14.4	8.50	30-Jun-11	15.7	8.75
140 Rue Marcel Paul, Gennevilliers	06-Jun-07	8.6	9.9	7.21	30-Jun-11	9.3	7.50
ZAC Papillon, Parçay-Meslay	06-Jun-07	6.3	6.6	8.00	30-Jun-11	6.6	8.25
6 Rue Doulaclouew, Toulouse	06-Jun-07	–	–	n/a	30-Jun-09	2.6	8.50

	Acquisition date	Total cost additions \$M	Carrying value 2011 \$M	Cap ¹¹ rate 2011 %	Latest external valuation	Carrying value 2010 \$M	Cap ¹¹ rate 2010 %
Japan							
Carino Chitosedai ⁷	30-Jun-07	117.9	107.6	5.00	30-Jun-11	124.7	5.00
Carino Tokiwadai ⁷	30-Apr-07	76.9	66.3	5.20	30-Jun-11	76.1	5.20
Izumiya Hakubaicho ⁸	30-Apr-07	68.0	61.3	5.30	30-Jun-11	70.8	5.40
Unicus Ina ⁸	30-Apr-07	56.3	49.2	5.30	30-Jun-11	59.4	5.30
Valor Toda ⁷	30-Apr-07	42.2	38.2	5.70	30-Jun-11	44.7	5.70
Life Higashinakano ⁸	30-Apr-07	32.6	28.6	5.10	30-Jun-11	33.6	5.20
Life Asakusa ⁸	30-Apr-07	27.4	25.2	5.10	30-Jun-11	29.6	5.30
Osada Nagasaki ⁸	30-Apr-07	21.1	19.4	6.50	30-Jun-11	22.6	6.30
Yaoko Sakato Chiyoda ⁸	30-Apr-07	18.1	14.9	5.40	30-Jun-11	19.4	5.30
Sunny Noma ⁸	30-Apr-07	16.4	15.3	5.60	30-Jun-11	17.7	6.20
Kansai Super Saigo ⁸	30-Apr-07	13.0	11.7	5.70	30-Jun-11	14.0	6.10
Kojima Nishiarai ⁷	30-Apr-07	10.8	9.6	5.70	30-Jun-11	11.2	5.50
DeoDeo Kure ⁸	31-Aug-07	31.4	28.5	5.80	30-Jun-11	33.8	6.10
Seiyu Miyagino ⁸	30-Sep-07	9.6	8.6	6.00	30-Jun-11	10.4	6.20
Aeon Kushiro ⁷	31-Dec-07	27.8	27.4	5.90	30-Jun-11	30.0	6.10
Valor Ichinomiya ⁷	31-Dec-07	27.9	23.2	5.60	30-Jun-11	29.3	5.70
Life Nagata ⁸	29-Feb-08	25.2	23.6	5.30	30-Jun-11	26.9	5.30
Renaissance Fujimidai ⁷	29-Feb-08	28.3	26.5	5.30	30-Jun-11	30.2	5.30
Valor Takinomizu ⁷	31-Mar-08	26.8	23.8	5.60	30-Jun-11	28.4	5.70
Life Kema ⁸	31-Mar-08	28.8	26.8	5.30	30-Jun-11	30.5	5.30
Total overseas		827.7	716.0			836.4	
Investment property in use/held-for-sale							
		2,339.6	2,466.9			2,487.0	
TRE Data Centre	14-Apr-10	8.5	8.5	n/a	30-Jun-11	6.0	n/a
Enfield ¹	31-Mar-07	18.5	18.5	n/a	30-Jun-11	19.0	n/a
Investment property under development							
		27.0	27.0			25.0	
Maitland	6-Dec-06	80.0	80.0	n/a	30-Jun-11	91.8	n/a
Smithfield	3-Aug-07	–	–	n/a	30-Jun-11	6.3	n/a
Development property held for resale							
		80.0	80.0			98.1	

¹ Property is 100% owned by Challenger Diversified Property Group (CDI).

² Property is 60% owned by CDI and 40% by Challenger Life Company Limited (CLC).

³ Valued by JLL.

⁴ Valued by Savills.

⁵ Valued by M3.

⁶ Valued by Cushman Wakefield.

⁷ Valued by HIRO.

⁸ Valued by TOEL.

⁹ Valued by Colliers.

¹⁰ Total cost represents the original acquisition cost plus additions less full and partial disposals since acquisition date.

¹¹ The capitalisation rate is derived by dividing the net property income over the carrying value of an investment property.

12. Investment and development property (continued)

The carrying values for investment properties in use have been determined with reference to independent valuations using market capitalisation and discounted cash flow methods.

Other than where indicated below, the properties are partially debt financed with funding that contains a number of negative undertakings (including an undertaking not to create or allow encumbrances, and an undertaking not to incur financial indebtedness which ranks in priority to existing debt). This debt funding is in place via a note issuance under a security trust structure.

CSIRO and County Court are each financed via separate capital markets bond issuances. Security has been granted over these properties under the bond issuances, which includes a mortgage over the properties.

Maitland is partially funded by external debt. Security has been granted over each development in relation to that funding, which includes a mortgage over each property.

As at 30 June 2011 the Hungarian properties are not funded by debt and so are not subject to any security or charge.

As at 30 June 2011 the investment property portfolio occupancy rate was 94.3% (CLC), 94.0% (CDI) and 100% (Japan) with a weighted average lease expiry of 7.3 years (CLC), 4.9 years (CDI) and 13.3 years (Japan).

13. Plant and equipment

	30 June 2011 \$M	30 June 2010 \$M
Office plant and equipment at cost	47.7	44.7
Less accumulated depreciation	(25.4)	(20.5)
	22.3	24.2
Infrastructure plant and equipment at cost	69.0	43.9
Less accumulated depreciation	(5.6)	(5.0)
	63.4	38.9
Total plant and equipment	85.7	63.1

	Office \$M	Infra- structure \$M	Total \$M
Reconciliations			
30 June 2011			
Opening balance	24.2	38.9	63.1
Additions ¹	3.0	33.8	36.8
Depreciation expense	(4.9)	(1.5)	(6.4)
Foreign exchange losses	–	(7.8)	(7.8)
Closing balance	22.3	63.4	85.7
30 June 2010			
Opening balance	27.8	29.0	56.8
Additions	4.3	14.6	18.9
Disposals	(2.4)	–	(2.4)
Depreciation expense	(5.5)	(1.4)	(6.9)
Foreign exchange losses	–	(3.3)	(3.3)
Closing balance	24.2	38.9	63.1

All plant and equipment is non-current.

¹ Infrastructure additions includes \$0.8 million of capitalised pooled interest at an interest rate of 6.2%.

14. Other assets

	30 June 2011 \$M	30 June 2010 \$M
Rental bond deposits	28.3	32.7
Prepayments – deferred portfolio and origination costs	12.5	27.9
Other	9.9	12.6
Other SPV	0.7	3.8
Total other assets	51.4	77.0
Current	15.0	36.5
Non-current	36.4	40.5
Total other assets	51.4	77.0

15. Goodwill and other intangible assets

	30 June 2011 \$M	30 June 2010 \$M
Goodwill	505.4	509.7
Other intangible assets		
Software at cost	23.9	23.7
Less accumulated amortisation	(22.6)	(21.9)
Total software	1.3	1.8
Operating lease intangible at cost	22.8	22.8
Less accumulated amortisation	(3.4)	(2.7)
Foreign exchange losses	(7.3)	(5.1)
Total operating lease	12.1	15.0
Other intangible assets	13.4	16.8

	Goodwill		Software		Operating lease	
	30 June 2011 \$M	30 June 2010 \$M	30 June 2011 \$M	30 June 2010 \$M	30 June 2011 \$M	30 June 2010 \$M
Opening balance	509.7	688.7	1.8	3.0	15.0	18.1
Acquisitions via business combinations	–	11.1	–	–	–	–
Additions	–	–	0.2	0.5	–	–
Disposals	–	(190.2)	–	–	–	–
Acquisition purchase price adjustment	(2.1)	2.5	–	–	–	–
Foreign exchange losses	(2.2)	(2.4)	–	–	(2.2)	(2.4)
Amortisation expense	–	–	(0.7)	(1.7)	(0.7)	(0.7)
Closing balance	505.4	509.7	1.3	1.8	12.1	15.0

16. Impairment testing of goodwill

Goodwill acquired through business combinations is allocated to the Life and Funds Management cash-generating units (CGU) for impairment testing. The recoverable amount of goodwill for each CGU is determined via a 'value in use' calculation that utilises cash flow projections based on financial budgets, approved by senior management, covering an appropriate time horizon. The discount rates, based on the Group's cost of capital, and key assumptions are as follows.

	30 June 2011	30 June 2010	30 June 2011 Discount rate %	30 June 2010 Discount rate %	Cash flow horizon (years)
	\$M	\$M			
Life	418.4	420.6	11.5	11.8	5
Funds Management	87.0	89.1	11.5	11.8	5
Total	505.4	509.7			

Budgeted gross margins – is the average gross margins achieved in the year ended immediately before the budgeted year, adjusted for the expected impact of competitive pressure on margins and expected efficiency improvements.

Bond rate – this is taken as the yield on a government bond rate at the beginning of the budgeted year.

Growth rates – are consistent with long-term trends in the industry segments in which the businesses operate.

The derived values for the CGU are in excess of the carrying value of goodwill. Management are of the view that reasonably possible changes in the key assumptions, such as a change in the discount rate of 1% or a change in cash flow of 5%, would not cause the respective recoverable amounts for each CGU to fall short of the carrying amounts as at 30 June 2011. All goodwill is non-current.

17. Payables

	30 June 2011 \$M	30 June 2010 \$M
Trade creditors and accruals	112.6	131.1
Distributions payable	58.8	20.8
Warrant liability ¹	42.5	39.9
Unsettled trades payable	49.1	18.1
Other creditors	42.6	40.7
Payables – SPV	48.4	66.6
	354.0	317.2
Current	270.8	201.0
Non-current	83.2	116.2
	354.0	317.2

¹ On 30 April 2004, the Group entered into a Deed of Assignment with Westpac Banking Corporation (WBC) whereby all legal and beneficial rights, title and interests in respect of a portfolio of financial assets were assigned to WBC, see Note 11 for details. The difference between the equity assets and warrant liability equals dividends receivable which are only assigned when paid.

18. Interest bearing liabilities

	30 June 2011		30 June 2010	
	Outstanding \$M	Facility \$M	Outstanding \$M	Facility \$M
Bank loans				
Recourse – Corporate	–	100.0	–	100.0
Non-recourse – Controlled property trusts	812.1	865.5	839.3	1,039.9
Non-recourse – Controlled infrastructure trusts	206.1	211.0	–	–
Total bank loans	1,018.2	1,176.5	839.3	1,139.9
Non-recourse non-bank loans				
Subordinated debt issuance	477.8	477.8	475.1	475.1
Loan note finance	63.1	63.1	66.2	66.2
Controlled property trusts	9.4	9.4	7.0	7.0
Total non-bank loans	550.3	550.3	548.3	548.3
Total interest bearing liabilities	1,568.5	1,726.8	1,387.6	1,688.2
Current	455.4		127.3	
Non-current	1,113.1		1,260.3	
	1,568.5		1,387.6	

Bank loans

Corporate – The facility of \$100 million is secured by guarantees in place between members of the Group. A floating interest rate was applied to this facility during the period.

Controlled property trusts – 30 June 2011 balance includes \$401.4 million (30 June 2010: \$463.2 million) of Yen denominated loans in the Japanese property trusts (30 June 2011 ¥34.8 billion, 30 June 2010: ¥34.8 billion). These loans have a mix of fixed and variable terms, are secured by way of first ranking mortgages over the investment properties and they mature in 2012.

Also included is a multi-option syndicated finance facility held by Challenger Diversified Property Trust (CDI) with Westpac Banking Corporation Limited (WBC) and Commonwealth Bank of Australia Limited (CBA). The total outstanding at 30 June 2011 is \$226.6 million (30 June 2010: \$165.5 million). Subsequent to the year end, CDI executed an amended facility agreement with WBC and CBA. The new limit is \$280.0 million, being three tranches with a limit of \$90.0 million, \$100.0 million and \$90.0 million maturing in 2013, 2014 and 2015 respectively. All tranches are able to be drawn in either Euros or Australian dollars and interest is calculated at floating rates plus a margin.

Bank loans in the other unlisted property trusts of \$184.1 million (June 2010: \$210.6 million) are secured solely by fixed and floating first mortgages over investment properties.

Controlled infrastructure trusts – The \$206.1 million loan is initially in the form of a construction facility that terminates in December 2011 at which point it automatically converts to an amortising facility with an expiry date of June 2016. This facility has variable terms and is secured by the way of a first ranking mortgage over the infrastructure asset.

Non-bank loans

Subordinated debt issuance – The Group issued subordinated notes into the US private placement market of US\$150 million in December 2006 and A\$400 million in November 2007. The notes were issued under an APRA approved Instrument of Issue and count as Approved Subordinated Debt for regulatory capital purposes.

The December 2006 notes are unsecured and were issued in two maturities (US\$125 million at 10 years with a non-call period of five years; and US\$25 million at 20 years with a non-call period of 10 years). A portion of this subordinated debt has a fixed interest rate with the remaining portion being floating. The November 2007 issuance was unsecured and matures at 30 years with a non-call period of 10 years.

The proceeds of both issuances were made available to Statutory Fund No.2 of Challenger Life Company Limited (SF2) and rank in right of payment either pari passu with, or senior to, all other unsecured and subordinated indebtedness of SF2, except for such indebtedness preferred by operation of bankruptcy laws or similar laws of general application. Subordinated debt is measured at fair value through profit and loss and adjusted for movements in interest rates, credit spreads and foreign exchange.

18. Interest bearing liabilities (continued)

Non-bank loans (continued)

Loan note finance – The Group has entered into a restricted recourse £25 million loan that is secured against properties. The fixed rate interest applied has been capitalised and is expected to be repaid together with the principal in 2012 (but no later than 2015).

Controlled property trusts – Non-bank loans in the unlisted property trusts are secured solely by fixed and floating first mortgages over properties.

19. External unit holders' liabilities

The Group controls a number of guaranteed index return trusts that contain contributed funds in respect of fixed term wholesale mandates. The external unit holders' liabilities represent the balance owing to third parties on these mandates.

	30 June 2011 \$M	30 June 2010 \$M
Current	490.0	131.5
Non-current	826.7	1,127.5
Total liabilities to external unit holders	1,316.7	1,259.0

20. Provisions

	30 June 2011 \$M	30 June 2010 \$M
Surplus lease provision	14.1	16.8
Employee entitlements	6.9	8.2
Relocation provision	4.4	3.6
Other provisions	4.9	13.9
	30.3	42.5

	Surplus lease provision \$M	Employee entitlements \$M	Relocation provision \$M	Other \$M
30 June 2011				
Opening balance	16.8	8.2	3.6	13.9
Arising during the year	1.3	9.3	0.8	4.5
Amounts utilised	(4.0)	(10.6)	–	(13.5)
Closing balance	14.1	6.9	4.4	4.9
30 June 2010				
Opening balance	21.0	13.5	2.8	15.6
Arising during the year	2.5	9.8	1.3	3.8
Amounts utilised	(6.7)	(15.1)	(0.5)	(5.5)
Closing balance	16.8	8.2	3.6	13.9

Surplus lease provision represents the Group's net rental expense obligation on surplus space in leased buildings in Sydney and London and the obligation on these leases expires in 2016. The relocation provision represents the Group's net make-good obligations on building leases.

