SOUTHERN CROSS BENEFITS LIMITED

ANNUAL REPORT

FOR THE YEAR ENDED

30 JUNE 2013

CONTENTS

SOUTHERN CROSS BENEFITS LIMITED

ANNUAL REPORT DISCLOSURES
For the year ended 30 June 2013

The Board of Directors of Southern Cross Benefits Limited (the "Company") present their Annual Report including the Financial Statements of the Company for the year ended 30 June 2013.

Dividend	No Dividends were paid during the year ended 30 June 2013 and no Dividend is proposed.
Nature of business	The Company is in the business of providing a range of travel insurance products. The joint venture investment, Fusion Insurance Services Limited, did not trade during the year. The Company has a branch in Australia which provides outbound travel insurance in Australia. The Company also operates in the New Zealand Pet Insurance market.
Results	The Company recorded a profit of $977,000.
Register of Directors	C B Durbin G S Hawkins (Chairman) I B McPherson P J Meyer
Use of Company Information	The Board received no notices during the year from Directors requesting to use Company information received in their capacity as Directors which would not have been otherwise available to them.
Share Dealings	No Director acquired or disposed of any interest in shares in the Company during the year.
Directors' Remuneration	The Directors received no remuneration from the Company as set out in Note 18b to the financial statements.
Indemnity and Insurance	The Company has insured its Directors and Officers for liabilities to other parties that may arise from their positions as Directors and Officers.
Auditor	KPMG.

For and on behalf of the Board

G S Hawkins
Chairman

3-9-13 Date

P J Meyer
Director

3-9-13 Date

GOVERNANCE STATEMENT

The Directors of the Company ensure that robust corporate governance policies, practices and processes are in place. Responsibility for the day-to-day operation and administration of the Company 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. The Company maintains a healthy risk culture under the frameworks of formal risk management, compliance, capital, investment, and delegated authority policies. Management report on these and other operational matters in a monthly report to the Board.

The Board delegates certain powers, duties and responsibilities to the Risk, Audit, and Remuneration Committees. All four Directors of the Company are considered to be independent per RBNZ guidelines. No executives of the Company hold a seat on the Board. All Directors and senior managers are required to meet Fit & Proper standards as prescribed by company policy.

Some key functions of the Board include:

- ensuring the Company's goals are clearly established and that strategies and business plans are in place for achieving them
- ensuring the Company's financial statements are true and fair and otherwise conform with legal requirements
- identifying steps necessary to protect the Company's financial position and brand
- appointing the CEO
- monitoring the performance of management
- ensuring the Board and management adhere to high ethical standards

The Company employs a full-time Risk & Compliance Officer, who reports to the Compliance & Risk Manager who is also the Financial Controller. The CEO is also the Chief Risk Officer. The associated responsibilities with these roles is formally imbedded into the respective position descriptions. In addition, the Company engages PWC as their Internal Auditor (outsourced) and the Board and Audit Committee approve an annual plan for independent review of the key risk areas of the business.

The Company monitors on a monthly basis its compliance with prudential capital requirements in accordance with RBNZ and APRA regulatory requirements.

Profiles of the Company's Directors are noted below.

Graeme Hawkins
BSC, BCom, ACA, FInstD

Chairman

Graeme Hawkins has been a professional director for 20 years. He was appointed to the Southern Cross Benefits Board in November 2008. He is also Chairman of the Southern Cross Health Trust and Southern Cross Medical Care Society. He 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.

Carole Durbin
BCom, LLB(Hons), FInstD

Carole Durbin was appointed to the Southern Cross Benefits Board in August 2006. She is also a Trustee of the Southern Cross Health Trust and a Director of the Southern Cross Medical Care Society. 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.

Ian McPherson
MB, Ch. B, Dip Obst

Dr McPherson started his career as a GP. In the 1980's he worked for the International Red Cross in war zones. He has held roles as chief executive of the Bay of Plenty Health Board, worked in the Prime Minister's Department, for the Ministry of Health, as executive chairman for Aetna Health and as regional general manager of health for Allianz Asia Pacific Ltd.

Since 2002, Dr McPherson has held the position of CEO of the Southern Cross Healthcare Group and Medical Care Society. He was appointed to the Southern Cross Benefits Board in November 2008. He is currently president of the IFHP (International Federation of Health Plans) and holds director positions on the Boards of Work and Income, Mercy Angiography Ltd, Southern Cross Hospitals and Southern Cross Primary Care.

Phillip Meyer
FAIM, FNZIM, AF Inst D, F Fin

Phillip Meyer is an experienced company director and investment banker who joined the Southern Cross Benefits Board in June 2002. He is also Chairman of the Southern Cross Benefits Audit Committee, a Director of the Southern Cross Medical Care Society and a Trustee of the Southern Cross Health Trust. 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. 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.

Independent auditor's report

To the Shareholder of Southern Cross Benefits Limited

Report on the financial statements

We have audited the accompanying financial statements of Southern Cross Benefits Limited ("the company") on pages 6 to 36. The financial statements comprise the statement of financial position as at 30 June 2013, the statements of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Directors' responsibility for the financial statements

The directors are responsible for the preparation of 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 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 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 financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the 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 company'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 company'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 company in relation to general accounting and other services. Partners and employees of our firm may also deal with the company on normal terms within the ordinary course of trading activities of the business of the company. These matters have not impaired our independence as auditor of the company. The firm has no other relationship with, or interest in, the company.

KPMG

Opinion

In our opinion the financial statements on pages 6 to 36:

- 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 company as at 30 June 2013 and of its financial performance and cash flows for the year then ended.

Report on other legal and regulatory requirements

In accordance with the requirements of sections 16(1)(d) and 16(1)(e) of the Financial Reporting Act 1993, we report that:

- we have obtained all the information and explanations that we have required; and
- in our opinion, proper accounting records have been kept by Southern Cross Benefits Limited as far as appears from our examination of those records.

