Southern Cross
Health Society

The Southern Cross Medical Care Society
2013 Annual Report

Oranges have long been popular as a rich source of vitamin C that can help ward off colds, assist healing and bolster the immune system.

Contents

Overview

FOR THE YEAR ENDED 30 JUNE 2013

- The Southern Cross Medical Care Society is in a strong and stable financial position with reserves maintained at approximately seven months' worth of claims.
- In February the Society received an A+ (Strong) financial strength rating from Standard and Poor's for the eleventh consecutive year.
- The Society ended the year with a surplus of $22.1 million, which is within the budgeted range.
- Members continued to receive very good value for money from their Southern Cross policies. For every dollar received in premium income, 88.1 cents was returned to members in claims for healthcare services.
- During the year the Society earned $725.5 million in premiums, up 2.6% on 2012, and incurred $639.1 million in claims, up 5.5%.

Chairman's report

I am very pleased to report that the Society ended 2013 in a healthy financial position with a surplus of $22.1 million. As a Friendly Society, this surplus is retained in the Society for the benefit of members, mitigating future premium increases and maintaining financial reserves at appropriate levels.

A surplus of this nature also enables us to review and increase the value of policy benefits. This ensures policies keep pace with the needs of members, and that members receive the best possible value for their premium dollar.

During the period the Society earned $725.5 million in premiums, up 2.6% on 2012, and incurred $639.1 million in claims, up 5.5%. For every dollar received in premium, 88.1 cents was returned to members in claims for healthcare services; this demonstrates the excellent value that we, as a not-for-profit organisation, deliver to members. Careful management saw overheads come in under budget.

STRENGTH AND STABILITY

As a licensed insurer, and one that has always prided itself on sound financial management, the Society must maintain strong financial reserves to account for the possibility of severe and unexpected claims cost volatility over a short timeframe. At year end, the Society's reserves sat at $395.4 million. This is equivalent to approximately seven months' worth of claims and is within the target solvency range established by the Board.

These reserves helped the Society maintain its A+ financial strength rating from Standard and Poor's for the eleventh consecutive year. They are also part of our investment portfolio which generated $21.9 million in the 2013 year for the Society and its membership.

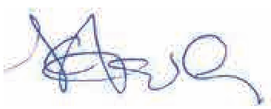
Members can have confidence that the Society is operating in a sound and sustainable manner, not just to meet regulatory requirements but to ensure that it will be here to meet members' healthcare funding requirements in years to come.

MEMBERSHIP LEVELS

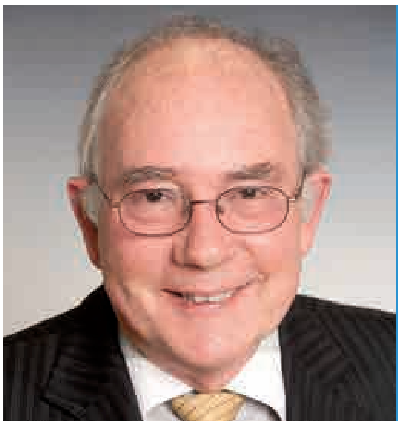
Over the past year the sector saw a small decline of 0.7% in the number of New Zealanders with health insurance. The Society fared slightly better than other insurers, with a membership decrease of 0.5%. This saw the Society's market share increase slightly from 61.0% to 61.1% and end the year with 817,822 members.

While the membership declined overall, some age groups, such as those between 21-35 and 51-55, increased in number. Most notably, an increase of 2.6% was observed among members aged 65 years and over. This age group now makes up 12% (101,000 members) of the total Southern Cross membership and accounts for 33% of all claims costs. Members aged 65 and over continue to receive very good value from their health insurance. During the financial year for every dollar of premium, 91 cents was returned to these members in claims for healthcare services.

To conclude, I would like to thank the Board and all Society staff for their hard work and commitment throughout the year. I would especially like to thank Phillip Meyer for his dedicated contribution to the Society. He will be retiring from the Society Board following the 2013 AGM, after eleven years of service. To our members, thank you for your continued support and loyalty to the Society.



Graeme Hawkins
Chairman



GRAEME HAWKINS
CHAIRMAN OF THE BOARD

Chief Executive Officer's report

The New Zealand public healthcare system is under enormous financial pressure. We have an ageing population, proportionally fewer taxpayers to fill the public purse, an increasing incidence of chronic conditions and a rising demand for new services and treatment options. A strong Southern Cross is important for New Zealand.

The spiralling cost to finance the public system is beginning to outpace the Government's ability to fund it. In July, Treasury released its four-yearly statement on the country's long term fiscal position in which it warned that rising healthcare costs are already beginning to create a challenge.

Treasury reported that since 1950, New Zealand's real per capita GDP has increased by 144%, while real per capita government spending on healthcare has increased by 412%. This trend is expected to continue. Public healthcare spending is forecast to increase from 6.8% of GDP in 2010 to 10.8% by 2060. This represents billions of additional dollars – and a potential economic time bomb.

One way or another, the healthcare services Kiwis expect must be paid for – whether through taxes, levies, insurances or directly out-of-pocket. It is not unreasonable to anticipate a greater personal contribution will be required towards one's healthcare in the future.

Treasury's fiscal statement also points out that adopting lower public healthcare spending might involve trade-offs, such as not funding some new treatments or introducing part payments from patients for some services.

With these concerns in mind, the Southern Cross Healthcare Group (of which the Health Society is one business) has:

- had discussions with Treasury
- participated in submissions to the New Zealand Productivity Commission
- contributed to this year's review of Retirement Income Policy and
- facilitated discussions among health leaders and politicians.

We are cognisant that healthcare costs are a massive problem on the horizon, and that individual New Zealanders having to save or spend more money on their own healthcare won't be a vote winner, but nevertheless we continue to engage in these issues with politicians.

TAX REBATES

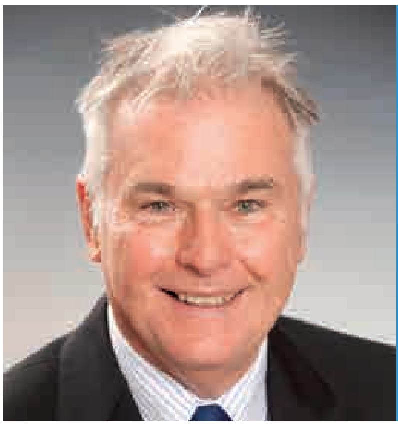
In March, the Affordable Healthcare Bill was tabled. The Bill calls for the removal of fringe benefit tax (FBT) on employer-paid health insurance premiums and a 25 per cent health insurance rebate for people aged 65 and over.

These are initiatives that Southern Cross has previously drawn attention to so it is pleasing for us to see they continue to be considered in Wellington.

Health insurance and healthcare affordability is a major issue for people in the 65 and over age group, whose premiums increase in line with their higher average claims costs. Making health insurance more affordable for those aged 65 years and over should:

- result in a significant improvement in overall health and quality of life for those who retain health insurance
- decrease the pressure on the public health system and
- free up resources for other patients to be seen more quickly in the public system.

As for employers, they provide health insurance for 640,000 working New Zealanders. They do this because there are clear, documented benefits in having a workforce with fast access to healthcare. Simply put, those with health insurance get back to work faster and this results in increased productivity.



DR IAN MCPHERSON
CHIEF EXECUTIVE OFFICER
SOUTHERN CROSS MEDICAL CARE SOCIETY

Southern Cross believes that the removal of FBT on employer-paid health insurance would:

- encourage more employers to offer this as a benefit to their workers
- align the tax treatment of health insurance premiums with levies under the ACC scheme and
- improve overall business productivity.

In reality, the Affordable Healthcare Bill may not be drawn from the ballot for some time, but it raises awareness and reinforces the essential message that New Zealanders need to be thinking about how they will finance their healthcare, particularly in retirement. Insurance and other Southern Cross services will help.

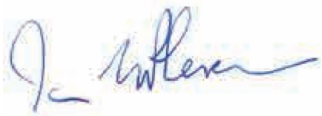
BETTER VALUE HEALTHCARE

In a TNS survey last September, just one in five respondents said they had actually started saving for future health costs.

Most people said they had no idea how much they need to save for healthcare in retirement but of those who felt they did, the majority vastly underestimated the actual costs that would be required. The median amount people thought they would need was $20,000. Unfortunately, this won't cover a lot over the course of a 15-year plus retirement – especially once medical inflation is accounted for.

To give an example of how healthcare costs have risen, forty years ago an adult health insurance policy cost 20 cents a week and a hip replacement was $350. The cost of a new hip now starts at $18,000 and a hospital and specialist plan for a forty year old is around $18 per week.

Unless we want to run the country dry, the increasing level of free elective healthcare available from the public health system cannot continue. The same public education and structures that exist for retirement savings need to exist for healthcare. This is something that is just starting to be talked about, yet it's as urgent as our need to save for housing, power, food and transport in retirement. And it needs long-term, apolitical leadership. Southern Cross wants to help provide this leadership.



Dr Ian McPherson
Chief Executive Officer
Southern Cross Medical Care Society

Operational report

With more than 800,000 members, the Society has a responsibility to take a leadership position with regard to implementing strategies that ensure long-term value for members' health spend. An area on which we continue to focus is new medical technology.

There is no doubt many recent advances in medical technology have resulted in better outcomes for patients – such as earlier, more precise diagnosis, faster recovery, and fewer complications.

In the private sector, individuals want to be able to access treatments not available in the public health system. However, we cannot take over everything from the public system. In order to maintain some control over impacts on premium levels, health insurers such as Southern Cross must ensure that any new medical technology has solid evidence to support any increase in claims costs that will be met by the membership.

In other industries, advances in technology usually reduce price. However, in healthcare the opposite often occurs. As a responsible insurer, we need to assess the clinical and cost effectiveness of new medical technology rigorously.

Southern Cross doesn't believe New Zealanders should be asked to fund the higher costs of new technology not yet proven to be better than already widely-used methods.

For this reason, Southern Cross canvasses the opinions of a broad range of medical experts, including medical representative bodies, and carefully assesses the cost and benefits of any new technology.

An example of this is Southern Cross' decision not to allow an extra charge for cataract surgery using new femtosecond laser technology. This technology, although showing early promise, has yet to prove significantly better outcomes than current methods of cataract surgery. Southern Cross funded 6,400 cataract surgeries in the past 12 months, at a total cost of $24.0 million. It is a big ticket item that the membership cannot afford to continually pay more for. As such, an Affiliated Provider agreement has been put in place for femtosecond laser to be funded for members but at the same price as a normal cataract procedure.

AFFILIATED PROVIDER PROGRAMME

Affiliated Providers are specialists and facilities contracted by Southern Cross to provide more convenient healthcare services to members at agreed prices. Benefits of the programme include that the:

- member knows up-front how much, if anything, he or she has to pay
- Affiliated Provider organises prior approval and processes the claim on the member's behalf
- member doesn't have to submit a paper claim and is not out of pocket while the claim is being processed.