21. Life contract liabilities

	30 June 2011 \$M	30 June 2010 \$M
Life investment contract liabilities – at fair value	4,998.2	4,096.1
Life insurance contract liabilities – at Margin on Services valuation	605.9	637.0
Reinsurance contract liabilities – at Margin on Services valuation	24.9	12.7
Total life contract liabilities	5,629.0	4,745.8

	Life investment contract liabilities		Life insurance contract liabilities		Reinsurance contract liabilities		Total contract liabilities	
	2011 \$M	2010 \$M	2011 \$M	2010 \$M	2011 \$M	2010 \$M	2011 \$M	2010 \$M
Reconciliation								
Opening balance	4,096.1	3,964.4	637.0	609.4	12.7	–	4,745.8	4,573.8
Deposits and premium receipts	1,898.0	933.1	5.6	–	–	–	1,903.6	933.1
Payments and withdrawals	(1,203.3)	(1,100.3)	(52.5)	(52.6)	(2.0)	–	(1,257.8)	(1,152.9)
Revenue per Note 3	(36.5)	91.9	(15.3)	46.9	14.2	12.7	(37.6)	151.5
Expense per Note 4	243.9	207.0	31.1	33.3	–	–	275.0	240.3
Closing balance	4,998.2	4,096.1	605.9	637.0	24.9	12.7	5,629.0	4,745.8

	30 June 2011 \$M	30 June 2010 \$M
Analysis of life insurance contract liability and expenses		
Best estimate liability		
Value of future life insurance contract benefits	573.0	605.1
Value of future expenses	32.9	31.9
Total best estimate liability	605.9	637.0
Value of future profit margins	–	–
Gross life insurance contract liability	605.9	637.0
Life insurance contract operating expenses		
Maintenance expenses – commission	0.4	0.4
Maintenance expenses – other	2.9	2.3
Total life insurance contract operating expenses	3.3	2.7
Analysis of life contract profit		
Profit attributable to life insurance contracts	33.1	45.1
Profit attributable to life investment contracts	266.0	257.2
Profit arising from difference between actual and assumed experience	299.1	302.3
Investment earnings on assets in excess of life contract liabilities	61.3	11.1
Life contract profit¹	360.4	313.4

¹ This profit represents that made by the statutory funds of Challenger Life Company Limited only and includes the investment return on assets backing the life contract liabilities.

21. Life contract liabilities (continued)

Methodology applied in the valuation of life contract liabilities

Life investment contracts are policies regulated by the *Life Insurance Act 1995* (the *Life Act*) that do not meet the definition of an insurance contract (under AASB 4 *Insurance Contracts*) and are measured at fair value through profit and loss. Life insurance contracts are policies regulated by the *Life Act* that meet the definition of an insurance contract and are measured using the Margin on Services (MoS) methodology.

The MoS valuation, calculated in accordance with Prudential Standards, results in the systematic release of planned margins over the life of the policy via a 'profit carrier'. The Group maintains only one type of life insurance contract, being individual lifetime annuities. Annuity payments are used as the profit carrier when determining the life insurance contract liability and the resulting profit recognition.

Key assumptions applied in the valuation of life contract liabilities

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. These rates are set at a margin to the swap curve, with the margin determined by reference to current observable market rates including government guaranteed bank debt and credit-risk adjusted corporate bonds. Discount rates applied at 30 June 2011 were between 5.04% and 6.15% (2010: 4.87% - 5.89%).

Maintenance expenses – are based on budgets for the financial year. The expenses are converted to a per-contract unit cost or percentage of account balance, depending on their nature, based on an expense analysis.

Inflation – based on long-term expectations and reviewed 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 is 2.64% for short-term inflation and 2.94% for long-term (2010: 2.43% short-term, 2.53% long-term).

Voluntary discontinuances/surrenders – no surrenders or voluntary discontinuances are assumed.

Mortality – base mortality rates are determined as a multiple of United Kingdom annuitant lives experience from 1999 to 2002 (IML00 and IFL00 tables), adjusted for expected future mortality improvements based on observed improvements in Australia. Rates of future mortality improvement applied at 30 June 2011 are between 1.0% and 4.0% (2010: 1.0% - 4.0%).

Impact of changes in assumptions on life insurance contracts

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

Restrictions on assets

The *Life Insurance Act 1995* requires the Group to hold investments to back life contract liabilities in separate statutory funds. The assets in a statutory fund can only be used to meet the liabilities and expenses of that fund, to acquire investments to further the business of the fund or as distributions when solvency and capital adequacy requirements are met.

Statutory fund information

The Group has three statutory funds. Fund 1 is a non-investment-linked fund and Fund 3 is investment-linked. Both are closed to new business. Fund 2 contains non-investment-linked contracts, including the Group's term annuity core business plus the lifetime annuity policies and the related reinsurance. Life contract liabilities for funds 1, 2 and 3 are \$6.9 million, \$5,618.2 million and \$3.9 million respectively (2010: \$8.2 million, \$4,733.6 million, \$4.0 million).

Current/non-current split for total life contracts

There is a fixed settlement date for the majority of life contract liabilities. Approximately \$837.0 million (2010: \$580.0 million) of life contract liabilities have a contractual maturity within 12 months of the reporting date. Based on assumptions applied for the 30 June 2011 valuation of life contract liabilities, \$1,029.0 million of principal payments on fixed term and lifetime business are expected in the year to 30 June 2012 (2011: \$789.0 million).

Life insurance risk

The Group is exposed to longevity risk on its life insurance liabilities, being the risk that annuitants may live longer than expectations. The Group manages this risk by using reinsurance as well as the regular review of the portfolio to confirm continued survivorship of annuitants receiving income plus regular review of mortality experience to ensure that mortality assumptions remain appropriate.

Insurance risk sensitivity analysis

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

	Increase in life insurance contract liabilities				Profit and equity impact			
	Gross		Net		Gross		Net	
	30 June 2011 \$M	30 June 2010 \$M	30 June 2011 \$M	30 June 2010 \$M	30 June 2011 \$M	30 June 2010 \$M	30 June 2011 \$M	30 June 2010 \$M
50% increase in the rate of mortality improvement	49.9	53.1	2.9	1.0	(34.9)	(37.2)	(2.0)	(0.7)
10% increase in maintenance expenses	2.9	2.7	2.9	2.7	(2.0)	(1.9)	(2.0)	(1.9)

Liquidity risk for insurance contracts

The following table summarises the undiscounted maturity profile of the Group's life insurance contracts. 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 27.

	1 year or less \$M	1-3 years \$M	3-5 years \$M	>5 years \$M	Total undiscounted amount \$M
Life insurance contract liabilities					
2011	54.4	107.6	104.8	837.6	1,104.4
2010	54.4	108.2	106.1	901.6	1,170.4

Actuarial information

Mr A Bofinger FIAA, as the Appointed Actuary of Challenger Life Company Limited, is satisfied as to the accuracy of the data used in the valuations of life contract liabilities in the financial report, the tables in this note and the solvency ratio in Note 23. The life contract liabilities and solvency ratios have been determined at the reporting date in accordance with the *Life Insurance Act 1995*.

22. Special Purpose Vehicles

Special purpose vehicles (SPV) are entities that fund pools of residential mortgage loans via the issuance of residential mortgage backed securities. All borrowings of these SPV are limited in recourse to the assets of the SPV. The Group is not originating any significant new mortgage assets or securitised liabilities but is managing the run-off of the portfolio.

The Group is deemed to control these entities as a consequence of holding the beneficial interest to the residual income stream but the major risks and rewards, notably credit risk, lie with the mortgage backed security holder. The assets and liabilities of the SPV have been separately disclosed in the financial report as this presentation is considered to provide a more transparent view of the Group's financial position. Transactions between the SPV and other entities within the Group are eliminated on consolidation. The amounts in respect of the SPV included in the consolidated Group, subject to the footnote on Payables below, are as follows.

	30 June 2011 \$M	30 June 2010 \$M
Cash and cash equivalents	386.4	458.1
Receivables	6,889.8	8,466.8
Other assets	0.7	3.8
Total assets	7,276.9	8,928.7
Payables ¹	308.2	291.7
Derivative liability	5.4	6.9
Interest bearing liabilities	6,968.7	8,637.0
Total liabilities	7,282.3	8,935.6
Net assets	(5.4)	(6.9)
Cash flow hedge reserve	(5.4)	(6.9)
Total equity attributable to residual income unit holders	(5.4)	(6.9)

¹ Payables differs from the SPV Payables per Note 17 by the value of the cumulative eliminations between the SPV and other members of the Group.

22. Special Purpose Vehicles (continued)

SPV receivables is stated net of impairment measured as any shortfall between the carrying amount of the loan and the present value of expected future cash flows, discounted at the loan's original effective interest rate and adjusted for lenders mortgage insurance coverage. A reconciliation of the provision is as follows:

	30 June 2011 \$M	30 June 2010 \$M
Opening balance	58.6	83.0
Additional accruals and adjustments to estimates	2.0	(3.9)
Utilisation of provision against incurred losses	(6.1)	(20.5)
Closing balance	54.5	58.6

23. Contributed equity

	30 June 2011		30 June 2010	
	No. of shares M	\$M	No. of shares M	\$M
Ordinary shares issued	497.6	1,191.1	507.1	1,235.6
LTIP shares treated as treasury shares	(1.4)	(5.1)	(10.0)	(35.1)
CPP Trust shares treated as treasury shares	(19.3)	(84.9)	(25.4)	(93.9)
Total contributed equity	476.9	1,101.1	471.7	1,106.6
Ordinary shares				
Movement in contributed equity:				
Opening balance	507.1	1,235.6	596.0	1,563.0
Cancelled under share based payment plan	—	—	(6.7)	(17.3)
Cancelled under share buy-back	(9.5)	(44.5)	(82.2)	(310.1)
Closing balance	497.6	1,191.1	507.1	1,235.6
LTIP				
Opening balance	10.0	35.1	40.7	117.5
Shares forfeited and cancelled	—	—	(6.7)	(17.3)
Shares transferred to CPP Trust	(7.1)	(25.9)	(20.5)	(56.1)
Vested shares released from LTIP plan	(1.5)	(4.1)	(3.5)	(9.0)
Closing balance	1.4	5.1	10.0	35.1
CPP Trust				
Opening balance	25.4	93.9	12.7	44.1
Shares purchased	11.1	51.2	5.4	20.0
Shares transferred from LTIP	7.1	32.1	20.5	74.7
Vested shares released to employees	(24.3)	(92.3)	(13.2)	(44.9)
Closing balance	19.3	84.9	25.4	93.9
	No. of shares \$M		No. of shares \$M	
Analysis of ordinary shares issued				
Listed on the ASX	496.7		499.6	
Unvested LTIP shares not listed on the ASX	0.9		7.5	
Total ordinary shares issued	497.6		507.1	

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.

Shares issued under the Long Term Incentive Plan (LTIP) – The terms and conditions of shares issued under the LTIP are disclosed in Note 31 of the financial report. The shares held under the LTIP are treated as treasury shares and deducted from equity.

Challenger Performance Plan Trust (CPP Trust) – The CPP Trust is a controlled entity and holds shares in the Company. As a result, the CPP Trust's shareholding in the Company is disclosed as treasury shares and deducted from equity and dividends paid from the Company to the CPP Trust are eliminated on consolidation.

Capital risk 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.

The Group manages capital risk via Capital Management Plans at both the Group and the prudentially regulated Challenger Life Company Limited (CLC) levels. The objective of these plans is to maintain financial stability of the Group and CLC whilst ensuring the shareholders earn an appropriate risk adjusted return through optimisation of the capital structures. The Capital Management Plans are approved by the respective boards and are reviewed at least annually.

Capital Management Plan – Group

The Group Capital Management Plan aims to maintain an investment grade credit rating and robust capital ratios in order to support its business objectives and maximise shareholder wealth. The Group believes that maintaining an investment grade rating is the most appropriate target from a capital structure perspective and is essential in order to secure access to capital at a reasonable cost.

Standard & Poor's long-term credit ratings for the Group and CLC as at the balance date are BBB+ (Stable) and A (Stable) respectively. There were no changes to either the Group or CLC ratings during the period.

The capital structure of the Group is monitored by reference to the gearing ratio, calculated as follows:

Gearing ratio = net recourse debt divided by (net recourse debt + common equity).

Where **net recourse debt** is calculated as recourse debt less cash and cash equivalents and **common equity** equates to **equity attributable to equity holders** per the balance sheet, that is, the aggregate of contributed equity, reserves, and retained profits less equity attributable to non-controlling interests.

To maintain the preferred investment grade rating, the Capital Management Plan targets a gearing ratio of no more than 30% and this ratio was not exceeded during the year. The year-end gearing ratio is as follows:

	30 June 2011 \$M	30 June 2010 \$M
Net recourse debt	–	–
Available cash	93.0	76.1
Total common equity	1,488.3	1,339.6
Gearing ratio (%)	0%	0%

The Group's current dividend payout ratio target is 30% of normalised profit after tax (as defined in Note 2). There were no material changes to the Group's Capital Management Plan during the year.

Capital Management Plan – CLC

CLC is a life insurance company regulated under the *Life Insurance Act 1995* (the *Life Act*). The *Life Act*, via Prudential Standards issued by APRA, imposes minimum statutory capital requirements on all life insurance companies. CLC complied with these requirements at all times during the year.

23. Contributed equity (continued)

Separate and distinct from the Group, CLC's Capital Management Plan integrates the statutory capital and solvency requirements, insurer financial strength rating as assessed by Standard & Poor's, and economic capital requirements. There were no material changes to CLC's Capital Management Plan during the financial year. CLC's resources available to meet statutory capital requirements at balance date are set out in the table below:

	30 June 2011 \$M	30 June 2010 \$M
Shareholder equity	1,267.8	1,123.8
Subordinated debt	477.8	475.1
Total regulatory capital	1,745.6	1,598.9
Solvency reserve		
Solvency reserve %	34.1	40.1
Coverage of solvency reserve (times) ¹	1.5	1.5

¹ APRA Prudential Standards establish a two-tier capital requirement for Life companies. These figures relate to the first tier (the solvency reserve) that is intended to ensure the solvency of the company, i.e. the ability to meet its obligations to life contract holders as and when they fall due. It is calculated as the assets available for solvency divided by the solvency reserve as defined by the APRA Prudential Standards.

24. Reserves

	30 June 2011 \$M	30 June 2010 \$M
Equity option premium reserve		
Opening balance	125.3	125.2
Amortisation of issue costs	0.1	0.1
Closing balance	125.4	125.3
Share based payments reserve		
Opening balance	80.2	57.8
Share based payments for the period	26.1	49.7
Releases from share based payment premium reserve	(43.6)	(27.3)
Closing balance	62.7	80.2
Available-for-sale asset revaluation reserve		
Opening balance	(0.2)	0.5
Revaluation loss net of tax	(1.4)	(5.6)
Impairment loss taken to income statement	–	4.9
Closing balance	(1.6)	(0.2)
Cash flow hedge reserve		
Opening balance	–	(1.3)
Charged to equity	–	1.3
Closing balance	–	–
Cash flow hedge reserve – SPV		
Opening balance	(6.9)	(13.7)
Charged to equity	1.5	6.8
Closing balance	(5.4)	(6.9)
Foreign currency translation reserve		
Opening balance	4.4	(0.6)
(Loss)/gain on translation of foreign entities	(41.3)	21.8
Gain/(loss) on hedge of net investment in foreign entities	23.8	(16.8)
Closing balance	(13.1)	4.4

	30 June 2011 \$M	30 June 2010 \$M
Adjusted controlling interest reserve		
Opening balance	8.3	–
Discount on increase in holding in controlled entity	3.5	8.3
Closing balance	11.8	8.3
Total reserves	179.8	211.1

Nature and purpose of reserves

Equity option premium reserve

This reserve represents the valuation assigned to options issued to Consolidated Press Holdings and to Colony Marlin-Holdings LLC.