KPMG

4 September 2013

Auckland

STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME
for the year ended 30 June 2013

	Note	2013 $000	2012 $000
Premium revenue		44,611	44,101
Reinsurers' share of premium		(1,819)	(1,669)
Net premiums		42,792	42,432
Claims expense		23,875	22,674
Reinsurance claim recoveries		(22)	(469)
Net claims expense	2	23,853	22,205
Underwriting surplus		18,939	20,227
Operating expenses	3	19,008	17,096
Other operating income		(49)	(61)
Operating profit/(loss)		(20)	3,192
Investment and other income	4	1,001	1,322
Profit/(loss) before taxation		981	4,514
Taxation	5	4	(74)
Profit/(loss) after taxation		977	4,588
Other comprehensive income			
Movement on foreign currency translation reserve		(975)	(252)
Total comprehensive income for the year		2	4,336

The accompanying notes form part of these financial statements

KPMG

STATEMENT OF CHANGES IN EQUITY
for the year ended 30 June 2013

2013	Note	Share Capital $000	Retained Earnings $000	Foreign Currency Translation Reserve $000	Total Reserves $000
Opening balance		600	17,484	978	19,062
Total comprehensive income:					
Profit/(loss) after taxation		-	977	-	977
Other comprehensive income					
Movement on foreign currency translation reserve		-	-	(975)	(975)
Total comprehensive income			977	(975)	2
Transaction with owners					
Dividend paid	6	-	-	-	-
Closing balance		600	18,461	3	19,064

2012	Note	Share Capital $000	Retained Earnings $000	Foreign Currency Translation Reserve $000	Total Reserves $000
Opening balance		600	14,046	1,230	15,876
Total comprehensive income:					
Profit/(loss) after taxation		-	4,588	-	4,588
Other comprehensive income					
Movement on foreign currency translation reserve		-	-	(252)	(252)
Total comprehensive income			4,588	(252)	4,336
Transaction with owners					
Dividend paid	6	-	(1,150)	-	(1,150)
Closing balance		600	17,484	978	19,062

The accompanying notes form part of these financial statements

KPMG

STATEMENT OF FINANCIAL POSITION
as at 30 June 2013

	Note	2013 $000	2012 $000
Assets			
Cash and cash equivalents		3,626	5,664
Premium and other receivables	7	3,679	2,779
Investments	8	33,096	30,740
Equipment	9	174	220
Intangible assets and goodwill	10	2,700	2,740
Leasehold improvement	11	531	589
Total assets		43,806	42,732
Liabilities			
Payables	12	2,016	2,244
Employee benefits	13	465	551
Insurance contract liabilities	14	22,261	20,875
Total liabilities		24,742	23,670
Net assets		19,064	19,062
Equity			
Share capital	6	600	600
Retained earnings		18,461	17,484
Foreign currency translation reserve		3	978
Total equity		19,064	19,062

For and on behalf of the Board

G S Hawkins
Chairman

3-9-13 Date

P J Meyer
Director

3-9-13 Date

The accompanying notes form part of these financial statements

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STATEMENT OF CASH FLOWS
for the year ended 30 June 2013

	Note	2013 $000	2012 $000
Cash flows from operating activities			
Premium revenue		46,061	44,377
Investment income		1,124	1,497
Other income		49	61
Reinsurance premiums		(1,866)	(1,722)
Payment of claims		(23,999)	(24,681)
Payments to employees		(5,409)	(4,722)
Payments to suppliers		(14,299)	(11,922)
Payment/(refund) of income tax		5	26
Net cash flows from operating activities	19	1,666	2,914
Cash flows from investing activities			
Payments for equipment and leasehold improvement		(34)	(65)
Payments for intangible assets		(609)	(1,243)
Net proceeds/(payments) for investments		(2,289)	220
Acquisition of business (net of cash acquired)		-	(176)
Advance to Southern Cross Health Trust		(700)	-
Net cash flows from investing activities		(3,632)	(1,264)
Cash flows from financing activities			
Dividend		-	(1,150)
Net cash flows from financing activities		-	(1,150)
Net increase/(decrease) in cash and cash equivalents		(1,966)	500
Cash and cash equivalents at 1 July		5,664	5,161
Effect of exchange rate movement on foreign currency balances		(72)	3
Cash and cash equivalents at 30 June		3,626	5,664

The accompanying notes form part of these financial statements

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

1. Statement of accounting policies

Reporting entity

Southern Cross Benefits Limited (the "Company") is a limited liability company domiciled and incorporated in New Zealand. It is a wholly owned subsidiary of the Southern Cross Health Trust.

The Company's registered office is Level 18 AMP Centre, 29 Customs Street West, Auckland.

The statutory base is the Insurance (Prudential Supervision) Act 2010, Companies Act 1993 and the Financial Reporting Act 1993.

The Company is registered as a charity under the Charities Act 2005, as part of the Southern Cross Health Trust group registration.

The Company's primary activity is the provision of travel and pet insurance.

The Company also operates in Australia selling outbound travel insurance. This activity is conducted through a branch structure which is a Category C Direct Offshore Foreign Insurer("DOFI") regulated by the Australian Prudential Regulation Authority ("APRA") and the Australian Securities and Investment Commission("ASIC").

In February 2013, the Company was granted a full licence by the Reserve Bank of New Zealand ("RBNZ") to operate as an insurer subject to the Insurance (Prudential Supervision) Act 2010.

Financial statements are presented for the Company, including the Australian branch and pet insurance business.

The Company has a non-trading joint venture Fusion Insurance Services Limited in which it has a 50% share.

