

CORPORATE GOVERNANCE

Insurance Australia Group's corporate governance structure and supporting risk management framework provide a sustainable balance of our core business function of paying claims and providing insurance at an affordable cost with our responsibility to provide fair and stable returns to shareholders.

The Board delegates responsibility for the day-to-day operations and administration of the Group to the CEO.

THE ROLE OF THE BOARD AND MANAGEMENT

The Insurance Australia Group Board is accountable to shareholders for the performance, operations and affairs of the Group:

- The Board drives the strategic direction of the Group by approving corporate strategies and setting goals and policies. Specific policy areas include risk management, internal compliance and control, codes of conduct and legal compliance.
- The Board monitors management's performance and strategy implementation and is responsible for appointing and removing the Chief Executive Officer (CEO), the Chief Financial Officer and the Company Secretary.
- The Board approves management recommendations on major expenditure, capital management, and acquisitions and divestments as well as monitoring the financial performance and reporting of the Group.

The Board delegates responsibility for the day-to-day operations and administration of the Group to the CEO.

The Board is committed to ensuring individual Directors clearly understand their term of office, duties, rights and responsibilities as a member of the Board. To that end, the Board has developed a charter to preserve existing practices. At the same time, all current Directors have been issued a formal letter acknowledging responsibilities. Formal appointment letters have also been developed for new Directors.

ETHICAL AND RESPONSIBLE DECISION MAKING

Insurance Australia Group takes ethical and responsible decision making very seriously. It expects its employees, including Directors and executive management, to do the same, as reflected in the Group's internal policies around conduct, continuous disclosure and insider trading.

Insurance Australia Group's Code of Conduct extends to all people employed by the Group. The code is designed to encourage ethical and appropriate behaviour in all avenues of work, based on the following principles:

- Acting honestly and openly in all dealings;
- Complying with all laws and industry codes that regulate our activities;
- Abiding by our rules to prevent insider trading;
- Maintaining confidentiality; and
- Avoiding conflicts of interest.

In keeping with the Code of Conduct and the spirit of continuous disclosure, Insurance Australia Group is committed to ensuring shareholders are informed of significant developments for the Group. All announcements to the Australian Stock Exchange are immediately posted on

the Group website, www.iag.com.au, and proactively relayed to registered shareholders through an email messaging service. Briefings are webcast where practical and copies retained on the website for ease of access. Media coverage of key events is also sought as a means of delivering information to shareholders and the market. Formal communication with shareholders is also conducted via the annual report, interim report and at the Annual General Meeting (AGM) of shareholders.

Insurance Australia Group takes ethical and responsible decision making very seriously. It expects its employees, including Directors and executive management, to do the same, as reflected in the Group's internal policies around conduct, continuous disclosure and insider trading.

The Group's Continuous Disclosure and Insider Trading Policy reinforces our commitment to continuous disclosure, as well as the responsibility of all employees regarding price sensitive information and insider trading. The policy includes a protocol outlining how information is released to the public and focuses on improving continuous disclosure and access to information for all investors. The policy also provides examples of what

could constitute price sensitive information and how knowledge of such information prohibits share trading. A Share Trading Protocol sets the framework for employee dealings in IAG shares and related interests, and aims to prevent the inadvertent breaching of insider trading laws. The protocol specifies that, subject to not being in possession of price sensitive information, Directors and designated employees may only buy or sell shares or options in the two to 30 day period immediately following the Group's six monthly results announcements and the AGM.

In keeping with the Code of Conduct and the spirit of continuous disclosure, Insurance Australia Group is committed to ensuring shareholders are informed of significant developments for the Group.

During the past year, both the Code of Conduct and Continuous Disclosure and Insider Trading Policy were recirculated to all employees and are displayed on the Group's intranet system.

BOARD COMPOSITION

With the exception of the CEO, the Board was comprised of nine non-executive Directors, including the Chairman, during the year to 30 June 2003. The Board has subsequently introduced a standard tenure of around two full three-year terms or approximately seven years,

with any further extensions only by invitation of the Board. In this context and in view of their length of service, Directors Maree Callaghan and Mary Easson advised they would not stand for re-election at the November AGM and retired from the Board, effective from 1 September 2003. Following this, the Board has resolved to reduce the number of Directors to a total of eight.