	Grant date	Expiry date	Exercise price	Number
Shares under option				
Consolidated Press Holdings Limited ¹	22 Dec 2003	22 Dec 2013	\$3.25	60,000,000
Colony Marlin-Holdings LLC ²	07 Nov 2007	07 Nov 2012	\$7.00	57,142,857

¹ Options issued to Consolidated Press Holdings Limited are non-transferable call options and may be exercised at any time within 10 years from their grant date.

² Options issued to Colony Marlin-Holdings LLC are non-transferable call options and may be exercised at any time within five years from their grant date.

Share based payments reserve

An expense is recognised over the vesting period of share options, performance rights and capped performance rights granted to employees as part of the Challenger Performance Plan and the Long Term Incentive Plan. This expense is based on the valuation of the equity benefits granted at the grant date. When an instrument is granted, and an expense incurred, there is a corresponding increase in the share based payments reserve directly in equity. The total of this reserve is net of any gain or loss realised on the disposal of forfeited shares held within the schemes.

Available-for-sale asset revaluation reserve

This reserve includes the cumulative net change in the fair value of financial assets classified as available-for-sale until the investment is derecognised or sold.

Cash flow hedge reserve

The cash flow hedge reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments related to hedged transactions that have not yet occurred.

Foreign currency translation reserve

The foreign currency translation reserve is used to record foreign exchange differences arising from the translation of the financial statements 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 interest 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.

25. Retained earnings

	30 June 2011 \$M	30 June 2010 \$M
Opening balance	21.9	(187.4)
Profit attributable to equity holders	261.4	282.5
Dividends paid	(75.9)	(73.2)
Closing retained earnings	207.4	21.9

26. Non-controlling interests

	30 June 2011 \$M	30 June 2010 \$M
Representing the following share of equity in the applicable entity:		
Contributed equity	357.8	437.9
Reserves	(7.8)	(6.5)
Opening retained losses	(70.0)	(62.6)
Profit for the year	31.1	11.3
	311.1	380.1

27. Financial risk management**Governance and risk management framework**

The Group's activities expose it to a variety of financial risks, such as market risk (including currency risk, interest rate risk, equity price risk and credit spread risk); credit default risk; and liquidity risk.

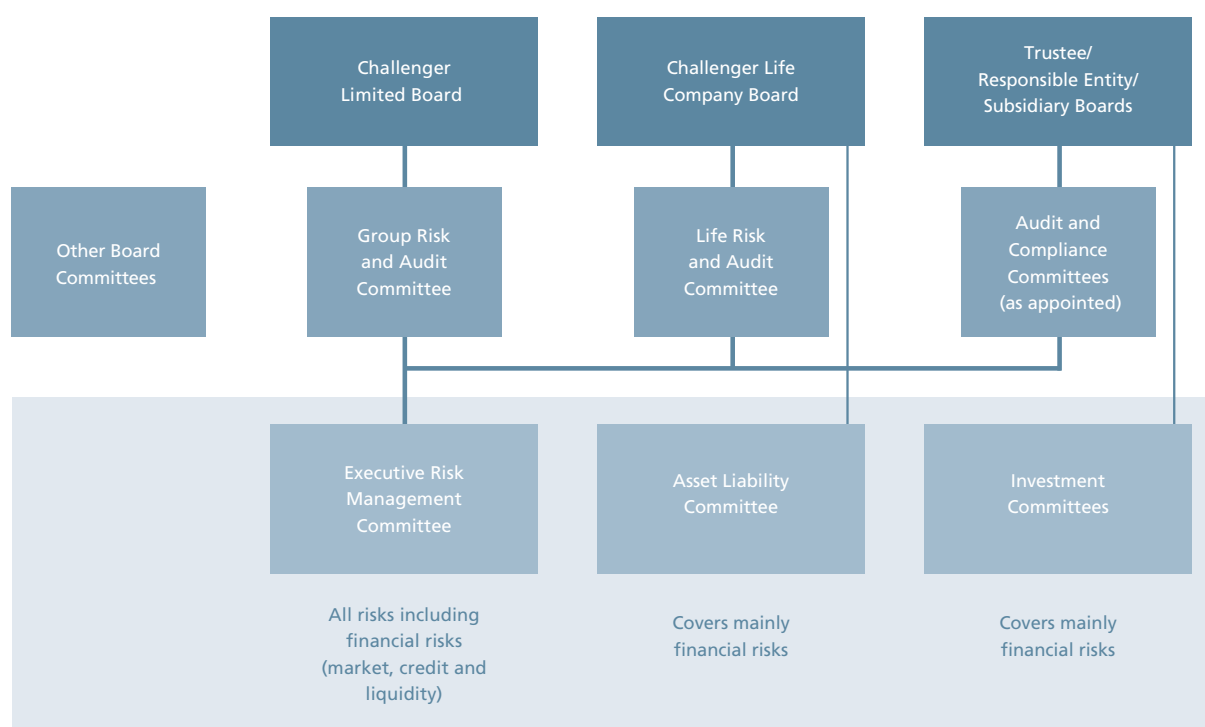
The management of risks is fundamental to the Group's business and to building shareholder value. The Board is responsible, in conjunction with senior management, for understanding the risks associated with the activities of the Group and putting in place structures and policies to adequately monitor and manage those risks.

The Board has established the Group Risk and Audit Committee (GRAC) as a board sub-committee to assist in the discharge of its responsibilities. In particular, setting risk appetite and ensuring the Company has an effective risk management framework incorporating management, operational and financial controls.

The Executive Risk Management Committee (ERMC) is an executive committee, chaired by the Chief Risk Officer (CRO), which assists the GRAC and Board in the discharge of their risk management obligations by implementing the Board approved Risk Management Framework.

The 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 GRAC and the Board. See below for a diagrammatic overview of the risk management framework of the Group.

Governance and risk management



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

Details of the significant accounting policies and methods adopted, including the criteria for recognition, the basis of measurement and the basis on which income and expenses are recognised, in respect of each class of financial instruments, are disclosed in Note 1.

Market risk

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

27. Financial risk management (continued)

Interest rate risk

Interest rate risk is the risk to the Group's earnings and equity arising from movements in 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 the interest rates.

It is the Group's policy to minimise the impact of interest rate movements on debt servicing capacity, Group profitability, business requirements and company valuation. The Group targets hedging of between 30% and 70% of drawn net recourse interest bearing liabilities of the corporate segment. The amount of drawn net recourse corporate interest bearing liabilities, and their duration, is determined with reference to the annual budget and the most current forecasts. The Group's strategy is to have no interest rate hedges with duration greater than five years and targets average hedge duration of three years.

Challenger Life Company Limited's (CLC's) Market Risk Policy is approved by the CLC Board and sets out the relevant risk limits for interest rate exposure. It is CLC's policy to minimise the impact of interest rate movements on its ability to service life contract holders. 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 Insurance Act 1995*. This includes satisfying solvency requirements, which in turn include consideration of how the interest rate sensitivity of assets and liabilities are matched.

Challenger Diversified Property Group (CDI) is also exposed to interest rate risk arising from liabilities bearing variable interest rates. Interest rate swaps are taken out to effectively hedge interest rates on a minimum of 60% of expected borrowings over the next 2 to 10 years.

For the Special Purpose Vehicles (SPV) the impact of a rising/falling BBSW benchmark over the Reserve Bank of Australia's target cash rate results in an increase/decrease in the cost of funding and therefore on the profit of the trusts. This interest rate risk is mitigated by actively adjusting the interest rate charged to borrowers if a sustained adverse differential to the benchmark is evidenced. SPV 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 for a floating rate on an amount equal to the notional value of the mortgages being fixed.

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 balance 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.

	Change in variable	Profit/(loss) 30 June 2011 \$M	Change in equity 30 June 2011 \$M	Profit/(loss) 30 June 2010 \$M	Change in equity 30 June 2010 \$M
Non-SPV	+100bps	6.4	6.4	11.0	11.0
	-100bps	(6.5)	(6.5)	(11.2)	(11.2)
SPV	+100bps	(6.1)	(6.1)	(7.4)	(7.4)
	-100bps	6.1	6.1	7.4	7.4
Total	+100bps	0.3	0.3	3.6	3.6
	-100bps	(0.4)	(0.4)	(3.8)	(3.8)

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

Price risk

Price risk is the risk that the fair value of a financial instrument will fluctuate because 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 traded on the market. The Group is exposed to equity price risk on its holdings in equity securities and credit spread risk on its debt securities.

It is the Group's policy to hedge the exposure resulting from movements in the value of listed equity portfolio investments. Equity investments regarded as 'operational' or 'strategic' will not be hedged. CLC is required to fair value all equities held to back life contract liabilities. No other entities within the Group have any significant exposure to equity price risk.

Equity price risk sensitivity

The potential impact of movements in the market value of listed and unlisted equities on the Group's income statement and balance sheet is shown in the below sensitivity analysis. This sensitivity analysis has been performed to assess the direct risk of holding equity instruments; therefore any potential indirect impact on fees from the Group's funds management business has been excluded. It is assumed that the relevant change occurs as at the reporting date.

Asset class	Change in variable	Profit/ (loss) 30 June 2011 \$M	Change in equity 30 June 2011 \$M	Profit/ (loss) 30 June 2010 \$M	Change in equity 30 June 2010 \$M
Property securities	+10%	11.8	11.8	10.8	10.8
	-10%	(11.8)	(11.8)	(10.8)	(10.8)
Infrastructure investment	+10%	24.8	24.8	34.4	34.4
	-10%	(24.8)	(24.8)	(34.4)	(34.4)
Available-for-sale assets	+10%	—	0.7	—	0.8
	-10%	(0.7)	(0.7)	(0.8)	(0.8)
Other assets	+10%	20.4	20.4	21.5	21.5
	-10%	(20.4)	(20.4)	(21.5)	(21.5)

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 above a 10% movement in equity prices would have a material impact on the consolidated Group's financial position.

Credit spread risk sensitivity

The Group is exposed to movements in credit spreads above the interbank swap curve through its debt securities. As at 30 June 2011, a fifty basis point increase/decrease in credit spreads would result in a post-tax (at 30%) unrealised loss/gain in the income statement and equity of \$62.5 million (2010: \$50.1 million).

Currency risk

It is the Group's policy to hedge the exposure of all balance sheet items to movements in foreign exchange rates. 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, British Pound, Japanese Yen and US Dollar against the Australian Dollar. In order to protect against 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 Japanese controlled property trust 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. The policy is to monitor the hedges closely and rebalance for maturities and underlying changes to the net assets. Effectiveness is monitored on a regular basis to ensure that the hedge remains within 80% to 125% effective and any ineffective portion of the hedge is recognised directly in the income statement.

The SPV entities hedge exposure to foreign currency risk arising from issuing mortgage backed securities in foreign currency. The currencies impacted are primarily the British Pound, Euro and US Dollar. All derivatives in the SPV are designated as cash flow hedges. These hedges are effective and there is no material impact on the results.

27. Financial risk management (continued)

Currency risk (continued)

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 2011					
Financial assets	509.8	1,053.0	795.6	243.4	92.8
Financial liabilities	–	(131.7)	(52.7)	(4.4)	–
Foreign currency contracts and cross currency swaps	(489.4)	(921.1)	(783.6)	(244.9)	(88.4)
Net exposure in Australian dollars	20.4	0.2	(40.7)	(5.9)	4.4
30 June 2010					
Financial assets	418.7	949.8	662.0	297.1	44.2
Financial liabilities	(0.4)	(164.8)	–	(10.9)	–
Foreign currency contracts and cross currency swaps	(410.8)	(771.6)	(664.0)	(290.4)	(39.4)
Net exposure in Australian dollars	7.5	13.4	(2.0)	(4.2)	4.8

The analysis below shows the impact on the income statement and equity of a movement in foreign currency exchange rates against the Australian dollar on the Group's major currency exposures using the net exposure at the balance date. All underlying exposures and related hedges are included in the analysis. A sensitivity of 10% has been chosen as this is a reasonable measurement given the current level of exchange rates and the volatility observed on an historic basis.

	Movement in variable against A\$	Profit/(loss) 30 June 2011 \$M	Change in equity 30 June 2011 \$M	Profit/(loss) 30 June 2010 \$M	Change in equity 30 June 2010 \$M
British Pound (GBP)	+10%	1.4	1.4	0.5	0.5
	–10%	(1.4)	(1.4)	(0.5)	(0.5)
US Dollar (USD)	+10%	–	–	0.9	0.9
	–10%	–	–	(0.9)	(0.9)
Euro (EUR)	+10%	(2.8)	(2.8)	(0.1)	(0.1)
	–10%	2.8	2.8	0.1	0.1
Japanese Yen (JPY)	+10%	–	6.8	–	8.3
	–10%	–	(6.8)	–	(8.3)
Other	+10%	0.3	0.3	0.2	0.2
	–10%	(0.3)	(0.3)	(0.2)	(0.2)

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 above a 10% movement in exchange rates would have minimal impact on the Group's financial position.

Credit default risk

Credit default risk is the risk of loss in value of an asset due to a counterparty failing to discharge an obligation. The Group's credit risk framework is based on the following core principles:

- independence from risk originators;
- recognition of the different risks in the various Group businesses;
- credit exposures are systematically controlled and monitored;
- credit exposures are regularly reviewed in accordance with existing credit procedures; and
- credit exposures include such exposures arising from derivative transactions.

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

Credit exposure by credit rating

The Group makes use of external ratings (Standard & Poor's, Fitch, Moody's or another reputable credit rating agency) and will ordinarily adopt a rating no greater than the lowest external rating assigned. Where an external rating is not available, an internal or implied rating will be used. Internal ratings are expressed on the basis of Standard & Poor's rating definitions. All credit exposures with an external rating are also rated internally and cross referenced to the external rating, if applicable. Internal credit ratings are assigned by appropriately qualified and experienced credit personnel who are independent from the risk originators.

The following table 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. 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-investment grade	Other	Total
	AAA	AA	A	BBB	grade		
	\$M	\$M	\$M	\$M	\$M	\$M	\$M
30 June 2011							
Cash and cash equivalents	788.6	–	–	–	–	–	788.6
Cash and cash equivalents – SPV	386.4	–	–	–	–	–	386.4
Receivables	0.5	4.1	0.2	65.2	–	48.3	118.3
Receivables – SPV	4,029.4	2,818.1	23.6	–	18.7	–	6,889.8
Debt securities	1,311.3	895.5	1,071.8	661.7	837.6	112.2	4,890.1
Derivative assets	2.4	62.5	256.3	–	39.0	–	360.2
Total	6,518.6	3,780.2	1,351.9	726.9	895.3	160.5	13,433.4

30 June 2010

Cash and cash equivalents	674.1	–	–	–	–	–	674.1
Cash and cash equivalents – SPV	458.1	–	–	–	–	–	458.1
Receivables	0.2	0.2	0.1	48.4	–	64.1	113.0
Receivables – SPV	7,914.3	496.6	32.5	20.7	2.7	–	8,466.8
Debt securities	1,305.7	762.4	902.5	279.9	816.5	–	4,067.0
Derivative assets	–	178.2	78.4	–	30.5	–	287.1
Total	10,352.4	1,437.4	1,013.5	349.0	849.7	64.1	14,066.1

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

Ageing and impairment of amortised cost financial assets

The below tables give information regarding the carrying value of the Group's financial assets measured at amortised cost. The analysis splits these assets by those that are neither past due nor impaired; those that are past due and not impaired (including an ageing analysis); and those past due and impaired at the balance sheet date.