The Company, with its shareholder's approval, has applied the exemption available under section 211 (3) of the Companies Act 1993 in not disclosing the information required under section 211 (1) paragraphs (a) and (d) to (j) of the Companies Act 1993.

Basis of preparation

The financial statements have been prepared in accordance with New Zealand generally accepted accounting practice ("NZ GAAP"). They comply with New Zealand equivalents to International Financial Reporting Standards ("NZ IFRS") and other applicable financial reporting standards, as appropriate for profit oriented entities.

The statement of financial position has 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: financial assets at fair value through profit or loss and insurance contract liabilities.

Functional and presentation currency

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

NOTES TO THE FINANCIAL STATEMENTS cont'd
for the year ended 30 June 2013

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 relate to insurance contract liabilities (notes 14 and 15) and risk management (note 16).

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

Adoption of new accounting standards

Presentation of financial statements

The Company has applied the amendment to NZ IAS 1 – Presentation of Financial Statements (2007), which became effective from 1 July 2012. Accordingly, the Company has renamed the Statement of Comprehensive Income to the Statement of Profit or Loss and Other Comprehensive Income and categorised other comprehensive income as items that may be re-classified subsequently to the profit or loss.

Business Combinations

Business combinations are accounted for using the acquisition method as at the acquisition date, which is the date on which control is transferred to the Company. Control is the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, the Company takes into consideration potential voting rights that currently are exercisable.

The Company measures goodwill at the acquisition date as:
- the fair value of the consideration transferred; plus
- the recognised amount of any non-controlling interests in the acquiree; plus
- if the business combination is achieved in stages, the fair value of the pre-existing equity interest in the acquiree; less
- the net recognised amount (generally fair value) of the identifiable assets acquired and liabilities assumed.

When the excess is negative, a bargain purchase gain is recognised immediately in profit or loss.
The consideration transferred does not include amounts related to the settlement of pre-existing relationships. Such amounts generally are recognised in profit or loss.
Transaction costs, other than those associated with the issue of debt or equity securities, that the Company incurs in connection with a business combination are expensed as incurred.
Any contingent consideration payable is measured at fair value at the acquisition date. Subsequent changes in the fair value of the contingent consideration are recognised in profit or loss.

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 the profit or loss".

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Premium and other receivables

Premium and other receivables are stated at their cost less impairment losses. Impairment losses for uncollectable 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

The Company designates its investments as "financial assets at fair value through the profit or loss" at inception.

Investments designated as fair value through the profit or loss at inception are those that are held to match insurance contract liabilities. The designation of these assets to be at fair value through the profit or loss eliminates or significantly reduces a measurement or recognition inconsistency between assets and liabilities.

All investments are carried at fair value using the market bid price or valuation based on market observable data with changes in fair value recognised in the profit and loss. Transaction costs are recognised in the profit or loss on transaction date.

All purchases of investments are recognised on the date of the trade.

Equipment and Leasehold improvement

Equipment and leasehold improvements are measured at cost, less accumulated depreciation and impairment losses.

Where material parts of an item of equipment and leasehold improvement have different useful lives, they are accounted for as separate items of equipment and leasehold improvement.

Subsequent costs are added to the carrying amount of an item of equipment and leasehold improvement when that cost is incurred if it is probable that the future economic benefits embodied with the item will flow to the Company and the cost of the item can be measured reliably. All other costs are recognised in the profit and loss as an expense as incurred.

Depreciation is recognised in the profit or loss on a straight-line basis over the estimated useful lives of each part of an item of equipment and leasehold improvement. The depreciation rates for the current and comparative periods are as follows:

- Computer equipment — 25% - 33% per annum
- Office equipment — 15% - 20% per annum
- Furniture and fittings — 15% - 20% per annum
- Leasehold improvement — 8.33% per annum

The estimated useful life of assets is reassessed annually.

Intangible assets and goodwill

Computer software

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.

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

Goodwill

Goodwill that arises upon the acquisition of businesses is presented with intangible assets. Measurement of goodwill at initial recognition is described under Business Combinations within note 1. Goodwill is subsequently measured at cost less accumulated impairment losses.

Customer Base

Customer base represents the value of a customer base acquired, through its ability to generate future cash flows from retained business. It is recognised as an intangible asset when a business is acquired and when the criteria for recognition are met. A customer base is initially recognised at cost which is the fair value at the acquisition date and subsequently carried at cost less accumulated amortisation and any accumulated impairment losses. The capitalised costs are amortised on a straight line basis over the period when future economic benefits are expected to flow to the Company. This period is determined to be ten years.

Fair Value of insurance contracts acquired

Fair value of insurance contracts acquired represents the expected future cash flows arising from the insurance contracts acquired. It is recognised as an intangible asset when a business is acquired and when the criteria for recognition are met. Fair value of insurance contracts acquired is initially recognised at cost which is the fair value at the acquisition date and subsequently carried at cost less accumulated amortisation and any accumulated impairment losses. The capitalised costs are amortised over the remaining life of the insurance contracts.

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 reporting date, are translated to New Zealand dollars at the foreign exchange rate ruling at that date. Foreign exchange differences arising on their translation are recognised in the profit or loss.

Foreign operations

Activities of the Australian branch are recorded in Australian dollars, its functional currency. Profit or loss items are translated to New Zealand dollars at an average exchange rate for each month. The assets and liabilities of the branch are initially translated to New Zealand dollars at the foreign exchange rate on the date they arise. At balance date, all the assets and liabilities are re-translated at the exchange rate ruling on that date.

Foreign exchange differences arising from this translation are recognised in other comprehensive income and the foreign currency translation reserve.

Impairment

The carrying amounts of the Company's assets are reviewed at each balance date 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 assets is the greater of fair value less costs to sell, or 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 the profit or loss.