Established in 1997, the Affiliated Provider programme now accounts for over 27% of all claims costs. There are currently 360 agreements in place, including 700 individual healthcare providers nationwide across 20 different medical specialities.

As a result of a continuing focus on cost containment over the last few years, we are making progress in our strategy to reduce medical inflation pressure. Agreed pricing for procedures between Southern Cross and Affiliated Providers is helping to minimise inflation of medical costs. The flow-on effect of this is to keep premium rises down.

Feedback from members tells us they value the simplicity of accessing healthcare services through Affiliated Providers. The Society will continue to increase this network.

PETER TYNAN
CHIEF EXECUTIVE
SOUTHERN CROSS HEALTH SOCIETY

CONVENIENCE AND ENHANCED SERVICE

Another area of focus is on better and easier ways for members to interact with us electronically. Going digital is not only improving member convenience but can reduce business costs.

Since starting down the digital pathway, the Society has seen steady growth in digital transaction volume, particularly with “My Southern Cross” and “Easy Claim”.

My Southern Cross is a secure member portal introduced to the Southern Cross website in July 2011. Through a personal internet account, members are able to receive and store communications from Southern Cross, check the status of claims and benefits with annual limits, change contact details and also choose to receive certain communications online rather than by post.

We now have over 36,000 registered users of My Southern Cross and we aim for that figure to double this financial year as we push forward to increase the capability and functionality.

Southern Cross Health Society Easy-Claim is an electronic claiming service exclusively for Southern Cross members. By presenting their Member Card, members can claim instantly at the payment counter. By eliminating the need to save receipts or submit claims forms, electronic claiming is much more convenient. This automation also provides the Society with more efficient business processes.

Since rolling out Easy Claim, we have had 365 pharmacies and over 100 other providers sign up. This includes sites around the country for Bay Audiology, Lumino, OPSM and Active Physio.

ADDING VALUE

With respect to declined surgery for Accident Compensation Corporation (ACC) injuries, we provide assistance to members for the review process. This not only helps mitigate our claims costs but ensures that the costs of our members’ healthcare services are met by the right organisation.

In the last year the Society worked with 394 members to seek review from ACC. This resulted in cost recovery of over $1.6 million. We also saw savings of $95,000, from treatment costs that the Society did not fund because the review was successful before the members’ surgeries had taken place.

Southern Cross also identified a further $2.2 million that had been paid for healthcare services more appropriately classed as ACC treatment injury claims. Upon request, this was reimbursed to Southern Cross by ACC. Further, the Society saw savings of $184,000 where the procedure was identified as an ACC treatment injury before payment was made.

At the centre of what we do is people. Our goal is to always put people first – ensuring we’re investing back into improving our services and evolving our product offering to keep pace with the evolving needs and expectations of our members.

Peter Tynan
Chief Executive
Southern Cross Health Society

Statement of corporate governance

The Southern Cross Medical Care Society adheres to principles designed to ensure sound corporate governance of its affairs, including Reserve Bank of New Zealand Governance Guidelines for licensed insurers issued under the Insurance (Prudential Supervision) Act 2010.

BOARD OF DIRECTORS

The Southern Cross Medical Care Society is governed by a Board of Directors who are elected by members of the Society. The administration, management and control of the Society is vested in the Board.

The Directors in office as at 30 June 2013 are:
Graeme S Hawkins (Chairman)
Dr Douglas D Baird
Carole B Durbin
Gregory W Gent
Elizabeth M Hickey
Phillip J Meyer
Keith B Taylor.

All current directors have been assessed by the Board in accordance with the Society's Fit and Proper Policy and have been certified as meeting the Reserve Bank of New Zealand's Fit and Proper Standard for directors of licensed insurers.

All current Directors are considered to be independent, in that they are independent of management and free from any associations that could materially interfere with the exercise of independent judgement. Profiles of these Directors, including their relevant qualifications and experience are contained on pages 9 and 10 of this Annual Report.

TRUSTEES

The Rules of The Southern Cross Medical Care Society provide for the appointment of three Trustees. All property belonging to the Society vests in the Trustees who hold it in trust for the members. As set out in the Investment Charter of Trustees, the Trustees are responsible for formulating overall investment policy (subject to approval by the Board) establishing investment guidelines, and monitoring the management of the investment portfolios. Trustees are nominated from among the Directors and elected by members of the Society.

The Trustees in office as at 30 June 2013 are:
Carole Durbin, Graeme Hawkins and Phillip Meyer.

BOARD ROLE AND CHARTER

The Board operates in accordance with the Friendly Societies and Credit Unions Act 1982, the Society's Rules and the Board Charter. The Board Charter describes the Board's role, procedures and relationship with management.

The role of the Board is to effectively represent, and promote the interests of, members. Means by which this is achieved include:

- ensuring the Society's goals are clearly established, and that strategies and business plans are in place for achieving them
- establishing policies for enhancing the performance of the Society
- monitoring the performance of management
- appointing the CEO
- identifying steps necessary to protect the Society's financial position
- ensuring the Society's financial statements are true and fair and otherwise conform with legal requirements
- ensuring the Board and management adhere to high ethical standards
- ensuring the Society has appropriate risk management and regulatory compliance policies and procedures in place.

The Board will regularly evaluate economic, political, social and legal issues and any other relevant external matters that may influence or affect the development of the business or the interests of members and/or stakeholders and, if thought appropriate, will take outside expert advice on these matters.

The Society's Rules and Board Charter, are available to view at www.southerncross.co.nz/board

The Board endorses the principles set out in the Code of Practice for Directors as adopted and approved by the Institute of Directors in New Zealand Inc. The Board has also adopted its own Code of Conduct and Ethics Policy to provide guidance to the Board, management and employees on how it expects them to conduct themselves when undertaking business on behalf of the Society.

All Directors disclose any actual or potential conflicts of interest. Should a conflict of interest arise during the course of Board business the affected Director is expected to excuse him or herself from the discussion and does not vote on those matters.

The Board meets formally on a regular scheduled basis and holds additional meetings as the occasion requires. At each normal meeting the agenda will include a report from management covering operational and financial performance, capital expenditure proposals, and major issues and opportunities. At intervals of not greater than one year the Board will review the Society's goals and strategies, approve budgets and financial statements, and undertake other activities listed in the Board Charter.

Separate strategic planning meetings are held in conjunction with the senior management team on a scheduled basis.

The Board reviews its own performance annually.

DELEGATION FRAMEWORK

Responsibility for the day-to-day operation and administration of the Society is delegated by the Board to the Chief Executive Officer and senior management. The CEO is authorised to make decisions in accordance with the strategy, plans, budgets and the specific delegation framework approved by the Board.

COMMITTEES

The Board has established a number of committees to assist in relation to specific business aspects. Each Board committee has a charter approved by the Board summarising the role, rights, responsibilities and membership requirements for that committee. The Board regularly reviews the charters of the Board committees and their performance against those charters. The charters are available to view at www.southerncross.co.nz/board

Audit Committee

The Audit Committee's objectives are to assist the Board in discharging its responsibilities in relation to oversight of financial matters including internal and external audit functions.

Specific responsibilities include reviewing the content and disclosure of the Annual Report's financial statements; ensuring the Board makes informed decisions regarding accounting policies, practices and disclosures; recommending the appointment of external and internal auditors; reviewing the annual external and internal audit plans; ensuring that adequate internal control systems are in place; and ensuring management has established a risk management framework to effectively identify, treat, monitor and report key business risks. The Audit Committee comprises Liz Hickey (Chairman), Graeme Hawkins, Phillip Meyer and Keith Taylor.

Remuneration Committee

The Remuneration Committee's objectives include providing advice to the Board in relation to the remuneration, employment conditions, development and performance management of the organisation's Chief Executive Officer and senior executives, and other remuneration-related matters including standard terms and conditions of employment. The Remuneration Committee comprises Carole Durbin (Chairman), Doug Baird, Greg Gent and Graeme Hawkins.

Nomination Committee

The Nomination Committee's objectives are to assist the Board in planning the Board's composition, evaluating the capabilities required of prospective Directors, identifying those prospective Directors, assessing Directors and relevant officers in accordance with the Society's Fit and Proper Policy, establishing the degree of Director independence, developing succession plans for the Board, and making recommendations to the Board accordingly. The Committee will consult with external advisors including executive search consultants and other independent sources of information and advice as it considers necessary for carrying out its responsibilities. The Nomination Committee currently comprises Graeme Hawkins (Chairman), Doug Baird, Carole Durbin, Greg Gent and Liz Hickey.

Investment Committee

The Investment Committee's role is to act in an advisory capacity to the Board and Trustees in fulfilling their oversight responsibility for the investment assets of the Society. The Committee monitors, and provides advice in relation to, the management of the Society's investment portfolios. The Investment Committee comprises the Trustees – Phillip Meyer (Chairman), Carole Durbin and Graeme Hawkins – and Keith Taylor.

EXTERNAL AUDIT INDEPENDENCE

The Board is committed to auditor independence. The Audit Committee is responsible for making recommendations to the Board concerning the appointment of external auditors and their terms of engagement. In September 2012 the Board supported the recommendation of the Audit Committee to re-appoint KPMG as the external auditors for the year ended 30 June 2013. Members confirmed the re-appointment of KPMG as auditors at the Annual General Meeting in December 2012.

LOANS TO DIRECTORS

The Southern Cross Medical Care Society does not make loans to Directors.

Board of Directors

GRAEME HAWKINS

(BSC, BCom, ACA, FInstD)
Chairman

Graeme Hawkins has been a professional director for 20 years. He was appointed to the Southern Cross Board in October 2008, and appointed Chairman on 1 July 2009. He is also Chairman of Southern Cross Health Trust. Mr Hawkins is a director of Cavalier Corporation Ltd and Ports of Auckland Ltd. From 2001 to 2007 he was an appointed director of Fonterra Co-operative Group and is a former chairman of Auckland Healthcare, now Auckland District Health Board. Earlier in his career he held a number of strategic and financial roles at Fletcher Challenge and is a former CEO of Dominion Breweries.

DR DOUGLAS BAIRD

(MBChB, DipObst, FRNZCGP)

Dr Douglas Baird was appointed to the Southern Cross Board in July 2007. He is managing director of Aotea Health Services and medical director for two accident and medical clinics in Auckland. Dr Baird is a Trustee of Southern Cross Health Trust and a Director of one Trust subsidiary company. Dr Baird is a past chairman of the Independent Practitioners Association Council (IPAC), was a founding director of ProCARE Health (which represents more than 500 GPs in Auckland) and of BPACnz (an organisation dedicated to effective use of resources by health providers). He has served in elected and advisory roles with the Auckland District Health Board, the ACC Medical Misadventure Unit and the Office of the Health and Disability Commissioner. Dr Baird has a Diploma of Obstetrics and is a Fellow of the Royal New Zealand College of General Practice.