		Past due but not impaired				Past due and impaired	Total
	Not past due/not impaired	0-1 months	1-3 months	3-6 months	Greater than 6 months		
	\$M	\$M	\$M	\$M	\$M	\$M	\$M
As at 30 June 2011							
Receivables	108.5	1.0	2.0	1.7	5.1	–	118.3
Receivables SPV	6,293.9	345.4	185.5	26.7	–	38.3	6,889.8
Total receivables	6,402.4	346.4	187.5	28.4	5.1	38.3	7,008.1

As at 30 June 2010

Receivables	97.5	0.7	5.8	5.6	3.4	–	113.0
Receivables – SPV	7,587.2	484.1	200.7	155.1	–	39.7	8,466.8
Total receivables	7,684.7	484.8	206.5	160.7	3.4	39.7	8,579.8

27. Financial risk management (continued)

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 balance. At all times of possession, the risks and rewards associated with ownership of the property are held by the Trustee on behalf of the RMBS holder.

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 balance sheet date.

Subordinated debt

CLC has subordinated debt liabilities with nominal value of A\$400 million and US\$150 million that are required to be classified as financial liabilities through profit and loss. The change recognised in the income statement in respect of valuation changes (excluding foreign exchange) for the year ended 30 June 2011 was a loss of \$39.7 million (2010: loss \$56.2 million). The liability is valued with regard to a basket of similar instruments.

Liquidity risk

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

The Group aims to ensure that it has sufficient liquidity to meet its obligations on a short-term and medium-term basis. In setting the level of sufficient liquidity, the Group considers new business activities in addition to current contracted obligations. It considers: minimum cash requirements; collateral and margin call buffers; Australian Financial Services (AFS) Licence requirements; cash flow forecasts; associated reporting requirements; other liquidity risks; and contingency plans.

The basis of the approach to liquidity management is on targeting sufficient liquidity to meet the regulatory guidelines set out in ASIC Policy Statement 166 for holders of an AFS Licence. AFS Licence holders make a reasonable estimate of cash flows over at least the next three months to demonstrate whether surplus capital will exceed either:

- 20% of the greater of cash outflows for the forecast three month average (equivalent to 18 days' outgoings); or
- cash outflow for the most recent financial year, adjusted to produce a three month average.

CLC aims to ensure that it has sufficient liquidity to meet its obligations on a short-term, medium-term and long-term basis. The Life 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 CLC Asset Liability Committee. At the reporting date, all requirements of the CLC Board approved liquidity management policy were satisfied.

Maturity profile of undiscounted liabilities

The table opposite 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 balance sheet by the amount of discounting recognised in the balance sheet values.

	1 year or less \$M	1-3 years \$M	3-5 years \$M	> 5 years \$M	Total \$M
30 June 2011					
Payables	305.2	48.8	–	–	354.0
Interest bearing liabilities	527.6	321.3	194.6	1,435.5	2,479.0
Interest bearing liabilities – SPV	128.9	–	–	8,850.9	8,979.8
External unit holders' liabilities	490.0	826.7	–	–	1,316.7
Life investment contract liabilities	1,384.6	2,515.5	1,027.8	1,413.2	6,341.1
Derivative financial liabilities	368.9	22.1	35.4	(107.1) ¹	319.3
Total financial liabilities¹	3,205.2	3,734.4	1,257.8	11,592.5	19,789.9
	1 year or less \$M	1-3 years \$M	3-5 years \$M	> 5 years \$M	Total \$M
30 June 2010					
Payables	200.9	116.3	–	–	317.2
Interest bearing liabilities	200.4	679.5	126.8	1,529.6	2,536.3
Interest bearing liabilities – SPV	117.6	–	–	11,388.0	11,505.6
External unit holders' liabilities	131.5	1,127.5	–	–	1,259.0
Life investment contract liabilities	967.4	1,492.3	896.5	1,579.1	4,935.3
Derivative financial liabilities	59.9	7.7	1.0	18.5	87.1
Total financial liabilities¹	1,677.7	3,423.3	1,024.3	14,515.2	20,640.5

¹ The Group is due to receive future cash inflows from interest rate swaps currently in a fair value liability position.

Fair value determination and classification

Fair value reflects the amount for which an asset could be exchanged or a liability settled, between knowledgeable, willing parties in an arm's length transaction. The majority of the Group's financial instruments are held in the life insurance statutory funds of CLC and, as a result, are required by Australian accounting standards to be designated at fair value through profit and loss wherever possible.

All other financial instruments in the Group, with the exception of the SPV balances carried at amortised cost listed below, are either designated at fair value through profit and loss at initial recognition, or the carrying value materially approximates fair value.

	30 June 2011		30 June 2010	
Difference between amortised cost and fair value	Carrying value \$M	Fair value \$M	Carrying value \$M	Fair value \$M
Receivables – SPV	6,889.8	7,000.6	8,466.8	8,696.2
Interest bearing liabilities – SPV	6,968.7	6,716.9	8,637.0	8,435.3

The fair value of investments that are actively traded in organised financial markets are determined by reference to quoted market bid prices at the close of business on each reporting date. Where no such market exists, valuation models that utilise both internal and external inputs are used to determine fair value. Financial instruments are split into the following categories depending on the level of observable inputs into the models used to determine fair value:

Level 1 unadjusted quoted prices in active markets.

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

Level 3 there are inputs for the asset or liability valuation 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 of cash flows, discount rates, earnings multiples and internal credit ratings.

Where different levels of the hierarchy are used in a valuation, the instrument is classified according to the lowest level that is significant to the input. The table on page 108 summarises those financial instruments for which a fair value has been determined and the level of observable inputs into the valuation methodology.

27. Financial risk management (continued)

	Level 1 \$M	Level 2 \$M	Level 3 \$M	Total \$M
30 June 2011				
Derivative assets	–	360.2	–	360.2
Debt securities	129.2	3,637.4	1,123.5	4,890.1
Equity securities	51.2	19.2	222.7	293.1
Infrastructure investments	145.1	0.2	510.8	656.1
Property securities	–	–	173.4	173.4
Available-for-sale assets	9.5	–	–	9.5
Fair value financial assets	335.0	4,017.0	2,030.4	6,382.4
Derivative liabilities	–	114.8	–	114.8
Interest bearing liabilities	–	157.8	477.8	635.6
External unit holders' liabilities	–	1,316.7	–	1,316.7
Investment contract liabilities	–	110.3	4,887.9	4,998.2
Fair value financial liabilities	–	1,699.6	5,365.7	7,065.3
30 June 2010				
Derivative assets	–	287.1	–	287.1
Debt securities	–	2,930.8	1,136.2	4,067.0
Equity securities	169.6	8.9	160.6	339.1
Infrastructure investments	177.7	0.3	311.6	489.6
Property securities	9.4	–	145.1	154.5
Available-for-sale assets	11.8	–	–	11.8
Fair value financial assets	368.5	3,227.1	1,753.5	5,349.1
Derivative liabilities	–	223.2	–	223.2
Interest bearing liabilities	–	165.3	475.1	640.4
External unit holders' liabilities	–	1,259.0	–	1,259.0
Investment contract liabilities	–	117.1	3,979.0	4,096.1
Fair value financial liabilities	–	1,764.6	4,454.1	6,218.7

The Group derivative financial instruments are 'over the counter' so, whilst they are not exchange traded, there is a market observable price. All of the listed debt and government/semi-government securities have prices determined by a market but are not actively traded. Externally rated unlisted debt is valued by applying market observable credit spreads on similar assets with an equivalent credit rating. Both are therefore Level 2. Internally rated debt is Level 3 as the determination of an equivalent credit rating is a significant non-observable input.

Unlisted equity, infrastructure and property securities are valued using either cash flow forecasts discounted using the applicable yield curve, earning-multiple valuations or, for managed funds, the net assets of the trust per the most recent financial report.

The interest bearing liabilities classified as Level 3 are the subordinated debt notes issued by CLC. These are valued using a benchmark credit spread based on a pool of similar assets and, as a result, are Level 3. External unit holder liabilities are valued at the face value of the amounts payable. 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 unmodified account balance, rather than a discounted cash flow as applied to the rest of the portfolio.

Level 3 reconciliation

The following table shows a reconciliation of the movement in the fair value of financial instruments categorised within Level 3 over the year.

	30 June 2011		30 June 2010	
	Assets \$M	Liabilities \$M	Assets \$M	Liabilities \$M
Opening balance	1,753.5	4,454.1	1,571.5	4,278.6
Total gains and losses	(132.0)	202.5	30.1	321.2
Additions	825.4	1,816.5	500.9	872.2
Disposals	(465.2)	(1,107.4)	(349.0)	(1,017.9)
Transfers from Level 1 or 2	48.7	–	–	–
Closing Level 3 balance	2,030.4	5,365.7	1,753.5	4,454.1
Total (losses)/gains included in the income statement for the year for assets and liabilities still held at the balance sheet date	(105.3)	(202.5)	14.4	(283.3)

Level 3 sensitivity

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

	Level 3 value \$M	Positive impact \$M	Negative impact \$M	Reasonable change in non-observable input
30 June 2011				
Debt securities	1,123.5	53.3	(29.7)	Primarily credit spreads
Interest bearing liabilities	(477.8)	(23.9)	21.5	Primarily credit spreads
Net debt	645.7	29.4	(8.2)	
Equity, infrastructure, property assets	906.9	30.0	(29.6)	Primarily discount rate on cash flow models
Investment contract liabilities	(4,887.9)	5.8	(1.2)	Primarily expense assumptions
Total Level 3	(3,335.3)	65.2	(39.0)	
	Level 3 value \$M	Positive impact \$M	Negative impact \$M	Reasonable change in non-observable input
30 June 2010				
Debt securities	1,136.2	32.2	(27.9)	Primarily credit spreads
Interest bearing liabilities	(475.1)	(23.8)	23.8	Primarily credit spreads
Net debt	661.1	8.4	(4.1)	
Equity, infrastructure, property assets	617.3	28.8	(28.6)	Primarily discount rate on cash flow models
Investment contract liabilities	(3,979.0)	6.2	(13.7)	Primarily expense assumptions
Total Level 3	(2,700.6)	43.4	(46.4)	

28. Derivative financial instruments

The table below shows the notional value, fair value and duration of the Group's derivative financial instruments:

	30 June 2011			30 June 2010		
	Notional/ Principal value \$M	Net fair value assets \$M	Net fair value liabilities \$M	Notional/ Principal value \$M	Net fair value assets \$M	Net fair liabilities liabilities \$M
Interest rate swaps						
Less than 1 year	2,421.2	2.0	(3.4)	440.6	1.8	(2.1)
1-3 years	1,789.9	19.1	(1.1)	1,326.2	19.8	(11.6)
3-5 years	876.6	34.4	(2.9)	715.6	35.8	(5.8)
Greater than 5 years	2,188.0	78.3	(49.8)	1,988.2	108.5	(37.7)
	7,275.7	133.8	(57.2)	4,470.6	165.9	(57.2)
Interest rate swaps – SPV						
Less than 1 year	115.3	0.1	(0.9)	263.9	–	(1.8)
1-3 years	246.4	0.3	(2.7)	279.4	–	(6.6)
3-5 years	3.4	–	(0.1)	47.6	0.4	–
Greater than 5 years	0.9	–	(0.1)	1.1	–	(0.1)
	366.0	0.4	(3.8)	592.0	0.4	(8.5)
Inflation-linked swaps						
Less than 1 year	570.0	4.7	(2.3)	–	–	–
1-3 years	1,200.0	13.7	(6.9)	590.0	5.3	(2.8)
	1,770.0	18.4	(9.2)	590.0	5.3	(2.8)
Futures contracts						
Less than 1 year	1,020.2	0.2	(0.1)	511.3	–	(4.6)
Forward currency contracts						
Less than 1 year	3,534.2	42.0	(19.1)	1,642.2	45.5	(99.2)
1-3 years	188.8	16.0	(6.6)	109.7	3.4	(3.2)
3-5 years	86.2	4.0	(2.0)	132.5	6.6	(10.0)
	3,809.2	62.0	(27.7)	1,884.4	55.5	(112.4)
Cross currency swaps						
Less than 1 year	286.5	33.0	(5.3)	201.0	11.1	(9.9)
1-3 years	573.6	54.4	(2.8)	491.9	23.8	(14.6)
3-5 years	445.8	47.3	(2.8)	333.3	23.0	(13.2)
Greater than 5 years	147.4	9.4	(2.6)	9.3	0.9	–
	1,453.3	144.1	(13.5)	1,035.5	58.8	(37.7)
Cross currency swaps – SPV						
Greater than 5 years	3,193.9	1.3	(3.3)	5,014.8	1.2	–
Total derivative financial instruments		360.2	(114.8)		287.1	(223.2)

Derivatives designated as hedges of net investment in foreign currency operations

As described in Note 1(xvi) 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 2011, a post-tax gain of \$23.8 million (2010: loss \$16.8 million) was recognised in equity for the hedging of exposure to the net investment in foreign operations arising.

Derivatives designated as cash flow hedges

As described in Note 1(xvi), 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 known outcome of a future transaction. As described in Note 27, SPV purchase interest rate swaps to hedge the interest rate risk between variable rate loans, which generally reprice with changes in official interest rates, and issued residual mortgage backed securities (RMBS) that reprice with changes in the 30 day and 90 day BBSW. Cross currency swaps are also purchased to hedge currency movements on foreign denominated RMBS. The SPV applies hedge accounting to both types of transaction, with the fair value change on the effective portion of the derivative being recognised in equity.

At 30 June 2011 a post-tax gain of \$1.5 million (2010: loss \$6.8 million) was recognised in equity for cash flow hedges with no income statement impact of any ineffective portions during either the current or prior period.

29. Commitments

Operating leases

Group as lessee

The Group has entered into commercial operating leases for the rental of properties where it is not in the best interests of the Group to purchase these properties. These leases have an average life of between one and 10 years with renewal terms included in the contracts. Renewals are at the specific option of the entity that holds the lease.

Surplus lease space under non-cancellable operating leases has been subleased with the revenue arising from the sublease being recognised on a straight-line basis. The leases have a remaining life of up to six years with renewal terms included in the contract. Renewals are at the specific option of the entity that holds the lease. A surplus lease provision has been created representing the Group's net rental expense obligation and, as such, does not form part of the commitment listed below. Refer to Note 20 for details.

Group as lessor

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

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.

Remuneration commitments

These represent commitments arising from employment contracts with key management personnel (retention bonuses, termination payments, interest etc.) referred to in the Remuneration Report but that have not been recognised as liabilities at the balance date.