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Goodwill is tested for impairment annually, whether or not there is evidence of impairment.

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 Company has determined that all travel and pet insurance policies provided to customers are insurance contracts.

Reinsurance

Reinsurance premium expense ("Reinsurer's share of premium") and deferred reinsurance premium receivable

The minimum reinsurance premium obligation is recognised in the statement of financial position when the contract is agreed with the reinsurer and a deferred reinsurance asset is recognised in the statement of financial position at the reporting date.

The amortisation of deferred reinsurance premiums and recognition of the expense in the profit or loss is in accordance with the pattern of reinsurance service received. The amount deferred at balance date represents the future economic benefit to be received from reinsurance contracts.

Reinsurance claim recoveries

The component of claims expense relating to policies ceded to reinsurers is recognised as reinsurance claim recoveries in the profit or loss and as reinsurance recoveries in the statement of financial position. The recoverability of these assets is assessed at the reporting date and impairment is recognised where there is objective evidence that the Company may not receive the amounts due to it and these amounts can be reliably measured.

Income recognition

Premiums

Gross earned premiums from insurance contracts are recognised evenly over the period covered by the contract. For the travel operations, revenue is recognised on the date from which the travel period commences. Premiums billed but unearned are recorded as unearned premiums. Premiums ceded to reinsurers are recognised as reinsurer's share of the premium and excluded from net premiums. Premiums are stated net of fire service levies and stamp duty. Where premiums are billed and paid by instalments, the premium to be billed up to the next renewal date is recognised as a receivable and unearned premium liability.

Fee and other income

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

Investment income

Interest income is recognised in the profit or loss as it accrues and is calculated by using the effective interest rate method. Investment income on financial assets held at fair value through the profit or loss are recorded in accordance with the policies described for in Investments (note 1). Distributions from investments in funds are recognised on a present entitlement basis.

KPMG

Leases

Payments made under operating leases are recognised in the profit or loss on a straight-line basis over the term of the lease.

Acquisition costs

The costs incurred in acquiring and recording insurance contracts are deferred in recognition that they represent future benefits. Acquisition costs are initially recorded in the profit or loss. Any amounts that give rise to premiums in subsequent reporting periods are deferred as an asset and amortised over the period covered by the insurance contract.

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 Company 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 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 incurred but not paid. 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 and claim handling costs.

Unexpired risk provision and liability adequacy test

The provision for unearned premium arises from premiums received for risks that have not yet expired and is recognised as premium income evenly over the duration of the period covered by the contract. A liability adequacy test is performed on each of the travel and pet insurance businesses to assess whether there is any deficiency in the provision for unearned premium arising from expected claims, reinsurance and administration costs during the period covered by the unearned premium. For the New Zealand travel insurance business, 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 and reinsurance expenses are calculated. In addition, a risk margin is added to reflect the inherent uncertainty in the estimate of future claims. The total is compared with the provision for unearned premium. Any deficiency is recognised in the profit or loss after first writing down any deferred acquisition costs. The deficiency (if any) in excess of deferred acquisition costs is recognised in the statement of financial position as an unexpired risk provision.

Employee benefits

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

KPMG

Income tax

The Company is exempt from New Zealand income tax due to its charitable status. Australian income taxes are no longer payable by the Australian branch due to a ruling by the Australian Tax Office ("ATO") in the 2012 financial year. The income tax expense recognised in the statement of profit or loss comprises non-resident withholding tax paid on interest income in Australia. In 2012, the income tax expense includes a refund from the ATO of income tax paid from 2009 to 2011.

Goods and services tax (GST)

The statement of profit or loss and other comprehensive income has been prepared so that all components are stated exclusive of GST. All items in the statement of financial position are stated net of GST, with the exception of receivables and payables, which include GST invoiced.

Changes in estimates

If a change in an accounting estimate gives rise to a change in an asset or liability, or relates to equity, it is recognised by adjusting the carrying amount of the asset, liability or equity item in the period of the change. Otherwise, it is recognised prospectively by including it in the statement of profit or loss and other comprehensive income in the period of the change and future periods, as applicable.

Comparatives

Certain comparatives have been restated to comply with current year presentation.

New financial reporting standards approved but not yet effective

The following new or amended standards and interpretations applicable to the Company, 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 de-recognition 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 Company 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 Company is still to be determined.

NOTES TO THE FINANCIAL STATEMENTS cont'd
for the year ended 30 June 2013

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 Company is still to be determined.

2 Net claims expense

	2013 $000	2012 $000
Claims incurred relating to risk borne in current financial year (gross)	24,548	24,559
Reinsurance recoveries relating to risk borne in current financial year	(13)	(329)
Claims incurred relating to risk borne in the current financial year (net)	24,535	24,230
Claims incurred relating to risk borne in previous financial year (gross)	(646)	(1,518)
Reinsurance recoveries relating to risk borne in previous financial year	(9)	(140)
Claims incurred relating to risk borne in previous financial year (net)	(655)	(1,658)
Movement in provision for claims handling cost	(7)	(297)
Movement in risk margin	(20)	(70)
Net claims expense	23,853	22,205

3 Operating expenses

	2013 $000	2012 $000
Auditor's remuneration		
– Audit fees	111	98
– Other services (see below)	74	34
Depreciation	138	164
Amortisation of computer software	505	342
Amortisation of customer base and fair value of insurance contracts acquired	144	122
Employee benefits expense	5,323	4,849
Rental of premises	537	506

Auditor's remuneration for other services consists of reviewing regulatory returns to the RBNZ and annual APRA reporting on the Australian branch.