Importantly, the roles of Chairman and CEO are separate, as set down in the Board charter and consistent with our aim to maintain an appropriate division between the roles and responsibilities of the Board and management. The Chairman acts as a mentor to the CEO, facilitated by contact at least weekly, and as the primary conduit between the individual Directors and management.

The non-executive Directors are all independent. The specific experience and expertise of each Director is set out on pages 24 and 25 of this report.

HOW THE BOARD OPERATES

The Board is scheduled to meet formally approximately 10 times during the year.

Supplementing these meetings are the biannual Board strategy forums with the executive team, which were held in September and April during the past financial year. These two day strategy forums facilitate in-depth education on and analysis of areas of the business as well as longer-term focus areas and strategic initiatives.

Directors are also involved in a number of due diligence meetings around specific Company developments, which during the past year included the CGU and NZI acquisition and associated funding initiatives.

In addition, Insurance Australia Group has three standing Board Committees, each with charters and established operating procedures.

The number of Board and committee meetings held during the year is set out on page 35.

The Chairman's Committee can have up to five members, who must be non-executive Directors. Currently, the members of this committee are James Strong (Chairman), John Astbury and Rowan Ross. Committee meetings must be held at least four times a year.

The Board approves management recommendations on major capital expenditure, capital management, and acquisitions and divestments as well as monitoring the financial performance and reporting of the Group.

The main responsibilities of the Chairman's Committee include:

- Ensuring the Group's overall remuneration policy and approach fit the strategic goals of the Company;
- Monitoring the effectiveness, integrity and compliance of the Group's remuneration and human resource policies and practices;
- Reviewing Board performance and composition, and recommending candidates for appointment to the Board; and

- Considering social and ethical impacts of the Group's business practices and setting standards for social and ethical practices.

The Audit Committee can have up to five members, who must be non-executive Directors. Currently, the members of this committee are John Astbury (Chairman), Geoffrey Cousins and Anne Keating.

Directors are also involved in a number of due diligence meetings around specific Company developments, which during the past year included the CGU and NZI acquisition and associated funding initiatives.

The main responsibilities of the Audit Committee include:

- Exercising due care, diligence and skill in relation to the Group's full and half year financial reporting to ensure it is consistent with committee members' information and knowledge and sufficient for shareholder needs;
- Monitoring the application of accounting and actuarial standards, policies and practices by senior financial management when preparing full and half year financial statements;
- Reviewing the internal audit function and external financial reporting arrangements including auditor engagement, remuneration, independence and effectiveness;

- Meeting with each of the external auditor, Approved Actuary and consulting actuaries on at least an annual basis without management being present; and
- Reporting to the Board on all matters relevant to the committee's responsibilities.

The Risk Management & Compliance Committee can have up to five members, who must be non-executive Directors. Currently, the members of this committee are Rowan Ross (Chairman), Dominique Fisher and Neil Hamilton. Committee meetings must be held at least four times a year.

The main responsibilities of the Risk Management & Compliance Committee include:

- Overseeing the Group's risk management systems, practices and procedures to ensure effectiveness of risk identification and management, and compliance with internal guidelines and external requirements;
- Reviewing and evaluating the Group's internal control systems to ensure effectiveness;
- Approving and monitoring progress against the operational risk plan on an annual basis;
- Meeting with each of the Head of Group Risk Compliance and the Group General Counsel on at least an annual basis without other management being present; and
- Reporting to the Board on all matters relevant to the committee's responsibilities.

MANAGING RISK

Insurance Australia Group's approach to managing risk is a key criterion in evaluating the performance of executive and senior management. The Board actively promotes a culture of transparency, encouraging early and open communication of risk. To facilitate this open culture, the Board provides open access to the Chairs of the Board, the Audit Committee, and the Risk Management &

Compliance Committee. In particular, the Group has established mechanisms for rapid escalation of important matters to relevant executives and/or Board members.

The Chairman's and Board's approach to understanding risk management translates directly into the selection and appointment of candidates to key executive positions.