	30 June 2011 \$M	30 June 2010 \$M
Commitments		
Non-cancellable operating leases – Group as lessee	69.1	87.3
Capital expenditure	81.5	46.4
Remuneration	0.5	4.5
Non-cancellable operating leases – Group as lessor	(1,642.5)	(1,899.4)
Operating leases – Group as lessee		
Amount due in less than 1 year	17.4	17.9
Amount due later than 1 year but not later than 2 years	14.4	17.6
Amount due later than 2 years but not later than 5 years	33.3	40.4
Amount due in more than 5 years	4.0	11.4
	69.1	87.3
Capital expenditure commitments		
Amount due in less than 1 year	48.5	18.0
Amount due later than 1 year but not later than 5 years	22.0	18.7
Amount due in more than 5 years	11.0	9.7
	81.5	46.4
Remuneration commitments		
Amount due in less than 1 year	0.5	4.0
Amount due later than 1 year but not later than 5 years	–	0.5
	0.5	4.5
Operating leases – Group as lessor		
Amount due in less than 1 year	(196.0)	(193.9)
Amount due later than 1 year but not later than 2 years	(175.5)	(190.9)
Amount due later than 2 years but not later than 5 years	(471.4)	(511.0)
Amount due in more than 5 years	(799.6)	(1,003.6)
	(1,642.5)	(1,899.4)

30. Related parties

Controlled entities

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.

Other related parties

During the year, there were transactions between the Group and Challenger specialised funds (Challenger Infrastructure Fund and Belvino Wine Trust (formerly Challenger Wine Trust)) for the provision of investment management, transaction advisory and other professional services. Transactions were also entered into between the Group and associated entities (refer to Note 36) for the provision of distribution and administration services.

The Group earned fee income during the year of \$17.1 million (2010: \$23.7 million) from transactions entered into with non-controlled funds and associates. Transactions are conducted on an arm's length basis under normal commercial terms and conditions.

Directors and Key Executives

The Directors and Key Executives of Challenger Limited at any time during the financial year were as follows:

Directors

Peter Polson, Chairman
 Graham Cubbin
 Jonathan Grunzweig (appointed 6 October 2010)
 Russell Hooper
 Brenda Shanahan (appointed 1 April 2011)
 Leon Zwier
 Thomas Barrack Jr. (resigned 6 October 2010).

Executive Director

Dominic Stevens, Chief Executive Officer and Managing Director.

Key Executives

Brian Benari, Group Chief Financial Officer/Group Chief Operating Officer
 Richard Howes, Chief Executive, Life
 Paul Rogan, Chief Executive, Distribution, Product & Marketing
 Robert Woods, Chief Executive, Funds Management
 Rob Adams, former Joint Chief Executive, Funds Management (ceased to be a key executive on 25 February 2011).

Loans to Directors and Key Executives

There were no loans made to Directors and specified Key Executives as at 30 June 2011 (2010: nil).

Director and Key Executive compensation for the year ended 30 June 2011

	Year	Short-term employee benefits \$	Post employment \$	Share based payments \$	Other long-term benefits \$	Total \$
Directors	2011	924,128	3,764	–	–	927,892
	2010	801,999	13,256	–	–	815,255
Executive Director	2011	2,042,606	15,199	2,784,683	1,016,904	5,859,392
	2010	2,090,795	14,461	2,906,881	1,615,143	6,627,280
Key Executives	2011	6,340,360	75,995	10,733,563	2,805,689	19,955,607
	2010	6,574,430	77,125	15,122,575	5,497,795	27,271,925
Total	2011	9,307,094	94,958	13,518,246	3,822,593	26,742,891
	2010	9,467,224	104,842	18,029,456	7,112,938	34,714,460

Split of statutory compensation components for the CEO and Key Executives:

Executive	Year	Fixed	Cash STI	Share based payments	Other	Total
Dominic Stevens	2011	17%	18%	48%	17%	100%
	2010	15%	17%	44%	24%	100%
Brian Benari	2011	12%	16%	59%	13%	100%
	2010	9%	13%	52%	26%	100%
Richard Howes	2011	14%	16%	56%	14%	100%
	2010	11%	13%	53%	23%	100%
Paul Rogan	2011	20%	17%	48%	15%	100%
	2010	17%	11%	58%	14%	100%
Robert Woods	2011	14%	15%	57%	14%	100%
	2010	12%	12%	55%	21%	100%

Director and Key Executive shareholdings in Challenger Limited

Details of the Directors' and Key Executives' and their affiliates' shareholdings in Challenger Limited as at 30 June 2011 are set out below. All shareholdings were acquired at arm's length prices.

2011 Number of shares	Held at 30 June 2010	Acquired on vesting of long term incentive awards	Other changes	Held at 30 June 2011
Directors				
P Polson	112,000	–	–	112,000
G Cubbin	177,702	–	–	177,702
J Grunzweig ¹	–	–	250	250
R Hooper	160,000	–	–	160,000
B Shanahan ¹	–	–	250,000	250,000
L Zwier	2,360	–	–	2,360
Executive Director				
D Stevens	2,649,087	1,960,278	(3,741,810)	867,555
Key Executives				
R Adams ²	529,947	1,806,276	(2,336,223)	–
B Benari	3,000,000	3,473,575	(4,307,269)	2,166,306
R Howes	3,500,000	3,223,291	(4,785,569)	1,937,722
P Rogan	3,720,000	1,209,509	(1,539,303)	3,390,206
R Woods	3,100,000	3,235,270	(4,297,548)	2,037,722
Total	16,951,096	14,908,199	(20,757,472)	11,101,823

¹ J Grunzweig and B Shanahan were appointed as Directors during the year. Any prior holdings are included in the 'Other changes' column.

² R Adams ceased to be a Key Executive during the period. Previously held shares are reported in 'Other changes'.

30. Related parties (continued)**Director and Key Executive shareholdings in Challenger Limited (continued)**

2010 Number of shares	Held at 30 June 2009	Acquired on vesting of long term incentive awards	Other changes	Held at 30 June 2010
Directors				
P Polson	99,500	–	12,500	112,000
T Barrack Jr.	–	–	–	–
G Cubbin	177,702	–	–	177,702
R Hooper	160,000	–	–	160,000
L Zwier	–	–	2,360	2,360
A Jacob ¹	20,000	–	(20,000)	–
J Packer ^{1, 2}	122,788,278	–	(122,788,278)	–
T Wada ¹	–	–	–	–
Executive Director				
D Stevens	7,782,655	666,432	(5,800,000)	2,649,087
Key Executives				
R Adams	2,029,947	483,155	(1,983,155)	529,947
B Benari	5,231,562	1,156,848	(3,388,410)	3,000,000
R Howes	4,101,821	1,057,011	(1,658,832)	3,500,000
P Rogan	3,553,541	639,957	(473,498)	3,720,000
R Woods	5,013,800	1,068,990	(2,982,790)	3,100,000
D Hall ³	565,989	1,412,771	(1,978,760)	–
Total	151,524,795	6,485,164	(141,058,863)	16,951,096

¹ T Wada, A Jacob and J Packer resigned as Directors during the year ended 30 June 2010.

² J Packer sold his shares in the Company prior to resigning as a Director.

³ D Hall ceased to be a Key Executive during the prior period. Shares held upon exit are therefore removed in 'Other changes.'

Director and Key Executive performance share rights

Details of Directors' and Key Executives' and their affiliates' performance share rights in the Company as at 30 June 2011 are set out below.

2011 Number of performance share rights	Held at 1 July 2010	Granted as remuneration	Vested	Held at 30 June 2011
Executive Director				
D Stevens	918,187	295,381	(660,278)	553,290
Key Executives				
R Adams ¹	212,110	171,420	(383,530)	–
B Benari	822,635	248,388	(607,711)	463,312
R Howes	421,904	201,396	(357,427)	265,873
P Rogan	320,880	114,124	(234,910)	200,094
R Woods	433,883	174,543	(369,406)	239,020
Total	3,129,599	1,205,252	(2,613,262)	1,721,589

¹ R Adams ceased to be a Key Executive during the period.

Performance share rights are exercised on vesting and shares are transferred out of the plan to the individual. Vested shares are transferred into the name of the Key Executive but remain subject to trading restrictions.

Terms and conditions of performance share rights allocations for the year ended 30 June 2011

2011 Performance share rights	Granted number	Grant date	Allocation price \$	Fair value at grant \$	Start vesting date	Last vesting date
Executive Director						
D Stevens	147,690	15/9/2010	3.724	3.79	15/9/2010	15/9/2011
	147,691	15/9/2010	3.724	3.65	15/9/2010	15/9/2012
Key Executives						
R Adams	57,062	15/9/2010	3.724	3.79	15/9/2010	15/9/2011
	57,062	15/9/2010	3.724	3.65	15/9/2010	15/9/2012
	28,648	24/2/2011	4.929	4.93	24/2/2011	15/9/2012
	28,648	24/2/2011	4.929	4.93	24/2/2011	15/9/2013
B Benari	124,194	15/9/2010	3.724	3.79	15/9/2010	15/9/2011
	124,194	15/9/2010	3.724	3.65	15/9/2010	15/9/2012
R Howes	100,698	15/9/2010	3.724	3.79	15/9/2010	15/9/2011
	100,698	15/9/2010	3.724	3.65	15/9/2010	15/9/2012
P Rogan	57,062	15/9/2010	3.724	3.79	15/9/2010	15/9/2011
	57,062	15/9/2010	3.724	3.65	15/9/2010	15/9/2012
R Woods	87,271	15/9/2010	3.724	3.79	15/9/2010	15/9/2011
	87,272	15/9/2010	3.724	3.65	15/9/2010	15/9/2012

Director and Key Executive hurdled performance share rights

Details of Directors' and Key Executives' and their affiliates' hurdled performance share rights for shares in the Company as at 30 June 2011 are set out below.

2011 Number of hurdled performance share rights	Held at 1 July 2010	Granted as remuneration	Vested	Other changes	Held at 30 June 2011
Executive Director					
D Stevens	–	750,000	–	–	750,000
Key Executive					
R Adams ¹	–	200,000	(48,147)	(151,853)	–
B Benari	–	350,000	–	–	350,000
R Howes	–	350,000	–	–	350,000
P Rogan	–	200,000	–	–	200,000
R Woods	–	350,000	–	–	350,000
Total	–	2,200,000	(48,147)	(151,853)	2,000,000

¹ R Adams ceased to be a Key Executive during the period. Forfeited hurdled performance share rights are included in the 'Other changes' column.

Terms and conditions of hurdled performance share rights allocations for the year ended 30 June 2011

2011 Performance share rights	Granted number	Grant date	Reference price \$	Fair value at grant \$	Start vesting date	Last vesting date
Executive Director						
D Stevens	750,000	8/9/2010	3.724	2.02	15/9/2012	15/9/2014
Key Executives						
R Adams	200,000	8/9/2010	3.724	2.02	15/9/2012	15/9/2014
B Benari	350,000	8/9/2010	3.724	2.02	15/9/2012	15/9/2014
R Howes	350,000	8/9/2010	3.724	2.02	15/9/2012	15/9/2014
P Rogan	200,000	8/9/2010	3.724	2.02	15/9/2012	15/9/2014
R Woods	350,000	8/9/2010	3.724	2.02	15/9/2012	15/9/2014

Hurdled performance share rights above vest in three tranches. For further details of this scheme see Note 31.

30. Related parties (continued)

Director and Key Executive options

Details of Directors' and Key Executives' and their affiliates' options over shares in the Company as at 30 June 2011 are set out below.

2011 Number of options	Held at 1 July 2010	Granted as remuneration	Exercised	Other changes	Held at 30 June 2011
Executive Director					
D Stevens	7,100,000	–	(1,300,000)	–	5,800,000
Key Executives					
R Adams ¹	2,000,000	–	(1,133,334)	(866,666)	–
B Benari	4,350,000	–	(2,383,334)	–	1,966,666
R Howes	4,350,000	–	(2,383,334)	–	1,966,666
P Rogan	1,700,000	–	(733,334)	–	966,666
R Woods	4,350,000	–	(2,383,334)	–	1,966,666
Total	23,850,000	–	(10,316,670)	(866,666)	12,666,664

¹ R Adams ceased to be a Key Executive during the period. Previously held options are reported in the 'Other changes' column.

Terms and conditions of option allocations for the year ended 30 June 2011

There were no option allocations during the year.

Director and Key Executive capped performance rights

Details of Directors' and Key Executives' and their affiliates' capped performance rights for shares in the Company as at 30 June 2011 are set out below.

2011 Number of capped performance rights	Held at 1 July 2010	Vested	Other remuneration	Held at 30 June 2011
Key Executives				
R Adams ¹	285,714	(241,265)	(44,449)	–
B Benari	571,428	(482,530)	(88,898)	–
R Howes	571,428	(482,530)	(88,898)	–
P Rogan	285,714	(241,265)	(44,449)	–
R Woods	571,428	(482,530)	(88,898)	–
Total	2,285,712	(1,930,120)	(355,592)	–

¹ R Adams ceased to be a Key Executive during the period.

Terms and conditions of capped performance rights allocations for the year ended 30 June 2011

There were no allocations of capped performance rights during the year.

Director and Key Executive participation in deferred loan scheme

Details of Directors' and Key Executives' and their affiliates' participation in the deferred loan scheme for shares in the Company as at 30 June 2011 are set out below.

2011 Shares held under deferred loan scheme	Held at 1 July 2010	Other changes	Held at 30 June 2011
Key Executives			
P Rogan	2,000,000	–	2,000,000
Total	2,000,000	–	2,000,000

Terms and conditions of deferred loan allocations for the year ended 30 June 2011

There were no allocations during the year.

31. Employee entitlements

	30 June 2011 \$M	30 June 2010 \$M
Employee entitlements provision (see Note 20)	6.9	8.2

The total number of employees of the Group at balance date totalled 455 (30 June 2010: 460).

Challenger Performance Plan

The Challenger Performance Plan (CPP) is a flexible plan that provides for the award of either options or performance rights with awards being satisfied from either the issue of new shares or on-market acquisition. Non-Executive Directors are not eligible to participate in the plan. The key features of the plan are as follows:

Performance share rights (PSR)

This instrument is a performance right which converts into a fully paid share in the Company at the end of the vesting period. The core purpose of PSR is to reward individuals for performance over the past 12 months.

The vesting period is typically two years. Performance rights are converted to ordinary fully paid shares upon vesting.

Hurdled performance share rights

Hurdled PSR were issued by the CPP during the year ended 30 June 2011 as a replacement for options. This instrument is a performance right which converts into a fully paid share in the Company at the end of a vesting period, subject to the achievement of performance conditions based on shareholder returns. The Hurdled PSR are awarded based on a range of criteria reflecting, in addition to current year performance, the longer term ability for an employee to add significant value to Challenger and for retention purposes. The award of Hurdled PSR ensures longer term alignment of interest between Challenger and employees.

The vesting period is typically over four years with three vesting parcels at the end of years 2, 3 and 4. Hurdled performance rights are converted to ordinary fully paid shares upon vesting.

Options

No new options were issued in the year ended 30 June 2011.

Capped performance rights

All capped rights converted into fully paid shares in the Company on 15 September 2010. No new capped performance rights were issued in the year ended 30 June 2011.

Performance share rights

The following table sets out the details of the performance share rights granted under the Challenger Performance Plan (CPP) during 2011 and movements on previous issues:

Grant date	Latest date for exercise ¹	Reference price \$	Fair value at grant \$	Out-standing at 1 July 2010	Granted during the year	Vested during the year	Expired during the year	Total out-standing at 30 June 2011 ¹
14 Sep 07	15 Sep 10	5.57	5.24	743,907	–	(741,059)	(2,848)	–
14 Sep 07	15 Sep 10	5.57	5.24	685,169	–	(676,185)	(8,984)	–
15 Sep 08	15 Sep 10	2.82	2.39	1,985,120	–	(1,969,158)	(15,962)	–
23 Oct 09	15 Sep 10	2.33	3.68	1,187,775	–	(1,183,678)	(4,097)	–
23 Oct 09	15 Sep 11	2.33	3.56	1,195,472	–	(77,372)	(12,451)	1,105,649
15 Sep 10	15 Sep 11	3.72	3.79	–	1,261,980	(75,352)	(13,541)	1,173,087
15 Sep 10	15 Sep 12	3.72	3.65	–	1,261,980	(75,355)	(13,545)	1,173,080
24 Feb 11	15 Sep 13	4.93	4.93	–	57,296	(57,296)	–	–
				5,797,443	2,581,256	(4,855,455)	(71,428)	3,451,816

¹ At the date of vesting, performance share rights are transferred to the individual and released from the CPP Trust.