CAROLE DURBIN

(BCom, LLB(Hons), FInstD)

Carole Durbin was appointed to the Southern Cross Board in August 2006 and has been a Society Trustee since 2007. She is also a Trustee of Southern Cross Health Trust and a Director of two of its subsidiary companies. Ms Durbin is a director of New Zealand-owned Fidelity Life. A part-time consultant to Simpson Grierson, one of New Zealand's leading legal firms, Ms Durbin has also held a number of previous board appointments including DamWatch Services Ltd, Simpson Grierson, Transpower NZ, software developer Synergy International (now Fronde), and was an Earthquake Commissioner. Until October 2009 she was chair of Mighty River Power, having been on that board since 1998. She is a Fellow of the Institute of Directors.

GREG GENT

Greg Gent was elected to the Southern Cross Board in December 2011. He is a Northland dairy farmer with a wealth of governance experience. From 2001 to 2011 he was a director of New Zealand's largest co-operative business, Fonterra. Prior to Fonterra's formation he was chairman of Northland Dairy and Kiwi Co-op Dairies. He is chairman of Farmers Mutual Group and Pengxin New Zealand Farm Management Limited; a director of New Zealand Institute for Plant and Food Research; and was appointed to the Northland District Health Board by the Minister of Health in 2010. Mr Gent is also a Trustee of Southern Cross Health Trust.

Board of Directors (L to R)

Phillip Meyer, Carole Durbin, Dr Douglas Baird, Graeme Hawkins, Greg Gent, Liz Hickey, Keith Taylor

ELIZABETH HICKEY

(MCom(Hons), FCA, MInstD, MNZM)

Liz Hickey is a chartered accountant and member of the Institute of Directors who joined the Southern Cross Board in October 2009. Ms Hickey is president of the Institute of Chartered Accountants (NZICA), a director of Diabetes New Zealand Inc., a co-opted member of the ASB Community Trust's Audit and Risk Committee, and a Trustee of Southern Cross Health Trust. Her past governance experience includes being a director of Radio New Zealand, Genesis Power and Environmental Science and Research. She has served on both the New Zealand and international boards of the World Association of Girl Guides and Girl Scouts. She is a Fellow of the NZICA.

PHILLIP MEYER

(FAIM, FNZIM, AF Inst D, F Fin)

Phillip Meyer is an experienced company director and investment banker who joined the Southern Cross Board in June 2002. He is also a Society Trustee and Chairman of its Investment Committee. He is chairman of Australian Financial Services Group and Institute of Directors (Wellington Branch) and a trustee of Young Enterprise Trust, Crimestoppers Trust and Zealandia. Mr Meyer is a Trustee of Southern Cross Health Trust, Chairman of the Trust's Audit Committee and a Director of Trust subsidiary companies. He is a national councillor and Accredited Fellow of the Institute of Directors in NZ; and a member of the NZ Markets Disciplinary Tribunal, Financial Services Institute of Australasia and the Returned Services Association Executive Management Committee. He is also national chairman of the Salvation Army Red Shield Appeal Committee and a member of its Investment Committee.

KEITH TAYLOR

(BSc, BCA, FIA, F Inst D)

Keith Taylor was elected to the Southern Cross Board in November 2010 and has over 30 years' experience in the insurance and financial services industries as a chief executive, chief financial officer and actuary. He is chair of the Government Superannuation Fund, Gough Gough & Hamer and Speirs Group, and deputy chair of the Earthquake Commission. He is a director of the Reserve Bank of New Zealand, Port Marlborough and Butland Holdings. He is a Trustee of the Southern Cross Health Trust and a member of the Carey Baptist College Board. He has previously been a director of property, insurance, trustee and investment companies in both New Zealand and Australia.

Director meeting attendance for the year ended 30 June 2013

	Society Board	AGM	Trustees	Strategic Workshops	Audit Committee	Remuneration Committee	Nomination Committee	Investment Committee	Group Strategic Meetings
GS Hawkins	9	1	4	1	6	5	3	4	8
Dr DD Baird	8			1		5	3		8
Ms CB Durbin	9	1	4	1		5	3	4	8
GW Gent	8	1		1		5	3		8
Ms EM Hickey	9	1			6				8
PJ Meyer	9	1	4	1	6			4	8
KB Taylor	9	1			6			4	8

Financial statements

STATEMENTS OF COMPREHENSIVE INCOME
for the year ended 30 June 2013

	NOTE	GROUP		SOCIETY	
		2013 $000	2012 $000	2013 $000	2012 $000
Premium revenue		725,483	706,834	725,483	706,834
Net claims expense	3	639,053	605,528	639,053	605,528
Underwriting surplus		86,430	101,306	86,430	101,306
Operating expenses	4	87,022	85,937	86,234	84,254
Operating surplus/(deficit)		(592)	15,369	196	17,052
Net investment and other income	5	21,939	23,585	21,910	21,917
Surplus before taxation		21,347	38,954	22,106	38,969
Taxation	6	–	–	–	–
Surplus after taxation		21,347	38,954	22,106	38,969
Other comprehensive income		–	–	–	–
Total comprehensive surplus for the year		21,347	38,954	22,106	38,969

The accompanying notes form part of these financial statements

STATEMENTS OF CHANGES IN RESERVES
for the year ended 30 June 2013

GROUP 2013	Retained Surpluses $000	Total Reserves $000
Opening balance	373,386	373,386
Total comprehensive surplus:		
Surplus after taxation	21,347	21,347
Other comprehensive income	–	–
Total comprehensive surplus	21,347	21,347
Closing balance	394,733	394,733

GROUP 2012	Retained Surpluses $000	Total Reserves $000
Opening balance	334,432	334,432
Total comprehensive surplus:		
Surplus after taxation	38,954	38,954
Other comprehensive income	–	–
Total comprehensive surplus	38,954	38,954
Closing balance	373,386	373,386

The accompanying notes form part of these financial statements

STATEMENTS OF CHANGES IN RESERVES (continued)
for the year ended 30 June 2013

SOCIETY 2013	Retained Surpluses $000	Total Reserves $000
Opening balance	373,268	373,268
Total comprehensive surplus:		
Surplus after taxation	22,106	22,106
Other comprehensive income	–	–
Total comprehensive surplus	22,106	22,106
Closing balance	395,374	395,374

SOCIETY 2012	Retained Surpluses $000	Total Reserves $000
Opening balance	334,299	334,299
Total comprehensive surplus:		
Surplus after taxation	38,969	38,969
Other comprehensive income	–	–
Total comprehensive surplus	38,969	38,969
Closing balance	373,268	373,268

The accompanying notes form part of these financial statements

STATEMENTS OF FINANCIAL POSITION
as at 30 June 2013

	NOTE	GROUP 2013 $000	GROUP 2012 $000	SOCIETY 2013 $000	SOCIETY 2012 $000
Assets					
Cash and cash equivalents		2,258	3,692	2,130	3,586
Premium and other receivables	7	64,897	63,690	65,392	63,449
Investments	8	492,035	468,863	492,034	468,861
Investment in subsidiaries	9	–	–	–	–
Property and equipment	10	11,452	13,484	11,452	13,484
Intangible assets	11	11,259	9,142	11,259	9,142
Total assets		581,901	558,871	582,267	558,522
Liabilities					
Payables	12	18,252	22,393	17,977	22,162
Employee benefits	13	9,362	8,537	9,362	8,537
Insurance contract liabilities	14	159,554	154,555	159,554	154,555
Total liabilities		187,168	185,485	186,893	185,254
Net assets		394,733	373,386	395,374	373,268
Reserves		394,733	373,386	395,374	373,268

For and on behalf of the Board

G S Hawkins, **Chairman** Date: 3 September 2013

E M Hickey, **Director** Date: 3 September 2013

The accompanying notes form part of these financial statements

STATEMENTS OF CASH FLOWS
for the year ended 30 June 2013

	NOTE	GROUP 2013 $000	GROUP 2012 $000	SOCIETY 2013 $000	SOCIETY 2012 $000
Cash flows from/(to) operating activities					
Premium revenue		725,905	705,067	725,905	705,067
Interest received		21,141	22,457	21,137	22,435
Other income		173	1,983	148	44
Payment of claims		(639,170)	(603,322)	(639,170)	(603,322)
Payments to employees		(38,697)	(38,776)	(38,579)	(37,028)
Payments to suppliers		(42,521)	(34,772)	(42,231)	(34,495)
Net cash flows from/(to) operating activities	18	26,831	52,637	27,210	52,701
Cash flows from/(to) investing activities					
Proceeds from sale of property and equipment		405	7,952	5	7,952
Payments for property and equipment		(799)	(1,206)	(799)	(1,206)
Payments for intangible assets		(4,910)	(5,305)	(4,910)	(5,305)
Net payments for investments		(22,961)	(51,624)	(22,962)	(51,622)
Net advances to subsidiaries		–	–	–	(94)
Net cash flows from/(to) investing activities		(28,265)	(50,183)	(28,666)	(50,275)
Net increase/(decrease) in cash and cash equivalents		(1,434)	2,454	(1,456)	2,426
Opening cash and cash equivalents		3,692	1,238	3,586	1,160
Closing cash and cash equivalents		2,258	3,692	2,130	3,586

The accompanying notes form part of these financial statements

1. STATEMENT OF ACCOUNTING POLICIES

REPORTING ENTITY

The Southern Cross Medical Care Society (the "Society") is a friendly society domiciled in New Zealand, registered under the Friendly Societies and Credit Unions Act 1982.

The Society's registered office is Level 1, Ernst & Young Building, 2 Takutai Square, Auckland.

Financial statements for the Society and consolidated financial statements are presented. The consolidated financial statements as at, and for the year ended, 30 June 2013 comprise the Society and its subsidiaries: Southern Cross Health Services Limited, Southern Cross Healthcare Limited (non-trading) and Activa Health Limited (together referred to as the "Group").

The statutory base for the Society is the Friendly Societies and Credit Unions Act 1982 and the Insurance (Prudential Supervision) Act 2010 ("IPSA"). The statutory base for the subsidiaries is the Companies Act 1993 and the Financial Reporting Act 1993.

The Society was granted a licence by the Reserve Bank of New Zealand ("RBNZ") on 21 February 2013 to operate as an insurer subject to the IPSA. As a consequence of being a licensed insurer, the Society is deemed to be an issuer under the Financial Reporting Act 1993 from 1 July 2012.

The Society's primary activity is the provision of health insurance.

BASIS OF PREPARATION

The financial statements have been prepared in accordance with New Zealand generally accepted accounting practice ("NZ GAAP") and the requirements of IPSA.

Under the specific criteria and definitions of the financial reporting standards, the Directors have classified the Society as a profit-oriented entity for financial reporting purposes.

The financial statements comply with New Zealand equivalents to International Financial Reporting Standards ("NZ IFRS") and International Financial Reporting Standards ("IFRS").

The statements of financial position have been presented in the order of decreasing liquidity.

The financial statements were approved by the Board of Directors on 3 September 2013.

BASIS OF MEASUREMENT

The financial statements are prepared on the historical cost basis except that the following are stated at their fair value: investments, cash and insurance contract liabilities.

FUNCTIONAL AND PRESENTATION CURRENCY

These financial statements are presented in New Zealand dollars ($), which is the Group's functional and presentation currency. All financial information presented in New Zealand dollars has been rounded to the nearest thousand, unless otherwise stated.