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NOTES TO THE FINANCIAL STATEMENTS cont'd
for the year ended 30 June 2013

3 Operating expenses cont'd

	2013 $000	2012 $000
Acquisition cost	1,445	1,281
Policy administration	628	644
Claims handling	1,282	1,291
Management	15,653	13,880
	19,008	17,096

4 Investment and other income

	2013 $000	2012 $000
Interest income	454	999
Distribution income	552	390
Net gains/(losses) on investments at fair value through profit and loss	67	(72)
Unrealised foreign exchange movement	(72)	5
	1,001	1,322

5 Taxation

	2013 $000	2012 $000
Australian income tax paid/(refunded) on written premiums	-	(84)
Australian income tax on interest earned	4	10
	4	(74)

The Australian branch is exempt from Australian income tax as confirmed by the Australian Tax Office during the 2012 financial year. Non-resident withholding tax on interest earned is still payable by the Australian branch.

6 Equity

Share capital comprises 600,000 (2012: 600,000) ordinary shares of $1, fully paid. All ordinary shares have equal voting rights, and share equally in dividends and surplus on winding up. No Dividends were paid during the year (30 June 2012 $1,150,000). A dividend per share of $1.92 was paid in February 2012.

7 Premium and other receivables

	2013 $000	2012 $000
Premium accounts receivable	1,730	1,409
Reinsurance recoveries	1	240
Interest receivable	7	125
Other accounts receivable	416	333
Deferred acquisition costs	698	670
Amounts owed by related parties	827	2
	3,679	2,779

a. Reconciliation of movements in reinsurance recoveries

	2013 $000	2012 $000
Opening balance	240	40
Gross reinsurance recoveries during the year	22	469
Reinsurance recoveries settled by reinsurer during the year	(261)	(269)
Closing balance	1	240

b. Reconciliation of movements in deferred acquisition cost

	2013 $000	2012 $000
Opening balance	670	635
Gross commissions paid during the year	1,473	1,316
Commisions incurred during the year	(1,445)	(1,281)
Closing balance	698	670

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

NOTES TO THE FINANCIAL STATEMENTS cont'd
for the year ended 30 June 2013

8 Investments
At fair value through the profit or loss

	2013 $000	2012 $000
At valuation :		
New Zealand Government stock	-	516
Corporate bonds	-	3,025
Bank deposits, commercial paper and floating rate notes	2,204	18,070
Investment in funds	30,892	9,129
	33,096	30,740

The maturity details of these investments are provided in note 16.

New Zealand Government stock held by the Public Trust as a deposit was returned to the Company in April 2013 as the Reserve Bank of New Zealand issued the Company with a full licence under the Insurance (Prudential Supervision) Act 2010 in February 2013.

The Company is required to hold designated levels of investments in Australia to comply with the capital adequacy requirements of APRA in relation to the activities of the Australian branch (refer note 21). Restrictions are imposed on these investments and the Company's ability to utilise them. At balance date $9,895,000 (2012: $9,129,000) in a cash fund was held in this category.

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NOTES TO THE FINANCIAL STATEMENTS cont'd
for the year ended 30 June 2013

9 Equipment

	Computer equipment	Office equipment	Furniture and fittings	Total
	$000	$000	$000	$000
At 30 June 2013				
Cost	485	388	427	1,300
Accumulated depreciation	(453)	(322)	(351)	(1,126)
Closing balance	32	66	76	174
Reconciliation of movement in equipment				
Opening balance	55	81	84	220
Additions	14	3	17	34
Depreciation for the year	(37)	(18)	(25)	(80)
Closing balance	32	66	76	174

	Computer equipment	Office equipment	Furniture and fittings	Total
	$000	$000	$000	$000
At 30 June 2012				
Cost	471	385	410	1,266
Accumulated depreciation	(416)	(304)	(326)	(1,046)
Closing balance	55	81	84	220
Reconciliation of movement in equipment				
Opening balance	63	94	106	263
Additions	29	6	29	64
Depreciation for the year	(37)	(19)	(51)	(107)
Closing balance	55	81	84	220

Equipment is a non-current asset.

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NOTES TO THE FINANCIAL STATEMENTS cont'd
for the year ended 30 June 2013

10 Intangible assets and goodwill

	Fair value of insurance contracts acquired	Goodwill	Customer base	Computer software	Work in progress	Total
	$000	$000	$000	$000	$000	$000
At 30 June 2013						
Cost	191	168	559	5,507	170	6,595
Accumulated amortisation	(191)	-	(75)	(3,629)	-	(3,895)
Closing balance	-	168	484	1,878	170	2,700
Reconciliation of movement in intangible assets						
Opening balance	88	168	540	999	945	2,740
Additions	-	-	-	-	609	609
Transfers from work in progress			-	1,384	(1,384)	-
Amortisation for the year	(88)	-	(56)	(505)	-	(649)
Closing balance	-	168	484	1,878	170	2,700

	Fair value of insurance contracts acquired	Goodwill	Customer base	Computer software	Work in progress	Total
	$000	$000	$000	$000	$000	$000
At 30 June 2012						
Cost	191	168	559	4,123	945	5,986
Accumulated amortisation	(103)	-	(19)	(3,124)	-	(3,246)
Closing balance	88	168	540	999	945	2,740
Reconciliation of movement in intangible assets						
Opening balance	-	-	-	698	344	1,042
Additions through business combinations	191	168	559	-	-	918
Additions	-	-	-	-	1,246	1,246
Transfers from work in progress	-	-	-	645	(645)	-
Amortisation for the year	(103)	-	(19)	(342)	-	(464)
Effect of foreign currency translation	-	-	-	(2)	-	(2)
Closing balance	88	168	540	999	945	2,740

The majority of the computer software and work in progress is internally generated. Intangible assets and goodwill are non-current assets.

Goodwill

Goodwill arose in February 2012 upon acquisition of Ellenco Pet Insurance Limited's customer contracts, systems, intellectual property and operating assets.