31. Employee entitlements (continued)

Hurdled performance share rights

The following table sets out details of the hurdled performance share rights granted under the Challenger Performance Plan during 2011.

Grant date	Latest date for vesting ¹	Reference price \$	Fair value at grant \$	Out-standing at 1 July 2010	Granted during the year	Vested during the year	Expired during the year	Out-standing at 30 June 2011
08 Sep 10	15 Sep 14	3.724	2.02	–	5,799,000	(66,005)	(307,495)	5,425,500
14 Dec 10	1 Dec 14	4.166	2.38	–	216,450	–	–	216,450
				–	6,015,450	(66,005)	(307,495)	5,641,950

¹ At the date of vesting, hurdled performance share rights are transferred to the individual and released from the CPP Trust.

Options

The following table sets out the details of the share options movement under the Challenger Performance Plan during 2011. No new grants were made during the year.

Grant date	Latest date for exercise	Exercise price \$	Fair value at grant \$	Out-standing at 1 July 2010	Granted during the year	Exercised during the year	Expired during the year	Out-standing at 30 June 2011
27 Feb 07	01 Feb 11	4.00	1.29 ¹	6,050,000	–	(5,550,000)	(500,000)	–
14 Sep 07	14 Sep 11	5.57	1.28 ²	2,575,000	–	–	(200,000)	2,375,000
28 Sep 07	28 Sep 10	5.57	1.30 ²	666,666	–	–	(333,333)	333,333
28 Sep 07	28 Sep 11	5.57	1.56 ²	666,668	–	–	–	666,668
30 Jun 08	30 Aug 10	2.20	0.27	2,100,000	–	(2,100,000)	–	–
30 Jun 08	30 Aug 11	2.20	0.32	2,100,000	–	–	(200,000)	1,900,000
22 Dec 08	22 Dec 10	1.34	0.52	3,517,000	–	(3,517,000)	–	–
22 Dec 08	22 Dec 11	1.34	0.57	3,504,991	–	–	(289,991)	3,215,000
09 Mar 09	22 Dec 10	1.13	0.22	66,667	–	(66,667)	–	–
09 Mar 09	22 Dec 11	1.13	0.22	66,666	–	–	–	66,666
30 Jun 09	30 Aug 10	2.29	0.56	116,667	–	(116,667)	–	–
30 Jun 09	30 Aug 11	2.29	0.65	116,667	–	–	(66,667)	50,000
30 Jun 09	30 Aug 12	2.29	0.68	116,666	–	–	(66,666)	50,000
23 Oct 09	30 Sep 10	2.33	1.56	4,855,019	–	(4,821,685)	(33,334)	–
23 Oct 09	30 Sep 11	2.33	1.62	4,854,995	–	–	(390,002)	4,464,993
23 Oct 09	30 Sep 12	2.33	1.58	4,854,995	–	–	(390,006)	4,464,989
CEO options								
27 Nov 08	29 Feb 12	2.36	0.24	5,500,000	–	–	–	5,500,000
Total				41,728,667	–	(16,172,019)	(2,469,999)	23,086,649

¹ The valuation method changed back to the original EPS from TSR due to vesting.

² In 2010 the valuation method changed from EPS to TSR.

Capped performance rights

The following table sets out the details of the capped performance rights movements under the Challenger Performance Plan during 2011. No new grants were made during the year.

Grant date	Latest date for vesting	Vesting price \$	Fair value at grant \$	Out-standing at 1 July 2010	Granted during the year	Exercised during the year	Expired during the year	Out-standing at 30 June 2011
22 Dec 08	15 Sep 10	1.50-3.50	0.532	3,857,137	–	(3,257,073)	(600,064)	–

All performance share rights granted during the year have been externally valued. The options are valued by a Monte Carlo simulation model using the TSR share price hurdles, or a binomial option pricing model for those options with an EPS hurdle. A Black Scholes model is used to value the performance rights. Key inputs into the valuation models are as follows:

Input	15-Sep-10 Rights ¹	24-Feb-11 Rights ³	8-Sep-10 Hurdled rights	14-Dec-10 Hurdled rights
Dividend yield (%)	3.6	n/a	3.6	3.4
Risk free rate (%)	4.42 – 4.44	n/a	4.56	5.26
Volatility (%) ²	38	n/a	38	33
Valuation (\$)	3.65 – 3.79	4.93	2.02	2.38

¹ Staggered vesting applies to this grant.

² Forecast volatility rate implied from historic trend.

³ Rights vested on 25 February so valuation is equal to reference price.

Long Term Equity Based Incentive Plan

The Long Term Incentive Plan (LTIP) was a share scheme provided by way of a limited recourse loan. LTIP was suspended in 2006 with the final award being made on 15 September 2006. The last tranche of this scheme reaches maturity in September 2011.

Details of the movement and fair value of employee shares remaining under the LTIP are detailed in the following table:

Grant date	Out- standing at 1 July 2010	Issue price \$	Fair value at grant \$	Vested	Forfeited	Out- standing at 30 June 2011
15-Sep-05	3,080,000	3.77	0.51	–	(3,080,000)	–
15-Mar-06	2,950,000	3.67	0.50	–	(2,950,000)	–
15-Sep-06	1,500,000	3.55	0.54	–	(600,000)	900,000
Total	7,530,000			–	(6,630,000)	900,000

Deferred Loan Plan

A small number of employees had outstanding future commitments under the LTIP at the time it was suspended. In lieu of a number of those commitments, an arrangement was entered into with Deutsche Bank AG to provide the individual with a loan over a similar number of shares as their prior LTIP commitment. The Group is responsible for meeting the interest payable on the loan over its term, net of any dividends paid on the shares. The loans are limited in their recourse to the Group and the Challenger Performance Plan Trust has the option of taking ownership of the shares and using them to satisfy other share awards in the event of forfeiture by the executive. The last of these plans matures in September 2011.

Other short-term employee benefits

Challenger pays interest on loans taken out by certain Key Executives to acquire Challenger shares on market. The loans are fully secured against the underlying shares and are not margin loans. Challenger has no exposure in relation to the loan principal advanced to the Key Executives by the third party for the purposes of acquiring the shares. In the Board's view, this arrangement, when considered with the Key Executive's other long term incentive arrangements, provides significant alignment with shareholders' interests. The last of these plans matures in September 2011.

32. Reconciliation of profit to operating cash flow

	30 June 2011 \$M	30 June 2010 \$M
Profit for the year	292.5	293.8
Non-cash and investing adjustments:		
Net realised gain on disposal of financial assets	(183.7)	(278.2)
Net unrealised loss/(gain) on revaluation of financial assets	100.2	37.9
Profit on disposal of controlled entities	–	12.1
Share of associates' net profit	(7.9)	(3.7)
Amortisation and depreciation	22.5	43.4
Share based payments	25.7	31.5
Operating cash flow not recognised in revenue		
Dividends from associates	4.0	1.8
Change in operating assets and liabilities, net of disposal/acquisition of controlled entities		
Decrease/(increase) in receivables	62.4	(251.6)
Decrease in other assets	25.6	12.9
Increase in payables	0.4	226.1
Decrease in provisions	(12.2)	(2.7)
Increase in life contract liabilities	883.2	172.0
Increase/(decrease) in net tax liabilities	7.2	(66.2)
Net cash inflow from operating income	1,219.9	229.1

33. Remuneration of auditor

	30 June 2011 \$'000	30 June 2010 \$'000
Amounts received or due and receivable by Ernst & Young for:		
Full year audit and half year review of the Group financial report	1,302.5	1,388.0
Other audit services – audit and review of trusts and funds	469.8	502.0
Other services in relation to the Group		
Taxation services	207.0	421.0
Due diligence services	–	246.0
Other assurance services	427.7	475.0
	2,407.0	3,032.0

Auditor's remuneration for the Group is paid by Challenger Group Services Limited, an entity within the Group.

34. Significant transactions

Deconsolidation of managed funds

The Group's holding in two unlisted managed funds fell below 50% in the period and, as a result, they have been deconsolidated as the Group is no longer considered to have control over their operations. The WaveStone Australian Equity Long/Short Fund (WaveStone) was deconsolidated as at 30 November 2010 and the Five Oceans World Fund (Five Oceans) was deconsolidated as at 31 December 2010.

Both of the changes were due to the dilutionary impact on the Group's holding arising from the funds issuing capital to external investors. For WaveStone, the controlling interest fell from 68.7% at 30 June 2010 to 41.2% at 30 November 2010. For Five Oceans, the controlling interest fell from 54.9% at 30 June 2010 to 37.2% at 31 December 2010. The net assets at the date of deconsolidation were \$160.8 million, consisting of \$166.5 million equity securities, \$1.8 million receivables, less \$7.5 million derivative liabilities. The net assets attributable to non-controlling interests at the date of deconsolidation totalled \$77.8 million.

Purchase of the Challenger High Yield Fund

On 25 February 2011, the Group acquired 100% of the units in the Challenger High Yield Fund (HYF). In return existing HYF unit holders received a combination of cash and units in a new fund called the Challenger Guaranteed Income Fund (the Fund). The Fund is a registered managed investment scheme that invests in an annuity issued by the Group. Consideration for the HYF units was \$556.2 million, comprising a 20% cash component and an 80% Fund unit component¹. In return the Group received \$556.2 million of net investment assets.

	Carrying amount \$M	Fair value \$M
Assets and liabilities acquired		
Cash and cash equivalents	59.5	59.5
Derivative assets	3.1	3.1
Other financial assets at fair value through profit and loss	493.6	493.6
Net assets	556.2	556.2

¹ Foreign unit holders received 100% cash under the scheme.

Purchase of Oaklands Hill Pty Limited

On 25 June 2011, the Group acquired a controlling interest in Oaklands Hill Pty Limited (Oaklands Hill). Oaklands Hill subsequently purchased an investment in Oaklands Hill Wind Farm Pty Limited (Oaklands Hill Wind) for a consideration of \$40 million. Oaklands Hill Wind is not a controlled entity and is recognised as an infrastructure investment. The following amounts in respect of Oaklands Hill have been recognised on the balance sheet at 30 June 2011 as a result of this transaction. No operating profit has been recorded for the period since acquisition.

	Carrying amount \$M	Fair value \$M
Assets and liabilities acquired		
Infrastructure asset	239.9	239.9
Interest bearing liability	(206.1)	(206.1)
Other receivable	2.6	2.6
Other payable	(36.4)	(36.4)
Net assets	—	—

35. Controlled entities

Name of entity	Country of incorporation	Class of shares/units	% owned 30 June 2011	% owned 30 June 2010
417 St. Kilda Road Melbourne Trust B	Australia	Ordinary	100	100
417 St. Kilda Road Holding Trust A	Australia	Ordinary	100	100
417 St. Kilda Road Trust	Australia	Ordinary	50	50
Allfine Holdings Pty Limited	Australia	Ordinary	100	100
Allfine Property Trust No. 1	Australia	Ordinary	100	100
Balloon Inflation Linked Bond Trust ¹	Australia	Ordinary	–	–
Belconnen Property Trust	Australia	Ordinary	100	100
Bluezen Property Trust No. 1	Australia	Ordinary	100	100
Bluezen Pty Limited	Australia	Ordinary	100	100
Cascade Pty Limited	Australia	Ordinary	100	100
CFSG Holdings No.2 Victoria Pty Limited	Australia	Ordinary	100	100
Challenger Alpha Prop Pty Ltd	Australia	Ordinary	100	100
Challenger Alpha Prop Holdings Pty Ltd	Australia	Ordinary	100	100
Challenger Australian Listed Property Holding Trust	Australia	Ordinary	100	100
Challenger Axminster Mortgages Trust	Australia	Ordinary	100	100
Challenger Boutique (GFI) Holdings Pty Limited	Australia	Ordinary	100	100
Challenger Boutique Alphinity Holdings Pty Limited	Australia	Ordinary	100	100
Challenger Boutique Ardea Holdings Pty Limited	Australia	Ordinary	100	100
Challenger Boutique Bentham Holdings Pty Ltd	Australia	Ordinary	100	100
Challenger Boutique Holdings Pty Ltd	Australia	Ordinary	100	100
Challenger Boutique Merlon Holdings Pty Ltd	Australia	Ordinary	100	100
Challenger Boutique Novaport Holdings Pty Limited	Australia	Ordinary	100	100
Challenger Boutique Wavestone Holdings Pty Limited	Australia	Ordinary	100	100
Challenger CKT Holding Trust	Australia	Ordinary	100	100
Challenger Commercial Lending Limited	Australia	Ordinary	100	100
Challenger Direct PTY Ltd	Australia	Ordinary	100	100
Challenger Diversified Properties Group	Australia	Ordinary	50	47
Challenger European Property Holding Trust	Australia	Ordinary	100	100
Challenger European Property Trust	Australia	Ordinary	100	100
Challenger Ferndale Trust	Australia	Ordinary	100	100
Challenger Financial Services Group	Australia	Ordinary	100	100
Challenger Financial Services Limited	Australia	Ordinary	100	100
Challenger FM 2 Holdings Pty Ltd				
(formerly Challenger Life Holdings Pty Limited)	Australia	Ordinary	100	100
Challenger FM Nominees Pty Limited	Australia	Ordinary	100	100
Challenger Funds Management Holdings Pty Limited	Australia	Ordinary	100	100
Challenger Gasvalpo Trust	Australia	Ordinary	100	100
Challenger German Property Trust	Australia	Ordinary	100	100
Challenger GIF Trust	Australia	Ordinary	100	100
Challenger Global Infrastructure Fund	Australia	Ordinary	100	100
Challenger Group Holdings Limited	Australia	Ordinary	100	100
Challenger Group Pty Limited	Australia	Ordinary	100	100
Challenger Group Services (UK) Limited	Australia	Ordinary	100	100
Challenger Group Services Pty Limited	Australia	Ordinary	100	100
Challenger Guernsey Trust	Australia	Ordinary	100	100
Challenger Holding Kft	Hungary	Ordinary	100	100
Challenger Home Loan Corporation Pty Limited	Australia	Ordinary	100	100
Challenger Howard Property Trust for 417 St. Kilda Road, Melbourne	Australia	Ordinary	100	100
Challenger Hungary International Capital Investment & Management Limited	Hungary	Ordinary	100	100
Challenger Infrastructure Unit Holding Trust	Australia	Ordinary	100	100
Challenger Infrastructure Unit Trust	Australia	Ordinary	100	100
Challenger Inventory Finance Servicing Pty Limited	Australia	Ordinary	100	100
Challenger Investment Services Limited	Australia	Ordinary	100	100
Challenger Jersey i3 Limited	Jersey	Ordinary	100	100