USE OF ESTIMATES AND JUDGEMENTS

The preparation of financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised.

Information about significant areas of estimation, uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amounts recognised in the financial statements are described in the following notes:

- Note 14: Insurance contract liabilities
- Note 15: Actuarial information
- Note 16: Risk management
- Note 20: Solvency and capital adequacy

The accounting policies set out below have been applied consistently, by all Group entities, to all periods presented in these financial statements.

BASIS OF CONSOLIDATION

Subsidiaries are all entities over which the Group has the power to govern the financial and operating policies, generally by holding more than half of the voting rights. The financial statements of subsidiaries are included in the Group financial statements from the date that control commences until the date that control ceases.

All intra-group balances and transactions are eliminated in preparing the Group financial statements.

1. STATEMENT OF ACCOUNTING POLICIES (CONTINUED)

CASH AND CASH EQUIVALENTS

Cash and cash equivalents comprise cash on hand and current account balances in bank accounts. Under the NZ IFRS definition of financial assets, cash and cash equivalents are classified as "financial assets at fair value through profit or loss".

PREMIUM AND OTHER RECEIVABLES

Premium and other receivables are stated at their cost less any impairment losses. Impairment losses for uncollectible premiums are written off against premium revenue in the year in which they are incurred. Under the NZ IFRS definition of financial assets, premium and other receivables are classified as "loans and receivables".

INVESTMENTS

Investments are purchased with the intention of being held until maturity.

All purchases of investments are recognised on the date at which they are originated. Transaction costs are recognised as an expense in determining the surplus or deficit before tax in the statements of comprehensive income on transaction date. Investments are de-recognised on the date of maturity or sale of an investment.

The Group designates its investments as "financial assets at fair value through profit or loss" at inception. That is, changes in fair value are recognised in determining the surplus or deficit before tax in the statements of comprehensive income.

Fair value is determined using a three-level fair value hierarchy that reflects the significance of the inputs used in measuring fair values of financial assets and liabilities. The hierarchy is described in Note 16 "Risk Management".

As the intention is for investments to be held to maturity, and then reinvested, only the net purchased or matured amounts are disclosed in the statements of cash flows.

INVESTMENT IN SUBSIDIARIES

Investment in subsidiaries is stated at cost less impairment losses.

PROPERTY AND EQUIPMENT

Items of property and equipment are measured at cost, less accumulated depreciation and impairment losses.

Where material components of an item of property or equipment have different useful lives, they are accounted for as separate items.

Subsequent expenditure that replaces a component, or enhances the item of property or equipment, is added to the carrying amount of an item of property or equipment when that cost is incurred, if it is probable that the future economic benefits embodied within the item will flow to the Group and the cost of the item can be measured reliably. All other costs are recognised as an expense in determining the surplus or deficit before tax in the statements of comprehensive income.

Capital expenditure on major projects is initially recorded as work in progress. On completion of the project the asset is transferred to the appropriate asset category. Work in progress is not depreciated.

Depreciation is recognised in determining the surplus or deficit before tax in the statements of comprehensive income on a straight-line basis over the estimated useful lives of each component of property or equipment as follows:

- Computer equipment 25% - 33% per annum
- Other fixed assets 15% - 20% per annum
- Leasehold improvements 10% - 33% per annum

The estimated useful life of assets is reassessed annually.

1. STATEMENT OF ACCOUNTING POLICIES (CONTINUED)

INTANGIBLE ASSETS

Computer software is recognised as an intangible asset when it is not an integral part of the computer hardware. Software development expenditure that meets the criteria for recognition as an intangible asset is capitalised and amortised over its expected useful life, subject to impairment testing. Costs incurred in researching and evaluating a project up to the point of formal commitment to a project are treated as research costs and are expensed as incurred. All capitalised costs are deemed to have an expected useful life of five years unless it can be clearly demonstrated that the net benefits are to be generated over either a longer or shorter period. The capitalised costs are amortised on a straight line basis over the period following completion of a project or implementation of part of a project.

The recoverability of the carrying amount of the asset is reviewed at each reporting date by determining whether there is an indication that the carrying value may be impaired. If any such indication exists, the item is tested for impairment by comparing the recoverable amount of the asset to its carrying value.

An impairment loss is recognised whenever the carrying value exceeds the recoverable amount. Impairment losses are recognised in determining the surplus or deficit before tax in the statements of comprehensive income and may be reversed where there has been a change in the estimates used to determine the recoverable amount.

FOREIGN CURRENCY TRANSACTIONS

Transactions in foreign currencies that are settled in the reporting period are translated at the settlement rate. Transactions in foreign currency that are not settled in the reporting period, resulting in monetary assets and liabilities denominated in foreign currencies at the end of the reporting period, are translated to New Zealand dollars at the foreign exchange rate ruling at the reporting date. Foreign exchange differences arising on their translation are recognised in determining the surplus or deficit before tax in the statements of comprehensive income.

IMPAIRMENT

The carrying amounts of assets are reviewed at the end of each reporting period to determine whether there is any objective evidence of impairment. If any such indication exists, the asset's recoverable amount is estimated.

The estimated recoverable amount of an asset is the greater of: fair value less costs to sell, and value in use.

An impairment loss is recognised whenever the carrying amount of an asset exceeds its recoverable amount. Impairment losses directly reduce the carrying amount of the asset and are recognised in determining the surplus or deficit before tax in the statements of comprehensive income.

INSURANCE CONTRACTS

Insurance contracts are defined as those containing significant insurance risk at the inception of the contract.

Once a contract has been classified as an insurance contract, it remains an insurance contract for the remainder of its lifetime, even if the insurance risk reduces significantly during the period.

The Society has determined that all health insurance policies provided to members are insurance contracts.

INCOME RECOGNITION

Premiums

Gross earned premiums from insurance contracts are recognised evenly over the current billing period of the contract. Revenue is recognised on the date from which the policy is effective. Premiums billed but unearned are recorded as an unearned premium liability in the statements of financial position.

Fee and other income

Fees and other income are recognised as income evenly over the period in which the related services are performed.

Investment income

Interest income is recognised in determining the surplus or deficit before tax in the statements of comprehensive income as it accrues, and is calculated by using the effective interest rate method. Premiums and discounts that are an integral part of the effective yield of the investment are recognised as an adjustment to the effective interest rate of the instrument.

Realised and unrealised gains and losses on investments, recorded in determining the surplus or deficit before tax in the statements of comprehensive income, include gains and losses on financial assets classified as financial assets at fair value through profit or loss.

1. STATEMENT OF ACCOUNTING POLICIES (CONTINUED)

LEASES

Leases are defined as an operating lease where they do not transfer substantially all the risks and rewards incidental to ownership.

Payments made under operating leases are recognised in determining the surplus or deficit before tax in the statements of comprehensive income on a straight-line basis over the term of the lease.

Any inducement payments received as part of an operating lease agreement are deferred and recognised on a straight-line basis over the term of the lease.

POLICY ACQUISITION COSTS

The costs incurred in acquiring and recording insurance contracts may give rise to future benefits from premiums. Acquisition costs are initially recorded in determining the surplus or deficit before tax in the statements of comprehensive income. Any amounts that give rise to premiums in subsequent reporting periods are deferred as an asset and amortised over the period covered by the premium paid.

PAYABLES

Payables are stated at cost. Under the NZ IFRS definition of financial liabilities, payables are classified as "other liabilities at amortised cost".

NET CLAIMS EXPENSE

The net claims expense represents payments made on claims and the movements in the outstanding claims and unexpired risk provisions (as described below).

PROVISIONS

A provision is recognised when the Group has a present legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market rates and, where appropriate, the risks specific to the obligation.

OUTSTANDING CLAIMS PROVISION

The liability for outstanding claims comprises claims incurred but not settled at the reporting date, whether reported or not. A central estimate is made of claims reported but not paid, claims incurred but not reported and claims incurred but not adequately reported. The central estimate includes expected claim payments plus associated claims handling costs. In addition a risk margin is added to reflect the inherent uncertainty in the estimate of claims.

UNEXPIRED RISK PROVISION AND LIABILITY ADEQUACY TEST

A liability adequacy test is performed to assess whether there is any deficiency in the unearned premium liability arising from expected claims and administration costs during the period covered by the unearned premium. The test is performed on all the policies as a whole as risks are broadly similar and are managed together as a single portfolio. The central estimate of claims and administration expenses is calculated. In addition, a risk margin is added to reflect the inherent uncertainty in estimating the claims. The total is compared with the unearned premium liability. Any deficiency is recognised as an expense in determining the surplus or deficit before tax in the statements of comprehensive income after first writing down any deferred acquisition costs. The deficiency in excess of deferred acquisition costs is recognised in the statements of financial position as an unexpired risk provision.

1. STATEMENT OF ACCOUNTING POLICIES (CONTINUED)

EMPLOYEE BENEFITS

Employee entitlements

Employee entitlements represents the current obligation to employees in respect of outstanding salaries, leave entitlements and other short term benefits.

Employee benefits

The Group's net obligation in respect of long service leave is the amount of future benefits that employees have earned in return for their service in current and prior periods. The financial value of the obligation is calculated based on estimated future cash flows and is discounted to its present value.

In determining future cash flows, consideration is given to historical data with respect to employee departures, periods of service and estimated future increases in wage and salary rates. The discount rate is the market yield rate on relevant New Zealand Government stock at the end of the reporting period.

Post employment benefits

The Group's obligation for post employment entitlements comprises post retirement health insurance benefits. The financial value of the obligation is calculated as the present value of estimated future cash flows. In determining future cash flows, consideration is given to future increases in health insurance premiums and historical data with respect to employee departures, periods of service and mortality rates. The discount rate is the market yield rate on relevant New Zealand Government stock at the end of the reporting period.

INCOME TAX EXPENSE

The Society is exempt from income tax due to its status as a friendly society. However, the subsidiaries are subject to income tax.

For subsidiary companies the income tax expense comprises current and deferred tax and is recognised in the statements of comprehensive income. Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years. Deferred tax reflects the tax effect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available against which temporary differences can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

GOODS AND SERVICES TAX (GST)

The statements of comprehensive income and statements of cash flows have been prepared so that all components are stated exclusive of GST. All items in the statements of financial position are stated net of GST, with the exception of receivables and payables, which include GST invoiced.

CHANGE IN ACCOUNTING ESTIMATES

A change in an accounting estimate that gives rise to a change in an asset or liability is recognised by adjusting the carrying amount of the related asset or liability item in the period of the change. Other changes in accounting estimates are recognised prospectively in the statements of comprehensive income in the period of the change and future periods, as applicable.