BOARD AND EXECUTIVE PERFORMANCE

Insurance Australia Group strives to ensure its Board collectively possesses the necessary expertise in insurance as well as a range of related and more generalist skills.

Insurance Australia Group's approach to managing risk is a key criterion in evaluating the performance of executive and senior management.

To that end, before Directors are appointed they must demonstrate a range of skills including industry knowledge, strategic planning, executive management, customer relations, finance, and legal and human resources expertise. Within these areas, the following experience is regarded as important though not exhaustive:

- Long term planning in social, business and regulatory frameworks;
- Ability to work in team environments;
- Knowledge of, or experience in, accounting and reporting issues;
- Working with executives, internal audit and risk teams, and external auditors;
- Working with industry bodies, regulators and government;

- Establishing policies and ethical standards of corporate behaviour; and
- Challenging views and proposals and taking well researched risks.

The Group also encourages the ongoing education and development of its Directors and management team to ensure they can expand and renew their skills and carry out their duties effectively.

From the outset, new Directors and senior executives have access to an orientation programme to introduce the management team and detail the Insurance Australia Group business. A programme introducing the fundamentals of general insurance is available to Directors and executives.

As required, Directors may take independent professional advice to assist with discharging their duties efficiently. A Board-agreed procedure allows Directors to obtain advice at the Group's expense, subject to prior clearance with the Chairman.

Every year, an independent party, commissioned by the Chairman's Committee undertakes an evaluation of the Board's performance. This year's review was carried out by Rosemary A Grieve & Associates. The Chairman has since met with each Director to discuss the recommendations flowing from the review and agree action plans as required.

COMPENSATION ARRANGEMENTS

Insurance Australia Group's approach to compensation arrangements for all employees, including Directors and executives, is based on ensuring we can attract and retain the best people to drive corporate performance and deliver returns to shareholders.

Compensation for executives is structured as a mix of fixed remuneration, short and

long-term incentives and is focused on reward for performance. Base pay is targeted at the market median for executive roles in similar-sized Australian companies.

Compensation for all other employees is structured as a mix of fixed remuneration and short-term incentives.

The Group also encourages the ongoing education and development of its Directors and management team to ensure they can expand and renew their skills and carry out their duties effectively.

Every employee (excluding Directors) has the capacity to earn at least 10% of their base pay as a short-term incentive. Short-term incentives are used to reward excellent performance. Incentive payments are determined based on a range of corporate, team and individual measures that relate to financial performance, customer service, people management, risk management and community engagement.

The Performance Award Rights Plan is used to provide a long-term incentive opportunity for the CEO and other selected executives. Performance Award Rights are rights over issued ordinary shares. Rights granted under the plan may be exercised for shares if a performance hurdle is met and a nominal amount is paid. The performance hurdle is based on the performance of the company (measured by total shareholder return) in

comparison with the other companies that comprise the S&P/ASX 100. The performance hurdle is tested in the period between three and five years after the rights are granted.

Insurance Australia Group no longer issues share options to executives over unissued shares.

Non-executive Directors

Base fees for non-executive Directors are set according to external advice. The payment of Directors' fees also seeks to align the interests of Directors with those of shareholders by requiring them to receive at least 20%, and up to 90%, of their annual base fee in IAG shares, rather than cash. No other equity-based remuneration is available to non-executive Directors.

Following consideration of changing views on non-executive Directors retirement benefit arrangements, the decision has been made to freeze the operation of the non-executive Directors retirement benefits scheme with effect from 1 September 2003. This means we will permit no further accruals to existing benefits and any new Directors will not be admitted to the scheme.

In consideration of the cessation of retirement benefits and the increased size and complexity of the Group, including additional duties on subsidiary boards, remuneration for non-executive Directors is being increased with effect from 1 September 2003. This is the first change since the Company listed three years ago. The base fee will increase from \$70,000 to \$100,000 per annum, with the Chairman's fee being maintained at three times the base fee per annum. Under the new fee arrangement, the Chairman does not receive additional fees for serving on the Chairman's Committee or for serving as a director of IAG Re.