Name of entity	Country of incorporation	Class of shares/ units	% owned 30 June 2011	% owned 30 June 2010
Challenger Kenedix Japan Trust	Australia	Ordinary	100	100
Challenger Life Company Holdings Pty Limited	Australia	Ordinary	100	100
Challenger Life Company Limited	Australia	Ordinary	100	100
Challenger Life Nominees No. 2 Limited	Australia	Ordinary	100	100
Challenger Life Nominees No.3 Pty Limited	Australia	Ordinary	100	100
Challenger Life Nominees Pty Limited	Australia	Ordinary	100	100
Challenger Life Offshore Investments Limited	Australia	Ordinary	100	100
Challenger Life Subsidiary Holdings Ltd	Australia	Ordinary	100	100
Challenger Listed Investments Limited	Australia	Ordinary	100	100
Challenger Luxembourg Holding No.1A S.a.r.l.	Luxembourg	Ordinary	100	100
Challenger Luxembourg Holding No.1B S.a.r.l.	Luxembourg	Ordinary	100	100
Challenger Luxembourg Holding No.2 S.a.r.l.	Luxembourg	Ordinary	100	100
Challenger Managed Investments (International) Pty Limited	Australia	Ordinary	100	100
Challenger Managed Investments Limited	Australia	Ordinary	100	100
Challenger Management Services (UK) Limited	UK	Ordinary	100	100
Challenger Management Services Limited	Australia	Ordinary	100	100
Challenger Margin Lending Pty Limited	Australia	Ordinary	100	100
Challenger MEIF Holding Trust	Australia	Ordinary	100	100
Challenger MEIF Trust	Australia	Ordinary	100	100
Challenger Millennium NPF Trust	Australia	Ordinary	100	100
Challenger Millennium NPL Trust	Australia	Ordinary	100	100
Challenger Millennium Series 2001-1C Trust	Australia	Ordinary	100	100
Challenger Millennium Series 2001-1E Trust	Australia	Ordinary	100	100
Challenger Millennium Series 2001-2 Trust	Australia	Ordinary	100	100
Challenger Millennium Series 2001-3 Trust	Australia	Ordinary	100	100
Challenger Millennium Series 2002-1G Trust	Australia	Ordinary	100	100
Challenger Millennium Series 2002-2 Trust	Australia	Ordinary	100	100
Challenger Millennium Series 2003-1G Trust	Australia	Ordinary	100	100
Challenger Millennium Series 2003-2 Trust	Australia	Ordinary	100	100
Challenger Millennium Series 2003-3G Trust	Australia	Ordinary	100	100
Challenger Millennium Series 2003-4 Trust	Australia	Ordinary	100	100
Challenger Millennium Series 2003-5G Trust	Australia	Ordinary	100	100
Challenger Millennium Series 2004-1E Trust	Australia	Ordinary	100	100
Challenger Millennium Series 2004-2G Trust	Australia	Ordinary	100	100
Challenger Millennium Series 2004-3P Trust	Australia	Ordinary	100	100
Challenger Millennium Series 2004-4E Trust	Australia	Ordinary	100	100
Challenger Millennium Series 2004-5 Trust	Australia	Ordinary	100	100
Challenger Millennium Series 2005-1G Trust	Australia	Ordinary	100	100
Challenger Millennium Series 2005-2L Trust	Australia	Ordinary	100	100
Challenger Millennium Series 2005-3E Trust	Australia	Ordinary	100	100
Challenger Millennium Series 2006-1 Trust	Australia	Ordinary	100	100
Challenger Millennium Series 2006-2G Trust	Australia	Ordinary	100	100
Challenger Millennium Series 2006-3L Trust	Australia	Ordinary	100	100
Challenger Millennium Series 2006-4H Trust	Australia	Ordinary	100	100
Challenger Millennium Series 2007-1E Trust	Australia	Ordinary	100	100
Challenger Millennium Series 2007-2L Trust	Australia	Ordinary	100	100
Challenger Millennium Series 2008-1 Trust	Australia	Ordinary	100	100
Challenger Millennium Series 2008-2 Trust	Australia	Ordinary	100	100
Challenger Millennium Series 2009-1 Trust	Australia	Ordinary	100	100
Challenger Millennium Warehouse C Trust	Australia	Ordinary	100	100
Challenger Millennium Warehouse F Trust	Australia	Ordinary	100	100
Challenger Millennium Warehouse Non-Performing Trust	Australia	Ordinary	100	100
Challenger Mortgage Management Pty Limited	Australia	Ordinary	100	100
Challenger Non-Conforming Finance Pty Limited	Australia	Ordinary	100	100
Challenger North of England Gas Holding Trust	Australia	Ordinary	100	100
Challenger NZ Millennium Series 2004-A Trust	New Zealand	Ordinary	100	100
Challenger NZ Millennium Series 2007-AP Trust	New Zealand	Ordinary	100	100
Challenger NZ Millennium Warehouse W Trust	New Zealand	Ordinary	100	100

35. Controlled entities (continued)

Name of entity	Country of incorporation	Class of shares/units	% owned 30 June 2011	% owned 30 June 2010
Challenger Originator Finance Pty Limited	Australia	Ordinary	100	100
Challenger Property Asset Management Pty Limited	Australia	Ordinary	100	100
Challenger Property Income Trust	Australia	Ordinary	100	100
Challenger Property Trust No. 18	Australia	Ordinary	100	100
Challenger Property Trust No. 19	Australia	Ordinary	100	100
Challenger Property Trust No. 25	Australia	Ordinary	100	100
Challenger Property Trust No. 27	Australia	Ordinary	100	100
Challenger Property Trust No. 28	Australia	Ordinary	100	100
Challenger Property Trust No. 29	Australia	Ordinary	100	100
Challenger Property Trust No. 30	Australia	Ordinary	100	100
Challenger Property Trust No. 31	Australia	Ordinary	100	100
Challenger Property Trust No. 32	Australia	Ordinary	100	100
Challenger Property Trust No. 33	Australia	Ordinary	100	100
Challenger Property Trust No. 34	Australia	Ordinary	100	100
Challenger Property Trust No. 35	Australia	Ordinary	100	100
Challenger Property Trust No. 36	Australia	Ordinary	100	100
Challenger Reit AFSL Pty Limited	Australia	Ordinary	100	100
Challenger Reit Holdings Pty Limited	Australia	Ordinary	100	100
Challenger Retirement Services Pty Limited	Australia	Ordinary	100	100
Challenger SCR LLP Member Limited	Australia	Ordinary	100	100
Challenger Seattle Trust	Australia	Ordinary	100	100
Challenger Securitisation Management Pty Limited	Australia	Ordinary	100	100
Challenger SkyBridge (Capital II) Investment LLP	Jersey	Ordinary	100	100
Challenger SkyBridge (Fund LP) Jersey Limited	Jersey	Ordinary	100	100
Challenger Skybridge (Fund) Holding Company Pty Limited	Australia	Ordinary	100	100
Challenger Skybridge (Group) Holding Company Pty Limited	Australia	Ordinary	100	100
Challenger Skybridge (Hastings) Holdings Company Pty Limited	Australia	Ordinary	100	100
Challenger Special Servicing Pty Limited	Australia	Ordinary	100	100
Challenger Strategic Property Partners 1 Fund	Australia	Ordinary	100	100
Challenger Structured Credit UK Trust	Australia	Ordinary	100	100
Challenger Titanium Series 2004-1 Trust	Australia	Ordinary	100	100
Challenger Titanium Series 2005-1 Trust	Australia	Ordinary	100	100
Challenger Titanium Series 2006-1 Trust	Australia	Ordinary	100	100
Challenger Titanium Warehouse C Trust	Australia	Ordinary	100	100
Challenger Towers Holding Trust	Australia	Ordinary	100	100
Challenger Towers Trust	Australia	Ordinary	100	100
Challenger Treasury Limited	Australia	Ordinary	100	100
Challenger UK Tank Storage Holding Trust	Australia	Ordinary	100	100
Challenger UK Tank Storage Limited	UK	Ordinary	100	100
Challenger UK Terminals Limited	Jersey	Ordinary	100	100
Challenger US Infrastructure Holdings Pty Limited	Australia	Ordinary	100	100
Challenger USPF II Trust	Australia	Ordinary	100	100
Challenger Wales and the West Gas Holding Trust	Australia	Ordinary	100	100
Challenger Welcome Break Limited	Jersey	Ordinary	100	100
Challenger Welcome Break Trust	Australia	Ordinary	100	100
Challenger Wholesale Finance Holdings Pty Ltd	Australia	Ordinary	100	100
Challenger Wind Holdings Pty Limited	Australia	Ordinary	100	100
Challenger Wind Trust	Australia	Ordinary	100	100
CLC Commercial Mortgages Trust	Australia	Ordinary	100	100
CLC Leveraged Loan Fund	Australia	Ordinary	100	100
CLC Liquidity Trust	Australia	Ordinary	100	100
CMM NIM Trust No 1	Australia	Ordinary	100	100
CMM NIM Trust No 2	Australia	Ordinary	100	100
CMM NIM Trust No 3	Australia	Ordinary	100	100
CMM NIM Trust No 4	Australia	Ordinary	100	100
CMM NIM Trust No 5	Australia	Ordinary	100	100

Name of entity	Country of incorporation	Class of shares/ units	% owned 30 June 2011	% owned 30 June 2010
CMM NIM Trust No 6	Australia	Ordinary	100	100
CMM NIM Trust No 7	Australia	Ordinary	100	100
CMM NIM Trust No 8	Australia	Ordinary	100	100
CMM NIM Trust No 9	Australia	Ordinary	100	100
CMS (UK) Pty Limited	UK	Ordinary	100	100
County Court Property Trust	Australia	Ordinary	100	100
CPHIC Investments Pty Limited	Australia	Ordinary	100	100
CSPP1 Broadbeach Pty Limited	Australia	Ordinary	100	100
CSPP1 Investment Company 1 Pty Limited	Australia	Ordinary	100	100
CSPP1 Maitland Pty Limited	Australia	Ordinary	100	100
CSPP1 Mavis Court Pty Limited	Australia	Ordinary	100	100
Discovery House Trust	Australia	Ordinary	100	100
Emerging Markets Infrastructure Fund Holdings Pty Ltd	Australia	Ordinary	100	100
Endowment Warrants Limited	Australia	Ordinary	100	100
Epping No.1 Trust	Australia	Ordinary	100	100
Epping No.2 Trust	Australia	Ordinary	100	100
Five Oceans Global Equity Extension Fund	Australia	Ordinary	95	95
Five Oceans World Fund	Australia	Ordinary	26	55
FXF Holdings Pty Limited	Australia	Ordinary	100	100
Goodman Fielder – North Ryde Property Trust	Australia	Ordinary	100	100
Harris Global Sovereign Bond Trust ¹	Australia	Ordinary	–	–
Hayes Park Property Trust	Australia	Ordinary	100	100
Hotel Investments Trust	Australia	Ordinary	100	100
Interstar NZ Millennium Series 2004-A	New Zealand	Ordinary	100	100
Interstar Titanium Series 2006-1Trust	Australia	Ordinary	100	100
LANV Pty Ltd	Australia	Ordinary	100	100
Challenger High Yield Fund	Australia	Ordinary	100	100
Maitland Unit Trust	Australia	Ordinary	100	100
Mavis Court Development Co Pty Ltd	Australia	Ordinary	80	80
Mawbury Pty Limited	Australia	Ordinary	100	100
Mercury Term Managed Trust ¹	Australia	Ordinary	–	–
Oaklands Hill Pty Limited	Australia	Ordinary	100	100
Rendezvous Hotels Flinders Street Trust	Australia	Ordinary	100	100
Riverside Trust No.1	Australia	Ordinary	100	100
Riverside Trust No.2	Australia	Ordinary	100	100
Sabrand Limited	Cyprus	Ordinary	100	100
Senator House Property Trust	Australia	Ordinary	100	100
Talavera Herring Unit Trust	Australia	Ordinary	50	50
Talaverra Herring Pty Limited	Australia	Ordinary	100	100
The Liberty Group Consortium Pty Limited	Australia	Ordinary	100	100
TLG Holding Unit Trust	Australia	Ordinary	100	100
TLG Services Pty Limited	Australia	Ordinary	100	100
TLG Unit Trust	Australia	Ordinary	100	100
TLGH Pty Limited	Australia	Ordinary	100	100
TMA C Warehouse C Trust	Australia	Ordinary	100	100
TRE Data Centre Trust	Australia	Ordinary	100	100
TRE Data Centres Canberra Pty Ltd	Australia	Ordinary	100	100
Village Property Trust	Australia	Ordinary	100	100
Waterford County Pty Limited	Australia	Ordinary	67	67
Wavestone Aust Equity Long/Short Fund	Australia	Ordinary	22	69
Westwind Finance Plc	Ireland	Equity	100	100
Wetherill Park Property Trust	Australia	Ordinary	100	100
World Business Centre Heathrow Property Trust	Australia	Ordinary	100	100
Wyetree Asset Management Limited (UK)	UK	Ordinary	85	85

¹ These Trusts are consolidated due to the risks borne by the Company as opposed to the % equity holding

36. Investments in associates

Name of company	Principal activity	Country of domicile	30 June 2011 %	30 June 2010 %	30 June 2011 \$M	30 June 2010 \$M
Challenger MBK Fund Management Pte Ltd	Funds Management	Singapore	50	50	3.1	1.6
Homeloans Limited	Mortgage Lending	Australia	23	23	19.7	26.7
Ardea Investment Management Pty Limited	Funds Management	Australia	30	30	2.6	2.4
Five Oceans Asset Management Limited	Funds Management	Australia	25	25	3.4	3.3
Greencape Capital Pty Limited	Funds Management	Australia	35	25	13.7	2.8
Kapstream Capital Pty Limited	Funds Management	Australia	25	25	4.8	4.6
Kinetic Investments Partners Limited	Funds Management	Australia	20	20	0.4	0.2
WaveStone Capital Pty Limited	Funds Management	Australia	30	28	2.0	2.0
Merlon Capital Partners Ltd ¹	Funds Management	Australia	58	30	0.9	0.4
Bentham Asset Management Pty Ltd ¹	Funds Management	Australia	64	49	1.1	0.2
Alphinity Investment Management Pty Ltd ¹	Funds Management	Australia	70	–	0.2	–
NovaPort Capital Pty Ltd ¹	Funds Management	Australia	59	–	0.2	–
Impairment ²					(11.2)	(11.2)
					40.9	33.0
Movements in carrying amount of investments in associates						
Opening balance					33.0	43.2
Investment in associates acquired in current year					12.0	0.4
Sale of interest in associates					–	(12.5)
Share of associates' net profit					7.9	3.7
Dividend/capital return received					(12.0)	(1.8)
Carrying amount at the end of the financial year					40.9	33.0
Share of the associates' profit or loss:						
Profit before tax					7.9	5.3
Income tax expense					–	(1.6)
Profit for the year					7.9	3.7
Retained profits attributable to associates at the beginning of the financial year					9.2	5.5
Retained profits attributable to associates at the end of the financial year					17.1	9.2
Share of the associates' balance sheet:						
Assets					129.9	143.4
Liabilities					(113.1)	(125.5)
Net assets					16.8	17.9

¹ Restriction in voting rights attached to the Group's holding make this investment an associate despite economic ownership being greater than 50%.² This impairment relates to Homeloans Limited.

37. Parent entity

The statement of comprehensive income and balance sheet for the Company for the year ended and as at 30 June are as follows:

	30 June 2011 \$M	30 June 2010 \$M
Statement of Comprehensive Income		
Revenue	258.8	180.1
Expenses	–	–
Profit before income tax	258.8	180.1
Income tax expense	(1.8)	(1.7)
Profit and total comprehensive income for the year	257.0	178.4
Balance Sheet		
Assets		
Cash and cash equivalents	1.2	1.0
Receivables	1,279.6	1,113.5
Current tax assets	–	3.0
Deferred tax assets	62.5	36.9
Investment in controlled entities	1,147.5	1,121.5
Total assets	2,490.8	2,275.9
Liabilities		
Payables	927.6	857.7
Current tax liability	0.9	–
Provisions	0.1	3.0
Total liabilities	928.6	860.7
Net assets	1,562.2	1,415.2
Equity		
Contributed equity	1,185.8	1,200.4
Equity option premium reserve	125.4	125.3
Share based payment reserve	50.5	66.7
Retained profits	201.5	22.8
Total equity	1,562.2	1,415.2

See Note 39 for details of any contingent liabilities applicable to the parent entity.