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NOTES TO THE FINANCIAL STATEMENTS cont'd
for the year ended 30 June 2013

10 Intangible assets and goodwill cont'd

This goodwill is attributable mainly to the opportunities for growth enabled by marketing the product to the members of the Southern Cross Medical Care Society ("Society") and relates entirely to the pet insurance business, being the cash-generating unit (CGU) as defined in NZ IAS 36. The carrying amount that relates to this CGU at 30 June 2013 is $168,000 (2012: $168,000).

Goodwill is assessed at each reporting date for indicators of impairment as it is not amortised. No impairment losses on goodwill were recognised during 2013 (2012: nil).

The recoverable amount of the CGU is determined based on value-in-use calculations, determined by discounting the future cash flows to be generated from the CGU. These calculations use discounted cash flow projections based on past experience, actual operating results and profit forecasts approved by management as part of the rolling operating plan process. The rolling operating plan covers a detailed two year time frame, approved by management. Profit forecasts greater than two years are estimated by management based on their assessment of sustainable growth. The discounted cash flow model has used a five year profit projection, a discount rate (pre-tax) of 12.0% (2012: 12.0%) and annual growth rates for pets covered (as detailed in the following table). The discount rates were based on the average risk-free rate obtained from the yield on 10-year bonds issued by the New Zealand Government adjusted for a risk premium to reflect the risk of the specific CGU. The projected growth in pets covered and cash flows were based on realising the opportunities for growth enabled by marketing the product to the members of the Society in conjunction with technology improvements enabling higher capacity.

Growth rate projections:

	Year 1	Year 2	Year 3	Year 4	Year 5
Pets covered 2013	20.0%	28.8%	29.4%	10.0%	10.0%
Pets covered 2012	10.0%	10.0%	10.0%	10.0%	10.0%

Key assumptions underlying the valuation relate to management's assessment of new business growth, claims cost escalation, premium increases, commission rates and operating expenses. Management utilise local market data as well as Group expertise and experience to validate key assumptions.

The key assumptions described above may change as economic and market conditions change. The Company estimates that reasonably possible changes in these assumptions are not expected to cause the recoverable amount of the CGU to decline below the carrying amount.

11 Leasehold improvement

	2013 $000	2012 $000
Cost	689	689
Accumulated depreciation	(158)	(100)
Closing balance	531	589

Reconciliation of movement in leasehold improvement

	2013 $000	2012 $000
Opening balance	589	646
Additions	-	-
Depreciation for the year	(58)	(57)
Closing balance	531	589

Leasehold improvement is a non-current asset.

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NOTES TO THE FINANCIAL STATEMENTS cont'd
for the year ended 30 June 2013

12 Payables

	2013 $000	2012 $000
Accounts payable	1,903	2,051
Income and witholding tax payable	25	16
Reinsurance premiums payable	-	47
Amounts owed to related parties	88	130
	2,016	2,244

Payables is a current liability except for $344,000 (2012: $385,000) of non-current deferred lease income within Accounts Payable.

13 Employee benefits

	2013 $000	2012 $000
Employee benefits	465	551
	465	551

Employee benefits is a current liability.

14 Insurance contract liabilities

	2013 $000	2012 $000
Provision for outstanding claims (refer note 14a)	7,007	7,392
Provision for unearned premium (refer note 14c)	15,254	13,483
	22,261	20,875

Insurance contract liabilities is a current liability.

a. Provision for outstanding claims

	2013 $000	2012 $000
Central estimate of outstanding claims liability	6,031	6,389
Claims handling costs	440	447
Risk margin	536	556
Closing balance	7,007	7,392

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NOTES TO THE FINANCIAL STATEMENTS cont'd
for the year ended 30 June 2013

a. Provision for outstanding claims cont'd

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 movements in provision for outstanding claims

	2013 $000	2012 $000
Opening balance	7,392	9,194
Amounts utilised during the year	(5,626)	(6,149)
Additional provision required / (reversal of unused provision)	(655)	(1,658)
Amounts provided during the year	5,923	5,899
Movement in claims handling costs	(7)	(297)
Movement in risk margin	(20)	(70)
Recognised on acquisition of insurance business	-	473
Closing balance	7,007	7,392

c. Reconciliation of movements in provision for unearned premium

	2013 $000	2012 $000
Opening balance	13,483	11,748
Premiums written in the year	46,382	44,487
Premiums earned during the year	(44,611)	(44,101)
Recognised on acquisition of insurance business	-	1,349
Closing balance	15,254	13,483

15 Actuarial information

Estimates of the provision for outstanding claims as at 30 June 2013 have been determined by Peter Davies, B.Bus.Sc, FIA, a Fellow of the New Zealand Society of Actuaries. The calculation of the provision for outstanding claims complies with Appendix D of 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.

Claims outstanding for two months or more are determined using a standard chain ladder method. Claims outstanding in respect of the most recent two months (Pet insurance, one month) are determined by applying an estimated loss ratio to the earned premiums for the month. In the travel insurance business, additional allowance has been made in the New Zealand and Australian outstanding claims provisions for a small number of relatively large notified claims (2012: adjustments were made for a small number of relatively large notified claims for New Zealand, and none in

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15 Actuarial information cont'd

Australia). Future claim payments are not discounted, as the expected duration to settlement is relatively short, and virtually all claims are settled within a year.

An additional margin of 9% (2012 : 8%) for New Zealand and Australia has been added to the central estimate of the outstanding claims costs, to take account of the uncertainties inherent in the setting of claim provisions. The additional margin for the pet insurance business is 7% (2012: 10%).

A further provision of 7% (2012 : 7%) of the central estimate of the outstanding claims has been made for direct and indirect claim management costs for the New Zealand business and 6% (2012 : 6%) for the Australian business and 7% (2012: 10%) for the pet insurance business.