2. NEW FINANCIAL REPORTING STANDARDS APPROVED BUT NOT YET EFFECTIVE

The following new or amended standards and interpretations, which are applicable to the Group, are not yet effective for the year ended 30 June 2013, and have not been applied in preparing these financial statements:

NZ IFRS 9 – Financial Instruments: Classification and Measurement (2009 and 2010)

NZ IFRS 13 – Fair Value Measurement

NZ IAS 19 – Employee Benefits

NZ IFRS 9 – Financial Instruments: Classification and Measurement (2009) is the first standard issued as part of a wider project to replace NZ IAS 39. It represents a significant change from the existing requirements in NZ IAS 39 – Financial Instruments: Recognition and Measurement, in respect of financial assets. The standard contains two primary measurement categories for financial assets (amortised cost and fair value), and eliminates the existing three NZ IAS 39 categories (held to maturity, available for sale, and loans and receivables). A financial asset would be measured at amortised cost if it is held to collect contractual cash flows of principal and interest on specified dates. All other financial assets would be measured at fair value.

NZ IFRS 9 – Financial Instruments: Classification and Measurement (2010) adds the requirements relating to classification and measurement of financial liabilities, and derecognition of financial assets and liabilities.

The above revisions to NZ IFRS 9 are effective for annual reporting periods beginning on or after 1 January 2015. The International Accounting Standards Board has deferred the mandatory effective date from the previous deadline of 1 January 2013. The impact of the requirements of this standard on the Group is still to be determined.

NZ IFRS 13 – Fair Value Measurement – defines fair value, establishes a framework for measuring fair value and sets out related disclosure requirements. It does not give rise to any new requirements as to when fair value measurements are required, but instead provides guidance currently included in individual IFRSs, with a single source of authoritative guidance on how to measure fair value.

NZ IFRS 13 is effective for annual reporting periods beginning on or after 1 January 2013. The impact of the requirements of this standard on the Group is still to be determined.

NZ IAS 19 Employment Benefits amends the definitions of short-term and long-term employee benefits, adds additional disclosures and changes the timing of recognition and measurement basis of certain employment benefits.

The above revisions to NZ IAS 19 are effective for annual reporting periods beginning on or after 1 January 2013. The impact of the requirements of this standard on the Group is still to be determined.

3. NET CLAIMS EXPENSE

	GROUP		SOCIETY	
	2013 $000	2012 $000	2013 $000	2012 $000
Claims incurred relating to risks borne in current financial year	638,655	605,488	638,655	605,488
Claims incurred relating to risks borne in previous financial years	(1,568)	(1,909)	(1,568)	(1,909)
Movement in provision for claims handling costs	725	(21)	725	(21)
Movement in risk margin	82	(22)	82	(22)
Net claims incurred	637,894	603,536	637,894	603,536
Movement in provision for unexpired risk	1,159	1,992	1,159	1,992
	639,053	605,528	639,053	605,528

4A. OPERATING EXPENSES

Operating expenses include	GROUP		SOCIETY	
	2013 $000	2012 $000	2013 $000	2012 $000
Auditor's remuneration:				
– Audit of financial statements	164	162	164	162
– Other services	116	145	116	145
Depreciation	3,119	3,208	3,119	3,206
Amortisation of intangible assets	2,793	2,738	2,793	2,735
Directors' fees	361	360	361	360
Employee benefits expense	39,521	39,598	39,403	37,850
Contributions to defined contribution plan	55	52	55	52
Rental of premises	4,524	4,729	4,524	4,723
Provision for impairment (gain)/loss on amounts receivable from subsidiaries	–	–	336	(52)
(Gains)/losses on disposal of property and equipment	(3)	(71)	(3)	(71)
(Gains)/losses on disposal of intangible assets	–	(329)	–	–

Auditor's remuneration for other services disclosed above consists of accounting and advisory services, reviewing regulatory returns and providing services at the AGM.

4B. OPERATING EXPENSES

Operating expenses consist of	GROUP		SOCIETY	
	2013 $000	2012 $000	2013 $000	2012 $000
Policy acquisition	9,223	9,118	9,223	9,118
Policy administration	30,889	30,946	30,889	30,946
Claims handling	10,011	9,036	10,011	9,036
Other operating expenses	36,899	36,837	36,111	35,154
	87,022	85,937	86,234	84,254

Other operating expenses consist of information technology, human resources, occupancy, governance, finance, actuarial, clinical and management expenses.

NOTES TO THE FINANCIAL STATEMENTS (continued)
for the year ended 30 June 2013

5. NET INVESTMENT AND OTHER INCOME

	GROUP 2013 $000	GROUP 2012 $000	SOCIETY 2013 $000	SOCIETY 2012 $000
Interest income	21,577	22,358	21,574	22,336
Net gains/(losses) on investments at fair value through profit or loss	210	(463)	210	(463)
Fee and other income	152	1,690	126	44
	21,939	23,585	21,910	21,917

6. TAXATION

Reconciliation of effective tax rate	GROUP 2013 $000	GROUP 2012 $000
Net surplus before tax	21,347	38,954
Income tax payable at the domestic tax rate of 28%	5,977	10,907
Effect of non-deductible expenses	–	1
Effect of exempt surplus	(6,284)	(10,896)
Tax effect of change in unrecognised temporary differences	(13)	64
Tax on current year deficit/(surplus) for which no deferred tax asset was recognised	320	–
Tax effect of prior year unrecognised tax losses utilised	–	(76)
	–	–

The aggregate amount of temporary differences arising in the subsidiaries for which a deferred tax asset has not been recognised is $344,000 at 30 June 2013 (30 June 2012: $392,000).

The Group has unrecognised tax losses carried forward of $32,000,000 at 30 June 2013 (30 June 2012: $30,856,000).

7. PREMIUM AND OTHER RECEIVABLES

	GROUP		SOCIETY	
	2013 $000	2012 $000	2013 $000	2012 $000
Premium accounts receivable	54,746	53,063	54,746	53,063
Interest receivable	4,150	3,713	4,150	3,713
Other accounts receivable	5,318	6,302	5,289	5,911
Amounts owed by related parties	655	212	1,179	762
Asset disposal proceeds receivable	28	400	28	–
	64,897	63,690	65,392	63,449

The fair value of premium and other receivables approximates the carrying amount.
Premium and other receivables is a current asset.

8. INVESTMENTS

At fair value through profit or loss	GROUP		SOCIETY	
	2013 $000	2012 $000	2013 $000	2012 $000
New Zealand Government stock	527	547	527	547
State owned enterprise bonds	20,402	28,558	20,402	28,558
Local authority stock	47,515	70,575	47,515	70,575
Other bonds	55,575	69,940	55,575	69,940
Bank deposits, commercial paper and floating rate notes	368,016	299,243	368,015	299,241
	492,035	468,863	492,034	468,861
Current assets	319,655	224,800	319,654	224,798
Non-current assets	172,380	244,063	172,380	244,063
	492,035	468,863	492,034	468,861

The New Zealand Government stock was held by the Public Trustee as a deposit required under the Insurance Companies' Deposits Act 1953 (repealed on 7 March 2012) until 5 April 2013, when it was returned to the Society as full licence holders are no longer required to hold such a deposit.

9. INVESTMENT IN SUBSIDIARIES

Investment in subsidiaries is stated at cost less impairment losses. Impairment losses arise as a result of the investment in subsidiaries being adjusted to the value of the net tangible assets of the subsidiaries. Investment in subsidiaries has now been fully impaired.

A provision for impairment has been made for loans and advances to subsidiaries to the extent the loans and advances exceed the net tangible assets of the subsidiaries.

The Directors have resolved to provide sufficient financial support as may be necessary to enable the subsidiary companies to trade as going concerns.

Investment in subsidiaries is a non-current asset.

On 28 June 2012, an unconditional agreement to dispose of the Care Advantage injury management business, owned by Southern Cross Health Services Limited, was entered into with Gallagher Bassett NZ Limited. Settlement occurred in early July 2012.

On 7 May 2013, the Society Directors resolved to discontinue the Activa product provided by Activa Health Limited effective as at 30 June 2013. There is no material effect on the Society's financial statements.

NOTES TO THE FINANCIAL STATEMENTS (continued)
for the year ended 30 June 2013

10. PROPERTY AND EQUIPMENT

	GROUP				
	Computer equipment $000	Other fixed assets $000	Leasehold improvements $000	Work in progress $000	Total $000
At 30 June 2013					
Cost	23,932	2,834	8,333	581	35,680
Accumulated depreciation	(21,194)	(949)	(2,085)	–	(24,228)
Closing balance	2,738	1,885	6,248	581	11,452
Reconciliation of movement in property and equipment					
Opening balance	3,868	2,035	7,100	481	13,484
Additions	359	285	27	446	1,117
Transfers from work in progress	346	–	–	(346)	–
Disposals	–	(30)	–	–	(30)
Depreciation	(1,835)	(405)	(879)	–	(3,119)
Closing balance	2,738	1,885	6,248	581	11,452

	GROUP				
	Computer equipment $000	Other fixed assets $000	Leasehold improvements $000	Work in progress $000	Total $000
At 30 June 2012					
Cost	23,159	2,596	8,306	481	34,542
Accumulated depreciation	(19,291)	(561)	(1,206)	–	(21,058)
Closing balance	3,868	2,035	7,100	481	13,484
Reconciliation of movement in property and equipment					
Opening cost	21,426	3,437	7,813	1,700	34,376
Opening accumulated depreciation	(17,559)	(445)	(345)	–	(18,349)
Opening balance	3,867	2,992	7,468	1,700	16,027
Additions	35	69	–	1,042	1,146
Transfers from work in progress	1,768	–	493	(2,261)	–
Disposals	–	(481)	–	–	(481)
Depreciation	(1,802)	(545)	(861)	–	(3,208)
Closing balance	3,868	2,035	7,100	481	13,484

10. PROPERTY AND EQUIPMENT (CONTINUED)

SOCIETY	Computer equipment $000	Other fixed assets $000	Leasehold improvements $000	Work in progress $000	Total $000
At 30 June 2013					
Cost	23,863	2,827	8,333	581	35,604
Accumulated depreciation	(21,125)	(942)	(2,085)	–	(24,152)
Closing balance	2,738	1,885	6,248	581	11,452
Reconciliation of movement in property and equipment					
Opening balance	3,868	2,035	7,100	481	13,484
Additions	359	285	27	446	1,117
Transfers from work in progress	346	–	–	(346)	–
Disposals	–	(30)	–	–	(30)
Depreciation	(1,835)	(405)	(879)	–	(3,119)
Closing balance	2,738	1,885	6,248	581	11,452

SOCIETY	Computer equipment $000	Other fixed assets $000	Leasehold improvements $000	Work in progress $000	Total $000
At 30 June 2012					
Cost	23,159	2,596	8,306	481	34,542
Accumulated depreciation	(19,291)	(561)	(1,206)	–	(21,058)
Closing balance	3,868	2,035	7,100	481	13,484
Reconciliation of movement in property and equipment					
Opening cost	21,357	3,430	7,813	1,700	34,300
Opening accumulated depreciation	(17,490)	(440)	(345)	–	(18,275)
Opening balance	3,867	2,990	7,468	1,700	16,025
Additions	35	69	–	1,042	1,146
Transfers from work in progress	1,768	–	493	(2,261)	–
Disposals	–	(481)	–	–	(481)
Depreciation	(1,802)	(543)	(861)	–	(3,206)
Closing balance	3,868	2,035	7,100	481	13,484

Other fixed assets include motor vehicles and office equipment.
Property and equipment is a non-current asset.