38. Subsequent events

At the date of this financial report and, other than as disclosed in this financial report, no other 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.

Global market volatility

Subsequent to 30 June 2011 there has been significant volatility in global equity and debt markets following the downgrade of the credit rating of US long-term sovereign debt by Standard & Poor's and continued market uncertainty in relation to European sovereign debt.

A detailed sensitivity analysis of asset and liability valuations to market risk, credit risk and liquidity risk is provided in Note 27 to the financial report. The Group actively manages levels of capital, gearing and liquidity of the investment assets held to support the Group's obligations to the life contract holders of Challenger Life Company Limited (CLC), which is subject to prudential regulation. As at 19 August 2011, CLC held significant capital in excess of its prudential regulatory requirements.

39. Contingent liabilities, contingent assets and credit commitments

Warranties

Over the course of its corporate activity the Group has given, as a seller of companies and as a vendor of real estate properties, warranties to purchasers on several agreements that are still outstanding at 30 June 2011. Other than noted below, at the date of this report no material claims against these warranties have been received by the Group.

The Victorian State Revenue Office (SRO) raised an assessment for stamp duty in respect of certain properties acquired by the Challenger Diversified Property Group which was disputed by the Group. A judgement in favour of Challenger was made during the period but the SRO has since lodged an appeal on some discrete issues. This appeal was held in July 2011 and the Group does not expect to incur any material liability on this case.

Parent entity guarantees and undertakings

Challenger Limited has extended the following guarantees and undertakings to entities in the Group:

- (i) A guarantee supporting the corporate banking facility;
- (ii) Letters of support in respect of certain subsidiaries in the normal course of business. The letters recognise Challenger Limited has a responsibility to ensure that those subsidiaries continue to meet their obligations; and
- (iii) Australian Financial Services Licence (AFSL) deeds of undertaking as an eligible provider.

Third party guarantees

Bank guarantees have been issued by a third party financial institution on behalf of the Group and its subsidiaries for items in the normal course of business, such as rental contracts. The amounts involved are not considered to be material to the Group.

Contingent future commitments

Challenger Life Company Limited has made capital commitments to external counterparties for future investment opportunities such as development or investment purchases. As at 30 June 2011 there are potential future commitments totalling \$175.2 million (30 June 2010: \$229.6 million) in relation to these opportunities.

Contingent tax asset

As a result of a retrospective amendment to the tax legislation in 2010, the Group has lodged a series of claims in relation to the Tax Consolidation treatment of rights to future income arising from the Group's entry into the tax consolidation regime in 2003. The amended legislation allows for deductions to be spread over 10 years from 2003. On 30 March 2011, the Assistant Treasurer announced a Board of Taxation review of the legislation surrounding these deductions. The Group's claims will not be processed until the findings of this review are communicated. If successful, the Group's tax claim, including prior year and future deductions, would be approximately \$45 million. No tax benefit or asset has been recognised in respect of this amount.

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; however, the Directors are of the opinion that no material loss will be incurred.

Directors' declaration

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

- (a) the financial statements and notes of Challenger Limited and its controlled entities (the Group) are in accordance with the *Corporations Act 2001*, including:
 - (i) giving a true and fair view of the Group's financial position as at 30 June 2011 and of its performance for the year ended on that date; and
 - (ii) complying with Australian Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Regulations 2001*;
- (b) the financial statements and notes of the Group also comply with International Financial Reporting Standards as issued by the International Accounting Standards Board as disclosed in Note 1(ii) to the financial statements;
- (c) there are reasonable grounds to believe that the Group will be able to pay its debts as and when they become due and payable; and
- (d) this declaration has been made after receiving the declarations required to be made to the Directors in accordance with section 295A of the *Corporations Act 2001* for the financial year ended 30 June 2011.

On behalf of the Board



G A Cubbin
Director

Sydney
19 August 2011



D J Stevens
Director

Sydney
19 August 2011



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Independent auditor's report to the members of Challenger Limited

Report on the Financial Report

We have audited the accompanying financial report of Challenger Limited, which comprises the consolidated balance sheet as at 30 June 2011, the consolidated income statement, the consolidated statement of comprehensive income, the consolidated statement of changes in equity and the consolidated statement of cash flows for the year then ended, notes comprising a summary of significant accounting policies and other explanatory information, and the directors' declaration of the consolidated entity comprising the company and the entities it controlled at the year's end or from time to time during the financial year.

Directors' Responsibility 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 controls as the directors determine are necessary to enable the preparation of the financial report that is free from material misstatement, whether due to fraud or error. In Note 1, the directors also state, in accordance with Accounting Standard AASB 101 *Presentation of Financial Statements*, that the financial statements comply with International Financial Reporting Standards.

Auditor's Responsibility

Our responsibility is to express an opinion on the financial report based on our audit. We conducted our audit in accordance with Australian Auditing Standards. Those standards require that we comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance about whether the financial report is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial report. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial report, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls relevant to the entity's preparation and fair presentation of the financial report 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 entity's internal controls. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial report.

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

Independence

In conducting our audit we have complied with the independence requirements of the *Corporations Act 2001*. We have given to the directors of the company a written Auditor's Independence Declaration, a copy of which is included in the directors' report. We confirm that the Auditor's Independence Declaration would be in the same terms if given to the directors as at the time of this auditor's report.

Opinion

In our opinion:

- a. the financial report of Challenger Limited is in accordance with the *Corporations Act 2001*, including:
 - i. giving a true and fair view of the consolidated entity's financial position as at 30 June 2011 and of its performance for the year ended on that date; and
 - ii. complying with Australian Accounting Standards and the *Corporations Regulations 2001*; and
- b. the financial report also complies with International Financial Reporting Standards as disclosed in Note 1.

Report on the Remuneration Report

We have audited the Remuneration Report included in pages 35 to 55 of the directors' report for the year ended 30 June 2011. The directors of the company are responsible for the preparation and presentation of the Remuneration Report in accordance with section 300A of the *Corporations Act 2001*. Our responsibility is to express an opinion on the Remuneration Report, based on our audit conducted in accordance with Australian Auditing Standards.

Auditor's Opinion

In our opinion the Remuneration Report of Challenger Limited for the year ended 30 June 2011, complies with section 300A of the *Corporations Act 2001*.

Ernst & Young



S J Ferguson
Partner
Sydney

19 August 2011

Five year history

	30 June 2007 \$M	30 June 2008 \$M	30 June 2009 \$M	30 June 2010 \$M	30 June 2011 \$M
Income statement					
Normalised cash operating earnings	163.8	207.9	250.8	338.0	400.8
Net fee income	183.7	187.3	114.4	102.0	88.4
Other income	6.8	6.5	4.7	7.6	4.8
Total management view of revenue	354.3	401.7	369.9	447.6	494.0
Operating expenses	(188.4)	(191.3)	(186.2)	(181.8)	(180.2)
Normalised EBIT	165.9	210.4	183.7	265.8	313.8
Interest and borrowing costs	(33.7)	(41.3)	(36.9)	(14.1)	(2.7)
Discontinued operations	98.2	110.2	136.1	39.1	–
Normalised profit before tax	230.4	279.3	282.9	290.8	311.1
Tax on normalised profit	(48.4)	(61.4)	(64.0)	(58.3)	(63.1)
Normalised profit after tax	182.0	217.9	218.9	232.5	248.0
Investment experience after tax	49.6	(192.3)	(309.6)	51.3	(28.7)
Significant items after tax	23.4	(69.8)	–	(1.3)	42.1
Statutory profit for the year	255.0	(44.2)	(90.7)	282.5	261.4
Balance sheet					
Total assets	27,015.2	27,157.3	25,237.8	18,375.9	17,836.2
Total liabilities	25,566.6	25,527.3	23,548.4	16,656.2	16,036.8
Net assets	1,448.6	1,630.0	1,689.4	1,719.7	1,799.4
Total equity attributable to equity holders of the parent	1,339.6	1,612.9	1,381.9	1,339.6	1,488.3
Assets under management and administration					
Life	3,476.0	5,245.0	5,767.0	7,578.0	8,387.0
Funds Management	22,996.0	21,921.0	16,041.0	20,221.0	23,608.0
Crossholdings	(886.0)	(1,478.0)	(2,164.0)	(3,851.0)	(4,086.0)
	25,586.0	25,688.0	19,644.0	23,948.0	27,909.0
Discontinued operations					
Mortgage Management	23,013.0	48,068.0	93,295.0	–	–
Financial Planning	8,796.0	–	–	–	–
Crossholdings (discontinued operations)	(3,185.0)	(3,044.0)	(2,604.0)	–	–
Total assets under management and administration	54,210.0	70,712.0	110,335.0	23,948.0	27,909.0

	30 June 2007 \$M	30 June 2008 \$M	30 June 2009 \$M	30 June 2010 \$M	30 June 2011 \$M
Earnings per share (cents)					
Basic – statutory profit/(loss)	46.3	(7.5)	(16.2)	55.3	54.5
Diluted – statutory profit/(loss)	43.2	(8.1)	(15.9)	51.9	50.7
Basic earnings per share – normalised profit (cents)	33.0	37.1	39.2	45.5	51.7
Diluted earnings per share – normalised profit (cents)	30.7	35.4	38.4	42.7	48.1
Dividends per share (cents)					
Interim	5.0	5.0	5.0	6.0	7.0
Final	7.5	7.5	7.5	8.5	9.5
Total	12.5	12.5	12.5	14.5	16.5
Dividend payout ratio – statutory profit/(loss) (%) ¹	27.0%	N/A	N/A	26.2%	30.3%
Dividend payout ratio – normalised profit/(loss) (%) ¹	37.9%	33.7%	31.9%	31.9%	31.9%
Ratios					
Net gearing (%) ²	5.6%	0.6%	11.5%	0.0%	0.0%
Gearing (%) ³	16.9%	13.4%	19.6%	0.0%	0.0%
Return on shareholders' funds – statutory profit ⁴	17.6%	(2.7%)	(6.6%)	21.1%	17.6%
Return on shareholders' funds – normalised ⁵	12.6%	13.5%	15.8%	17.4%	16.7%
Staff numbers ⁶	1,063	911	837	460	455
Share price at 30 June (\$)	5.83	1.89	2.24	3.52	4.89
Ordinary share capital (million shares) ⁷	554.6	600.4	569.3	499.6	496.7
Market capitalisation at 30 June (\$ million) ⁸	3,233.3	1,134.8	1,275.3	1,758.6	2,428.8

¹ Dividends per share/EPS (basic).

² Calculated as net debt/(net debt + equity).

³ Calculated as debt/(debt + equity).

⁴ Calculated as statutory profit/total equity attributable to equity holders.

⁵ Calculated as normalised profit after tax/total equitable attributable to equity holders.

⁶ 2008 numbers exclude Financial Planning employees transferred on the sale of the business on 30 June 2008. 2009 excludes Mortgage Management employees transferred on completion of the sale of the business on 30 October 2009.

⁷ Represents issued ASX shares.

⁸ Calculated as share price x ordinary share capital.

Investor information

Distribution of shares as at 28 September 2011

Range	Number of shareholders	Number of shares	% of issued capital
1 – 1,000	8,620	4,273,445	0.87
1,001 – 5,000	9,100	21,982,059	4.48
5,001 – 10,000	1,861	13,777,436	2.81
10,001 – 100,000	1,188	28,356,015	5.78
100,001 and over	111	421,918,638	86.05
	21,075	496,667,291	100.00

The number of unmarketable parcels is 676 and number of unmarketable shares is 34, 332.

Substantial shareholders

The number of shares held by substantial shareholders and their associates, based on the latest substantial shareholder notifications, and the 20 largest individual shareholders are as follows:

Shareholder	Number of shares	% of issued capital
National Australia Bank Limited	52,833,463	10.70
AMP Limited	33,194,935	6.64
Caledonia (Private) Investments Pty Limited and associates	39,023,063	7.90
Ausbil Dexia Limited	33,624,405	6.81

Twenty largest shareholders as at 28 September 2011

1. National Nominees Limited	95,323,678	19.44
2. HSBC Custody Nominees (Australia) Limited	86,638,527	17.67
3. J P Morgan Nominees Australia Limited	62,655,546	12.78
4. UBS Nominees Pty Ltd	38,201,942	7.79
5. Citicorp Nominees Pty Limited	31,384,292	6.40
6. UBS Nominees Pty Ltd	13,351,744	2.72
7. AMP Life Limited	10,249,842	2.09
8. JP Morgan Nominees Australia Limited	8,773,988	1.79
9. Cogent Nominees Pty Limited	8,235,313	1.68
10. CPU Share Plans Pty Ltd	8,005,468	1.63
11. Queensland Investment Corporation	4,289,505	0.87
12. HSBC Custody Nominees (Australia) Limited – A/C 2	3,462,226	0.71
13. Cogent Nominees Pty Limited	3,202,985	0.65
14. Citicorp Nominees Pty Limited	3,050,709	0.62
15. WIN Television Nsw Pty Limited	3,046,601	0.62
16. UBS Nominees Pty Ltd	2,500,000	0.51
17. UBS Wealth Management Australia Nominees Pty Ltd	2,108,749	0.43
18. Invia Custodian Pty Limited	2,081,903	0.42
19. Australian Reward Investment Alliance	1,877,181	0.38
20. CPU Share Plans Pty Ltd	1,800,000	0.37
	390,240,199	79.59

Voting rights

On a show of hands, every member present at the meeting in person or by proxy shall have one vote and upon a poll each share shall have one vote.

ASX listing

Challenger Limited shares are listed on the ASX under code CGF. Share price details and company information can be accessed via either the company website www.challenger.com.au or the ASX website www.asx.com.au.

Shareholder queries

For any administrative matters in respect of your Challenger Limited shareholding, please contact the Company's share registrar, Computershare.

Computershare Investor Services Pty Limited
Level 3, 60 Carrington Street, Sydney NSW 2000.
Investor queries 1300 850 505
www.computershare.com.au

To assist with all enquiries, please quote your unique Security Reference Number (SRN) and your current address when dealing with Computershare.

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Directory

Principal place of business and registered office in Australia

Level 15
255 Pitt Street
Sydney NSW 2000
Telephone: 02 9994 7000
Facsimile: 02 9994 7777

Directors

Peter Polson (Chairman)
Dominic Stevens (Chief Executive Officer)
Graham Cubbin
Jonathan Grunzweig
Russell Hooper
Brenda Shanahan
Leon Zwier

Company secretaries

Michael Vardanega
Suzanne Koeppenkastrop

Share registry

Computershare Investor Services Pty Limited
Level 3, 60 Carrington Street
Sydney NSW 2000
Telephone: 02 8234 5000
Facsimile: 02 8234 5050
Website: www.computershare.com.au

Auditor

Ernst & Young
680 George Street
Sydney NSW 2000

Internet address

www.challenger.com.au

Level 15

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Sydney NSW 2000
Telephone 02 9994 7000
Facsimile 02 9994 7777

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Brisbane QLD 4000
Telephone 07 3136 5400
Facsimile 07 3136 5407

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Adelaide SA 5000
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