The actuary has reviewed the adequacy of the provision for unearned premium at 30 June 2013. In performing this test, an additional risk margin has been added to the central estimate of the future claim costs, to take account of the uncertainties inherent in the central estimate. A further allowance has been made for direct and indirect claim management costs and also policy administration costs.

For the travel insurance businesses, if the loss ratio was to increase by 10%, the premium liability will also increase by 10%. As there is a significant margin between the premium liability and the unearned premium provision, the liability adequacy test in respect of unearned premiums can cover quite significant levels of variability in the loss ratio. For the pet insurance business, the premium liability including risk margins, is slightly lower than the unearned premium, therefore any increase in the loss ratio will have a direct impact to profitability.

In the actuary's view, the liability adequacy tests identified surpluses and there is no requirement to recognise unexpired risk provisions in respect of the unearned premium provision (2012 : no provision required).

	2013			2012		
	Pet	New Zealand	Australia	Pet	New Zealand	Australia
	$000	$000	$000	$000	$000	$000
Percentage Risk margin on expected future cash flows relating to future claims	12.3%	15.8%	15.8%	17.5%	14.0%	14.0%
Probability of adequacy (LAT & OCR)	75.0%	75.0%	75.0%	75.0%	75.0%	75.0%
Sensitivity:						
IBNP (incl margins)	537	4,674	1,796	486	5,490	1,309
IBNP if settlement 10% longer	699	6,588	2,179	631	7,338	1,785
IBNP if settlement 10% shorter	430	3,472	1,533	388	4,220	1,013

16 Risk management

The Company is exposed to a number of risks in the normal course of business. Primarily there is the risk of conducting 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 risks and any objectives, policies and processes to manage the risks are described below.

16 Risk management cont'd

A. Insurance risk

The Company assumes insurance risk through its travel and pet 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.
- Maintaining a reinsurance programme for the travel insurance business which protects the Company against single large claims in excess of the Company's retention, and against a catastrophic event involving multiple claims.
- 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 claims experience of the portfolio.
- Adherence to a formal capital management plan monitored monthly to ensure minimum prudential capital requirements are complied with.
- The Company has implemented a risk management policy, which is in accordance with the prudential standards issued by RBNZ and APRA.

II. Sensitivity to insurance risk

The financial results of the Company 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 for the travel insurance business involves the reimbursement of losses during travel for medical and surgical expenses in addition to the losses relating to personal property, cancellation, personal accident and personal liability, and rental vehicle excesses. 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.

III. Concentration of insurance risk

The Company transacts travel insurance business in New Zealand for inbound and outbound customers, and in Australia for outbound customers. The nature of its business means that this concentration of risk cannot be avoided. Management defines concentration of risk by geographic region, specific destination, and unknown and unforeseen accumulations of insured on a single transport carrier. The Company is most at risk to the global commercial aviation industry and its ability to offer continuous operations given the impacts of oil prices, pandemics, natural disasters and terrorism, which lends itself to a single event resulting in a high volume of relatively low dollar value cancellation / delay claims.

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16 Risk management cont'd

The Company's concentration risks are mitigated by its catastrophe, pandemic and terrorism reinsurance treaties for the travel insurance business, to protect it from high severity losses and catastrophic events. Reinsurance is placed to cover losses in excess of agreed retentions.

B. Financial risks

I. Credit risk

In the normal course of its business the Company incurs credit risk from its travel and pet insurance operations and from investment in financial assets. There are no significant concentrations of credit risk other than the AMP Capital Cash and Short Duration Funds $20,997,000 (2012 nil) and Colonial First State Cash Fund $9,895,000 (2012 $9,129,000).

The Company maintains an investment policy which is used to manage the exposure to credit risk.

The maximum exposure to credit risk at balance date is the amount of financial assets stated in the balance sheet.

These exposures are net of any recognised provisions for impairment losses. There were no impairments at 30 June 2013 (2012: none). The Company does not require any collateral or security to support financial assets due to the quality of the counter-party organisations. The credit quality of counter-parties is assessed based on published credit ratings, issued by Standard & Poor's or equivalent ratings agencies.

The credit quality of financial asset counter-parties is as follows:

2013	AAA $000	AA $000	A $000	BBB $000	Non-rated $000	Total $000
Cash and cash equivalents	-	3,626	-	-	-	3,626
Premiums and other receivables:						
- Premium accounts receivable	-	-	-	-	1,730	1,730
- Reinsurance recoveries	-	-	1	-	-	1
- Interest receivable	-	7	-	-	-	7
- Other accounts receivable	32	154	87	-	143	416
- Amounts due by related parties	-	-	5	-	822	827
Investments	414	24,994	6,321	1,367	-	33,096
	446	28,781	6,414	1,367	2,695	39,703

16 Risk management cont'd

2012	AAA $000	AA $000	A $000	BBB $000	Non-rated $000	Total $000
Cash and cash equivalents	-	5,664	-	-	-	5,664
Premiums and other receivables:						
- Premium accounts receivable	-	-	-	-	1,409	1,409
- Reinsurance recoveries	-	127	113	-	-	240
- Interest receivable	6	98	21	-	-	125
- Other accounts receivable	42	173	-	-	118	333
- Amounts due by related parties	-	2	-	-	-	2
Investments	-	23,625	7,115	-	-	30,740
	48	29,689	7,249	-	1,527	38,513

A look-through approach has been taken to assess the credit ratings of the investments in funds for this credit quality analysis.

II. Liquidity risk

The Company 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 investment policy sets out criteria to ensure funds are available to meet calls to cover claims and expenses at unexpected levels of demand.