11. INTANGIBLE ASSETS

	GROUP		
	Computer software $000	Work in progress $000	Total $000
At 30 June 2013			
Cost	38,355	2,855	41,210
Accumulated amortisation	(29,951)	–	(29,951)
Closing balance	8,404	2,855	11,259
Reconciliation of movement in intangible assets			
Opening balance	6,867	2,275	9,142
Additions	2,587	2,323	4,910
Transfers from work in progress	1,743	(1,743)	–
Amortisation	(2,793)	–	(2,793)
Closing balance	8,404	2,855	11,259

	GROUP		
	Computer software $000	Work in progress $000	Total $000
At 30 June 2012			
Cost	34,025	2,275	36,300
Accumulated amortisation	(27,158)	–	(27,158)
Closing balance	6,867	2,275	9,142
Reconciliation of movement in intangible assets			
Opening cost	29,393	1,639	31,032
Opening accumulated amortisation	(24,470)	–	(24,470)
Opening balance	4,923	1,639	6,562
Additions	167	5,151	5,318
Transfers from work in progress	4,515	(4,515)	–
Amortisation	(2,738)	–	(2,738)
Closing balance	6,867	2,275	9,142

11. INTANGIBLE ASSETS (CONTINUED)

	SOCIETY		
	Computer software $000	Work in progress $000	Total $000
At 30 June 2013			
Cost	38,246	2,855	41,101
Accumulated amortisation	(29,842)	–	(29,842)
Closing balance	8,404	2,855	11,259
Reconciliation of movement in intangible assets			
Opening balance	6,867	2,275	9,142
Additions	2,587	2,323	4,910
Transfers from work in progress	1,743	(1,743)	–
Amortisation	(2,793)	–	(2,793)
Closing balance	8,404	2,855	11,259

	SOCIETY		
	Computer software $000	Work in progress $000	Total $000
At 30 June 2012			
Cost	33,916	2,275	36,191
Accumulated amortisation	(27,049)	–	(27,049)
Closing balance	6,867	2,275	9,142
Reconciliation of movement in intangible assets			
Opening cost	29,235	1,639	30,874
Opening accumulated amortisation	(24,315)	–	(24,315)
Opening balance	4,920	1,639	6,559
Additions	167	5,151	5,318
Transfers from work in progress	4,515	(4,515)	–
Amortisation	(2,735)	–	(2,735)
Closing balance	6,867	2,275	9,142

Intangible assets is a non-current asset.

The majority of the computer software and work in progress are internally generated.

Impairment losses arise from software development projects that do not have a positive quantifiable financial benefit. Where indicators of impairment exist, the future financial benefit is recalculated using a net present value analysis. Where the net present value is not positive, impairment is recognised in determining the surplus or deficit before tax in the statements of comprehensive income.

12. PAYABLES

	GROUP		SOCIETY	
	2013 $000	2012 $000	2013 $000	2012 $000
Accounts payable	14,888	18,167	14,613	17,936
Amounts owed to related parties	–	428	–	428
Deferred income – lease inducement	3,364	3,798	3,364	3,798
	18,252	22,393	17,977	22,162
Current	15,322	19,029	15,047	18,798
Non-current	2,930	3,364	2,930	3,364
	18,252	22,393	17,977	22,162

13. EMPLOYEE BENEFITS

	GROUP		SOCIETY	
	2013 $000	2012 $000	2013 $000	2012 $000
Employee entitlements	5,762	5,137	5,762	5,137
Employee benefits	1,150	1,020	1,150	1,020
Post-employment benefits	2,450	2,380	2,450	2,380
	9,362	8,537	9,362	8,537
Current	5,934	5,325	5,934	5,325
Non-current	3,428	3,212	3,428	3,212
	9,362	8,537	9,362	8,537

14. INSURANCE CONTRACT LIABILITIES

	GROUP		SOCIETY	
	2013 $000	2012 $000	2013 $000	2012 $000
Provision for outstanding claims (refer note 14a)	75,321	73,608	75,321	73,608
Provision for unearned premium (refer note 14c)	74,915	72,828	74,915	72,828
Provision for unexpired risk (refer note 14d)	8,468	7,309	8,468	7,309
Other insurance provisions	850	810	850	810
	159,554	154,555	159,554	154,555

14. INSURANCE CONTRACT LIABILITIES (CONTINUED)

a. Provision for outstanding claims

	GROUP 2013 $000	GROUP 2012 $000	SOCIETY 2013 $000	SOCIETY 2012 $000
Central estimate of outstanding claims liability	68,946	68,040	68,946	68,040
Claims handling costs	2,788	2,063	2,788	2,063
Risk margin	3,587	3,505	3,587	3,505
Closing balance	75,321	73,608	75,321	73,608

Claims are predominantly short-term in nature and are generally settled within twelve months of being incurred. Accordingly, amounts are not discounted.

b. Reconciliation of movement in provision for outstanding claims

	GROUP 2013 $000	GROUP 2012 $000	SOCIETY 2013 $000	SOCIETY 2012 $000
Opening balance	73,608	74,077	73,608	74,077
Amounts utilised during the year	(64,440)	(64,790)	(64,440)	(64,790)
Additional provision/(reversal of unused provision)	(1,568)	(1,909)	(1,568)	(1,909)
Amounts provided during the year	66,914	66,273	66,914	66,273
Movement in claims handling costs	725	(21)	725	(21)
Movement in risk margin	82	(22)	82	(22)
Closing balance	75,321	73,608	75,321	73,608

c. Reconciliation of movement in provision for unearned premium

	GROUP 2013 $000	GROUP 2012 $000	SOCIETY 2013 $000	SOCIETY 2012 $000
Opening balance	72,828	70,976	72,828	70,976
Premiums written in the year	727,570	708,686	727,570	708,686
Premiums earned during the year	(725,483)	(706,834)	(725,483)	(706,834)
Closing balance	74,915	72,828	74,915	72,828

14. INSURANCE CONTRACT LIABILITIES (CONTINUED)

d. Provision for unexpired risk

	GROUP 2013 $000	GROUP 2012 $000	SOCIETY 2013 $000	SOCIETY 2012 $000
Present value of expected future cash flows for claims and expenses	80,567	77,493	80,567	77,493
Risk margin	3,223	3,100	3,223	3,100
Unearned premiums	(74,915)	(72,828)	(74,915)	(72,828)
Write-down of deferred acquisition costs	(407)	(456)	(407)	(456)
Closing balance	8,468	7,309	8,468	7,309

e. Reconciliation of movement in provision for unexpired risk

	GROUP 2013 $000	GROUP 2012 $000	SOCIETY 2013 $000	SOCIETY 2012 $000
Opening balance	7,309	5,317	7,309	5,317
Reversal of opening balance	(7,309)	(5,317)	(7,309)	(5,317)
Net liability for unexpired risk recognised during the year	5,652	4,665	5,652	4,665
Risk margin	3,223	3,100	3,223	3,100
Write-down of deferred acquisition costs	(407)	(456)	(407)	(456)
Closing balance	8,468	7,309	8,468	7,309

15. ACTUARIAL INFORMATION

Estimates of the outstanding claims and unexpired risk as at 30 June 2013 have been determined by John Smeed, a Fellow of the New Zealand Society of Actuaries. These were presented to the Directors of the Society in a report dated 20 August 2013. There were no qualifications to the report. The calculations of the provisions for outstanding claims and unexpired risk each comply with both NZ IFRS 4: Insurance Contracts, and Professional Standard No. 4: General Insurance Business, of the New Zealand Society of Actuaries.

The actuary is satisfied as to the nature, sufficiency and accuracy of the data used to determine these provisions.

a. Outstanding claims provision

Outstanding claims liabilities are assessed as the central estimate of the present value of expected future payments for claims incurred but not settled at 30 June 2013, whether reported or not, together with related claims handling costs and an additional risk margin to allow for the inherent uncertainty in the central claims estimate. The central estimate of the outstanding claims has been calculated using historical experience to determine the pattern of claims development.

A projected payment per member method has been adopted for estimating outstanding claims payments. Calculations are based on recent claims experience. Payment per member factors are selected to achieve a sensible progression of past incurred claims.

15. ACTUARIAL INFORMATION (CONTINUED)

Estimation of outstanding claims liabilities includes an allowance for claims incurred but not reported, claims incurred but not adequately reported, unpaid reported claims and future claims handling costs associated with paying claims. An explicit allowance of $0.75m has been made for expected ACC recoveries as at 30 June 2013 (30 June 2012: $0.75m).

A risk margin has been added to reflect the inherent uncertainty in the central estimate. An analysis of the volatility of the historical experience has been used in determining the risk margin. Future volatility is assumed to be consistent with historical volatility. A risk margin of 5% of the central estimate was established at 30 June 2013 (30 June 2012: 5%). The risk margin was determined with the objective of achieving at least 75% probability of sufficiency of the outstanding claims provision.

Key assumptions:

1. Future patterns of claims development will be similar to historical patterns depending on the type of policy, type of claim and development month.
2. Monthly seasonality factors used for claims incurred. These were calculated from the 5 years' previous claims experience, and range from 71% to 113% (30 June 2012: 73% to 113%) of the monthly average.
3. Historical claims inflation 7.0% p.a. (30 June 2012: 5.0%), based on previous claims experience.

Claims handling costs include internal and external costs incurred in connection with the negotiation and settlement of claims. Internal costs include all direct expenses of the claims department and any part of the general administrative costs directly attributable to the claims function. Claims handling costs were determined to be 4% (30 June 2012: 3%) of the underlying claims amounts based on an analysis of administration expenses.

The average weighted term from 30 June 2013 to the expected settlement date for claims included in the liability for outstanding claims is 75 days (30 June 2012: 72 days). Accordingly, expected future payments are not discounted due to the short tail nature of the liabilities.

b. Unexpired risk provision and liability adequacy test

A liability adequacy test was performed to determine whether the unearned premium liability is adequate to cover the present value of the expected future cash flows arising from rights and obligations under current insurance contracts, plus an additional risk margin to reflect the inherent uncertainty in the central estimate. The future cash flows are future claims, associated claims handling costs and other administration costs relating to the business.

If the present value of the expected future cash flows plus the additional risk margin to reflect the inherent uncertainty in the central estimate exceeds the unearned premium liability less related intangible assets and related deferred acquisition costs then the unearned premium liability is deemed to be deficient.

The unexpired risk liability has been calculated as the projected premium deficiency for current in-force business until the next policy billing date on or after 1 July 2013.

The calculation of the risk margin has been based on an analysis of the volatility of historical claims experience within the time period covered by the unearned premiums. A risk margin of 4% of the present value of expected future cash flows has been applied at 30 June 2013 (30 June 2012: 4%). The risk margin was determined with the objective of achieving at least 75% probability of sufficiency of the unexpired risk liability.

Key assumptions:

1. Monthly seasonality factors used for claims incurred. These were calculated from the 5 years' previous claims experience, and range from 74% to 111% (2012: 73% to 109%) of the monthly average.
2. Projected claims inflation of 7% p.a., plus 4% for the effect of ageing, based on current expectations (2012: 7% plus 4%).
3. Expenses based on the business plan for 2013/14, including allowance for amortisation of deferred acquisition costs.

No explicit allowance has been made for cancellations or transfers. These are allowed for implicitly in the inflation assumption.

Expected future payments are not discounted due to the short tail nature of the liabilities.

16. RISK MANAGEMENT

The Group is exposed to a number of risks in the normal course of business. Primarily there are the risks associated with underwriting an insurance business (insurance risk). Other risks include financial risks (credit risk and liquidity risk), market risks (interest rate risk and foreign currency risk), and non-financial risks (operational risk and compliance risk). The Directors and management recognise the importance of having an effective risk management policy in place. The new Insurance Prudential Supervision regime requires insurers to maintain a risk management policy, which the RBNZ will assess for appropriateness. The risks and any objectives, policies and processes to manage these insurance and financial risks are described below.

a. Insurance risk

The Group assumes insurance risk through its health insurance activities. The key risk arises in respect of claims costs and, in particular, those costs varying from what was assumed in the setting of premium rates.

I. Risk management objectives, policies and processes for mitigating risk

The primary objective in managing risk is, as far as possible, to reduce the magnitude and volatility of claims costs. A secondary objective is to ensure funds are available to pay claims and maintain the solvency of the business if there is adverse deviation in experience. Key policies and methods for mitigating risk include:

- Underwriting policies and processes which evaluate new risks and offer terms that do not endanger the portfolio.
- Strict claims management procedures to ensure the payment of claims is in accordance with policy conditions.
- A long-term pricing strategy adopted by the Board which supports pricing based on underlying risk.
- Regular monitoring of financial and operating results and detailed investigations into the morbidity and persistency experience of the portfolio.
- Maintaining a target solvency margin in excess of the minimum required by the standard established by the RBNZ. The solvency margin ensures the Society is able to withstand a period of adverse insurance or investment experience and still maintain a satisfactory financial position (refer to note 20).

II. Sensitivity to insurance risk

The financial results of the Society are primarily affected by the level of claims incurred relative to that implicit in the premiums. The assumptions used in the valuation of the outstanding claims provision and the liability adequacy test directly affect the level of estimated claims incurred. The key assumptions used are detailed in note 15.

The scope of insurance risk is managed by the terms and conditions of the policy. The main insurance benefit involves the reimbursement of medical and surgical expenses depending upon the plan option.

The level of benefits specified in the contract is a key determinant of the amount of future claims although the exact level of claims is uncertain.

Other variables affecting the level of claims include the underlying morbidity of the lives insured, the nature of treatment given and the costs of treatment.

III. Concentration of insurance risk

Management defines concentration of risk by type of insurance business and geographic region. The Society transacts health insurance business in New Zealand and, therefore, the concentration of risk by type of insurance and geographic region cannot be avoided. Insurance risks are well diversified within the health insurance portfolio with claims costs spread across many different types of surgery and medical events. There is no significant exposure to individual large claims.

b. Financial risks

I. Credit risk

In the normal course of its business the Group incurs credit risk from its health insurance operations and from investment in financial assets.

The Group maintains a credit policy which is used to manage the exposure to credit risk. Limits on counter-party exposures have been set and are monitored on an ongoing basis. In addition, the RBNZ has issued concentration risk limits, as part of its solvency standards. The credit quality of counter-parties is assessed based on published credit ratings issued by Standard & Poor's or equivalent ratings agencies. Where local authorities do not have a formal credit rating, comfort is obtained from their ability to levy rates. There are no concentrations of credit risk at 30 June 2013 (2012: nil) in excess of policy.

16. RISK MANAGEMENT (CONTINUED)

The credit quality of investment counter-parties is as follows:

	GROUP 2013 $000	GROUP 2012 $000	SOCIETY 2013 $000	SOCIETY 2012 $000
AAA	266	438	266	438
AA	289,778	279,559	289,777	279,557
A	93,812	81,225	93,812	81,225
BBB	53,535	34,886	53,535	34,886
Non-rated	54,644	72,755	54,644	72,755
	492,035	468,863	492,034	468,861

The maximum exposure to credit risk at the end of the reporting period is the amount of financial assets stated in the statements of financial position.

These exposures are net of any recognised provisions for impairment losses. The Group does not require any collateral or security to support financial assets due to the quality of the counter-party organisations.

The cash and cash equivalents balances are held with a counter-party rated AA– (30 June 2012: AA).

Premium receivables are due from a very large number of counter-parties, ranging from large corporates to individual members. Analysing these by credit quality would not be feasible, as the majority of counter-parties will be non-rated.

II. Liquidity risk

The Group is exposed to daily calls on its available cash resources from claims and administration expenses. Liquidity risk is the risk that payment of obligations may not be met in a timely manner at a reasonable cost. The Directors set limits on the minimum proportion of maturing funds available to meet such calls to cover claims and expenses at unexpected levels of demand.

The contractual maturities of investments are as follows:

	GROUP 2013 $000	GROUP 2012 $000	SOCIETY 2013 $000	SOCIETY 2012 $000
On call	7,027	3,214	7,026	3,212
0–6 months	186,372	148,426	186,372	148,426
7–12 months	126,257	73,159	126,257	73,159
1–2 years	62,729	102,340	62,729	102,340
2–5 years	96,473	121,469	96,473	121,469
Beyond 5 years	13,177	20,255	13,177	20,255
	492,035	468,863	492,034	468,861

The cash and cash equivalents are available on call. All premium receivables, and substantially all other receivables are due within one month of the end of the reporting period.

Financial liabilities are all short term or payable on demand. Investments could be liquidated at any time to settle liabilities.

16. RISK MANAGEMENT (CONTINUED)

c. Market risks

I. Foreign currency risk

At 30 June 2013, the Group had assets of $292,000 and no liabilities denominated in foreign currencies (30 June 2012: assets of $288,000 and no liabilities). Given that the foreign currency risk exposure is minimal, the Group does not enter into any derivative contracts to manage this risk.

II. Interest rate risk

The Group invests in both fixed and variable rate financial instruments such as bonds, commercial paper and floating rate notes. There is a risk that any movement in interest rates can have an effect on the profitability and cash flows of the Group. The Group maintains a spread of investment types and maturity profiles to mitigate this risk.

(i) Cash flow interest rate risk

The cash flows from the Group's investments in the short term are susceptible to changes in interest rates. However, as the majority of longer-term investments are fixed rate, and these investments are held until maturity, this exposure is mitigated. The following analysis shows the impact of any changes in interest rates on the cash flows:

	GROUP AND SOCIETY	
	2013 $000	2012 $000
Impact of increase in interest rates by 100 basis points on cash flows	1,152	1,464
Impact of decrease in interest rates by 100 basis points on cash flows	(1,152)	(1,464)

(ii) Fair value risk

The fair value of fixed rate investments can fluctuate depending on changes in interest rates. The Group's policy is to hold all investments until maturity. This eliminates any effects of fair value changes to the investments upon realisation, however unrealised fair value changes are recognised in determining the surplus or deficit before tax in the statements of comprehensive income for each period. The following analysis shows the impact of any changes in interest rates:

	GROUP AND SOCIETY	
	2013 $000	2012 $000
Impact of increase in interest rates by 100 basis points on surplus before taxation	(2,792)	(3,375)
Impact of decrease in interest rates by 100 basis points on surplus before taxation	2,859	3,462

(iii) Fair values of financial assets and financial liabilities

All financial assets and financial liabilities included in the statements of financial position are carried at amounts that approximate fair value.

The table below analyses financial assets measured at fair value at the end of the reporting period, by the level in the fair value hierarchy into which the fair value measurement is categorised.

Definition of the fair value hierarchy

Level 1: Valuation based on quoted market prices (unadjusted) in an active market.

Level 2: Valuation techniques based on observable market data, either directly (as prices) or indirectly (derived from prices).

Level 3: Valuation techniques not based on observable market data.

16. RISK MANAGEMENT (CONTINUED)

	GROUP			
30 June 2013	Level 1 $000	Level 2 $000	Level 3 $000	Total $000
New Zealand Government stock	527	–	–	527
State owned enterprise bonds	–	20,402	–	20,402
Local authority stock	–	47,515	–	47,515
Other bonds	–	55,575	–	55,575
Bank deposits, commercial paper and floating rate notes	7,027	360,989	–	368,016
Total investments	7,554	484,481	–	492,035

	GROUP			
30 June 2012	Level 1 $000	Level 2 $000	Level 3 $000	Total $000
New Zealand Government stock	547	–	–	547
State owned enterprise bonds	–	28,558	–	28,558
Local authority stock	–	70,575	–	70,575
Other bonds	–	69,940	–	69,940
Bank deposits, commercial paper and floating rate notes	3,214	296,029	–	299,243
Total investments	3,761	465,102	–	468,863

16. RISK MANAGEMENT (CONTINUED)

	SOCIETY			
30 June 2013	Level 1 $000	Level 2 $000	Level 3 $000	Total $000
New Zealand Government stock	527	–	–	527
State owned enterprise bonds	–	20,402	–	20,402
Local authority stock	–	47,515	–	47,515
Other bonds	–	55,575	–	55,575
Bank deposits, commercial paper and floating rate notes	7,026	360,989	–	368,015
Total investments	7,553	484,481	–	492,034

	SOCIETY			
30 June 2012	Level 1 $000	Level 2 $000	Level 3 $000	Total $000
New Zealand Government stock	547	–	–	547
State owned enterprise bonds	–	28,558	–	28,558
Local authority stock	–	70,575	–	70,575
Other bonds	–	69,940	–	69,940
Bank deposits, commercial paper and floating rate notes	3,212	296,029	–	299,241
Total investments	3,759	465,102	–	468,861

Investments were independently valued by Bancorp Treasury Services Limited at 30 June 2013 and 30 June 2012. Investments are valued based on closing market prices as reported to wholesale investors. Where closing market prices are not available for certain investments, for example private placements by local authorities in which the Society has participated, the value of these investments are based on observable inputs using quoted prices for similar instruments ensuring that all significant inputs are directly or indirectly observable from market data.

Cash and cash equivalents are valued using a level 1 basis (30 June 2012: level 1).

17. RELATED PARTIES

a. Identity and relationship of related parties:

• The Southern Cross Medical Care Society ("Society")	Parent
• Southern Cross Health Services Limited ("Health Services")	100% subsidiary of Society
• Activa Health Limited ("Activa")	100% subsidiary of Society
• Southern Cross Healthcare Limited (non-trading)	100% subsidiary of Society
• Directors of The Southern Cross Medical Care Society	Are Trustees of Southern Cross Health Trust
• Southern Cross Health Trust ("Trust")	Related party of Society
• Southern Cross Benefits Limited ("Benefits")	100% subsidiary of Trust
• Southern Cross Hospitals Limited ("Hospitals")	100% subsidiary of Trust
• Southern Cross Primary Care Limited ("Primary Care")	100% subsidiary of Trust

The Society and its subsidiaries, and the Trust and its subsidiaries, have 30 June reporting dates.

The Society and the Trust are separate legal entities operating at "arm's length".

The Society contracts healthcare services on behalf of its members from all providers, including Hospitals, on a contestable and contractual basis.

The Society charges Benefits a fee for enabling marketing opportunities to the membership. During the current financial year, the Society purchased an investment bond from Benefits for $1,015,000 (2012: nil), being the market value.

All Group and related parties provide their normal services to the other Group and related parties on normal commercial terms.

Some goods and services are purchased by the Group and other related parties on a combined basis. These costs are on-charged to the other related parties at cost.

All related party balances are payable on normal trading terms and unsecured. No related party transactions have taken place at nil or nominal value. No related party balances have been written off or forgiven during the year.

Included within related party receivables of the Society are amounts receivable from subsidiary companies which are payable on demand. However, these are not currently intended to be called for payment. Provision has been made for any receivables considered to be impaired. The provision is for $10,095,000 (30 June 2012: $9,759,000).

The amount of transactions between the Group entities are:

	PAYABLES		RECEIVABLES	
	2013 $000	2012 $000	2013 $000	2012 $000
Society	–	2,875	56	77
Health Services	–	14	–	66
Activa	56	63	–	2,809

The outstanding balances between the Group entities are:

	PAYABLES		RECEIVABLES	
	2013 $000	2012 $000	2013 $000	2012 $000
Society	–	5	524	571
Health Services	58	508	–	5
Activa	466	63	–	–

17. RELATED PARTIES (CONTINUED)

The amount of transactions with other related parties are:

	GROUP		SOCIETY	
	2013 $000	2012 $000	2013 $000	2012 $000
Sale of services	6,597	5,680	6,597	5,650
Purchase of services	242	292	242	292
Purchase of investments	1,015	–	1,015	–

The outstanding balances with other related parties are:

	GROUP		SOCIETY	
	2013 $000	2012 $000	2013 $000	2012 $000
Balances outstanding on sales	757	212	757	197
Balances outstanding on purchases	102	428	102	428

b. Remuneration of Directors

Directors' fees paid by the Society for the year ended 30 June 2013 were as follows:

Director	2013 Amount $	2012 Amount $
Dr D D Baird	45,250	44,250
C B Durbin	49,000	49,000
G W Gent – appointed 6 December 2011	45,250	26,125
G S Hawkins (Chairman)	80,000	80,000
E M Hickey	47,000	46,000
P J Meyer	48,500	48,500
K B Taylor	46,000	46,000
M J Verbiest – retired 6 December 2011	–	20,208
Trustee		
C B Durbin	–	–
G S Hawkins	–	–
P J Meyer	–	–

Where Directors are directors of subsidiary companies of the Society, they do not receive any fees for these appointments.

The Society provides Trustees and Directors with Directors' and Officers' liability insurance cover for liabilities to other parties that may arise from their positions as Trustees and Directors.

The Society does not provide loans or advances to Directors or Trustees.

17. RELATED PARTIES (CONTINUED)

c. Remuneration of key management personnel

	GROUP		SOCIETY	
	2013 $000	2012 $000	2013 $000	2012 $000
Salaries and other short-term benefits	2,721	2,713	2,721	2,713
Post-employment benefits	74	56	74	56

Key management personnel include the Chief Executive and senior executives.

The Society does not provide loans or advances to key management personnel. At each reporting date, there are amounts outstanding to key management personnel comprising salaries, earned leave and short term incentives.

18. RECONCILIATION OF NET SURPLUS WITH NET CASH FLOWS FROM OPERATING ACTIVITIES

	GROUP		SOCIETY	
	2013 $000	2012 $000	2013 $000	2012 $000
Net surplus after taxation	21,347	38,954	22,106	38,969
Add/(less) non-cash items:				
Depreciation	3,119	3,208	3,119	3,206
Amortisation of intangible assets	2,793	2,738	2,793	2,735
Provision for impairment loss on amounts receivable from subsidiaries	–	–	336	(52)
Add items classified as investing activities :				
(Gains)/losses on disposal of property and equipment	(3)	(71)	(3)	(71)
(Gains) on disposal of intangible assets	–	(329)	–	–
Net (gains)/losses on investments at fair value through profit or loss	(210)	463	(210)	463
Movement in receivables and payables relating to investing activities	(691)	(7,022)	(627)	(7,207)
Add/(less) movements in working capital items:				
Receivables	(1,207)	8,842	(1,943)	8,957
Payables	(4,141)	1,667	(4,185)	1,514
Other insurance provisions	40	(10)	40	(10)
Employee benefits	825	822	825	822
Provision for outstanding claims	1,713	(469)	1,713	(469)
Provision for unearned premium	2,087	1,852	2,087	1,852
Provision for unexpired risk	1,159	1,992	1,159	1,992
Net cash flows from operating activities	26,831	52,637	27,210	52,701

19. CREDIT RATING

On 23 October 2012 Standard & Poor's reaffirmed the Society's Insurer Financial Strength Rating at A+. On 2 July 2013 Standard & Poor's again reaffirmed the Society's Insurer Financial Strength Rating at A+ under its new global insurance industry rating methodology. This signifies the insurer "has strong financial security characteristics".

20. SOLVENCY AND CAPITAL ADEQUACY

The Society is a registered friendly society. As a consequence of its legal structure the Society has no recourse to external capital and therefore internally generated capital is of paramount importance. The Society's capital of $395.4 million (2012: $373.3 million) is equal to the reserves as disclosed in the financial statements.

From 31 December 2012, as a provisional licence holder, the Society was subject to new solvency margin requirements. From 21 February 2013, as a consequence of being a fully licensed insurer, the Solvency Standard for Non-life Insurance Business ("the solvency standard") issued by the RBNZ requires the Society to retain a solvency margin of greater than zero, meaning that the actual solvency capital position exceeds the minimum required under the solvency standard.

During the year ended 30 June 2013 the Society complied with all externally imposed capital requirements. At 30 June 2013 the solvency ratio (actual solvency capital divided by minimum solvency capital required) was 5.48.

The Directors' policy for managing capital is to have a strong capital base to establish security for members and enable the Society to conduct its business whilst maintaining financial soundness. The Society has embedded in its capital management framework the necessary tests to ensure continuous and full compliance with the solvency standard. The key internal benchmark is to maintain the solvency margin at between 35% and 45% of annualised premium income. At 30 June 2013 this margin was 42.56% of annualised premium income. The policy in respect of capital management is regularly reviewed by the Directors in line with the guidelines issued by the RBNZ.

21. LEASE COMMITMENTS

At 30 June 2013 commitments under operating leases in respect of payments due to be made in the following years were:

	GROUP		SOCIETY	
	2013 $000	2012 $000	2013 $000	2012 $000
Within 1 year	5,543	5,101	5,543	5,101
Between 1 and 2 years	5,050	4,677	5,050	4,677
Between 2 and 5 years	14,806	12,969	14,806	12,969
Greater than 5 years	14,267	15,798	14,267	15,798
	39,666	38,545	39,666	38,545

The major components of the lease commitments are the leases on the Auckland and Hamilton office premises.

The Society entered into an agreement to lease the Auckland premises in December 2009 for a lease term of 10 years, commencing 1 April 2011. The agreement to lease provides for a rental review every three years based on prevailing market rates at the time of review.

The Society entered into an agreement to lease new premises in Hamilton in March 2013 for a lease term of 9 years, commencing 2 September 2013. The agreement to lease provides for an annual 2.5% rent increase with every third review based on prevailing market rates at the time of review.

22. CAPITAL COMMITMENTS

The Group had capital commitments of $2,276,000 at 30 June 2013 (2012: $515,000).

23. CONTINGENT LIABILITIES

The Group had no contingent liabilities at 30 June 2013 (2012: Nil).

Independent auditor's report

To the Members of The Southern Cross Medical Care Society

KPMG

We have audited the accompanying financial statements of The Southern Cross Medical Care Society ("the Society") and the Group, comprising the Society and its subsidiaries, on pages 12 to 42. The financial statements comprise the statements of financial position as at 30 June 2013, the statements of comprehensive income, changes in reserves and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information, for both the Society and the Group.

Directors' responsibility for the Society and Group financial statements

The Directors are responsible for the preparation of Society and Group financial statements in accordance with generally accepted accounting practice in New Zealand and International Financial Reporting Standards that give a true and fair view of the matters to which they relate, and for such internal control as the Directors determine is necessary to enable the preparation of Society and Group financial statements that are free from material misstatement whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on these Society and Group financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing (New Zealand). Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the Society and Group financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the Society and Group financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Society and Group's preparation of the financial statements that give a true and fair view of the matters to which they relate 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 Society and Group's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates, as well as evaluating the presentation of the financial statements.

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

Our firm has also provided other services to the Society and Group in relation to general accounting and other services. Partners and employees of our firm may be members of the Society and deal with the Society and Group on normal terms within the ordinary course of trading activities of the business of the Society and Group. These matters have not impaired our independence as auditor of the Society and Group. The firm has no other relationship with, or interest in, the Society and Group.

Opinion

In our opinion the financial statements on pages 12 to 42:

- comply with generally accepted accounting practice in New Zealand;
- comply with International Financial Reporting Standards;
- give a true and fair view of the financial position of the Society and the Group as at 30 June 2013 and of the financial performance and cash flows of the Society and the Group for the year then ended.

KPMG

5 September 2013
Auckland

Appointed actuary’s report

To the Members of The Southern Cross Medical Care Society

finity

Review of Actuarial Information contained in the Financial Statements as at 30 June 2013

Finity Consulting Pty Limited (Finity) has been asked by Southern Cross Medical Care Society (Southern Cross) to carry out a review of the 30 June 2013 actuarial information contained in the financial statements and provide an opinion as to its appropriateness. John Smeed is an employee of Finity and is the Appointed Actuary to Southern Cross. Finity has no relationship with Southern Cross apart from the Appointed Actuary role.

Southern Cross’s policy is to seek and adopt the advice of the Appointed Actuary in respect of the actuarial information contained in its financial statements. We confirm that the financial statements as at 30 June 2013 have been prepared in accordance with this policy, and as such this satisfies the requirements of the Insurance (Prudential Supervision) Act 2010.

Having carried out the actuarial review, nothing has come to our attention that would lead us to believe that the actuarial information used in the financial statements or the determination of the solvency position for Southern Cross as at 30 June 2013 are inappropriate. No limitations were placed on us in performing our review, and all data requested was provided.

This report is being provided for the sole use of Southern Cross for the purpose stated above. It is not intended, nor necessarily suitable, for any other purpose and should only be relied on for the purpose for which it is intended.

John Smeed
Appointed Actuary
Fellow of the New Zealand Society of Actuaries

Jeremy Weight
Fellow of the New Zealand Society of Actuaries

3 September 2013

Notes

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Southern Cross
Health Society

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