The contractual maturities of investments are as follows:

	2013 $000	2012 $000
On call	33,096	11,731
0-6 months	-	13,491
7-12 months	-	516
1-2 years	-	-
2-5 years	-	5,002
Beyond 5 years	-	-
	33,096	30,740

During the year, the investment funds for the New Zealand operations were invested in funds managed by AMP Capital. These funds are available on call along with the Australian Branch investment in the Colonial First State Cash Fund. The cash and cash equivalents are available on call. All premium accounts receivable, with the exception of unbilled premiums on pet policies, are due within one month of balance date and within two months for the pet insurance business. Unbilled premiums of $1,091,000 are paid by instalments and are due within 12 months of balance date (30 June 2012: $874,000). Substantially all liabilities are payable within one year of balance date.

NOTES TO THE FINANCIAL STATEMENTS cont'd
for the year ended 30 June 2013

16 Risk management cont'd

C. Market risks

I. Foreign currency risk

At 30 June 2013, the New Zealand operations had assets of New Zealand dollars $217,000 and no liabilities denominated in foreign currencies (30 June 2012: assets of $2,353,000 and no liabilities). Foreign currency bank balances are maintained to meet future claim expenses in these currencies, thereby creating a natural hedge.

The balances held in foreign currencies are:

	New Zealand dollar equivalent	
	2013 $000	2012 $000
Australian dollar	3	2,228
Canadian dollar	124	63
United States dollar	90	62
	217	2,353

A movement of 100 basis points on these exchange rates would have an immaterial impact on the statement of profit or loss and other comprehensive income.

The Company's Australian branch exposes it to currency risk, as the branch's functional currency is Australian dollars. The New Zealand dollar equivalents of the Australian assets and liabilities at balance date amounted to $13,389,000 and $5,235,000 (30 June 2012: assets of $12,544,000 and liabilities of $3,912,000).

As the Australian operation is considered an on-going investment, no hedging of the foreign currency exposure is undertaken. Any movement in the Australian dollar exchange rate is reflected in the foreign currency translation reserve. A movement of 100 basis points on the Australian dollar exchange rate at year end would have an impact of $82,000 (2012: $86,000) on the net assets of the Company and the foreign currency translation reserve.

II. Interest rate risk

In the prior year the Company invested in both fixed and variable rate financial instruments such as bonds, commercial paper and floating rate notes. During the current year, the Company invested in the AMP Funds and Colonial First State Cash Fund and has indirect exposure to interest rate risk. There was a risk that any movement in interest rates could have affected the profitability and cash flows of the Company. The Company maintained an investment policy to mitigate this risk.

Fair value risk

The fair value of investments can fluctuate depending on changes in interest rates. The following analysis shows the impact of notional changes in interest rates on profitability in 2012:

16 Risk management cont'd

	2012 $000
Impact of increase by 100 basis points on profit and loss statement	(33)
Impact of decrease by 100 basis points on profit and loss statement	34

Cash flow interest rate risk

The cash flows from investments of the Company in the short term are susceptible to changes in interest rates. The variable interest rate instruments pose cash flow interest rate risk and the following analysis shows the impact of notional changes in interest rates on cash flows and profit and loss:

	2013 $000	2012 $000
Impact of increase by 100 basis points on cash flows and profit and loss	22	30
Impact of decrease by 100 basis points on cash flows and profit and loss	(22)	(30)

III. Price risk

The Company is exposed to price risk through unit price changes of its investments in the AMP Capital and Colonial First State funds. The Company manages its price risk by ensuring all activities are transacted in accordance with the funds investment statements and the Company's investment policy. The following analysis shows the impact of changes in prices on profitability:

	2013 $000	2012 $000
Impact of increase by 100 basis points on profit and loss statement	309	91
Impact of decrease by 100 basis points on profit and loss statement	(309)	(91)

D. Fair values of financial assets and financial liabilities

All financial assets and financial liabilities included in the statement 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.

NOTES TO THE FINANCIAL STATEMENTS cont'd
for the year ended 30 June 2013

16 Risk management cont'd

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.

30 June 2013	Level 1 $000	Level 2 $000	Level 3 $000	Total $000
New Zealand Government Stock	-	-	-	-
Corporate bonds	-	-	-	-
Bank deposits, commercial paper and floating rate notes	2,204	-	-	2,204
Investment in funds	-	30,892	-	30,892
Total investments	2,204	30,892	-	33,096

As at 30 June 2013, the investment portfolio was valued using month-end closing market rates as supplied by AMP Capital Investors (New Zealand) Limited and Colonial First State Asset Management for the Australian Branch.

30 June 2012	Level 1 $000	Level 2 $000	Level 3 $000	Total $000
New Zealand Government Stock	516	-	-	516
Corporate bonds	-	3,025	-	3,025
Bank deposits, commercial paper and floating rate notes	2,602	15,468	-	18,070
Investment in funds	-	9,129	-	9,129
Total investments	3,118	27,622	-	30,740

Bancorp Treasury Services Limited valued the investment portfolio as at 30 June 2012 on the June 2012 month-end closing market rates as supplied by ANZ Bank each month to wholesale investors. Where there are investments that are not included in the valuation, for example private placements in which the Company 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.

17 Acquisition of business

On 29 February 2012 the Company acquired the pet insurance business from Ellenco Pet Insurance Limited by obtaining control of the customer contracts, systems, intellectual property and operating assets, enabling the on going operation of the business. The pet insurance business provides insurance cover for veterinary care for both illness and accidents for cats and dogs. The business is operated by the Society under a management contract with the Company.

The purchase of the pet insurance business will add to the Company's offerings of insurance products and diversify its business risk.

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NOTES TO THE FINANCIAL STATEMENTS cont'd
for the year ended 30 June 2013

18 Related parties

Identity of related party	Nature of relationship
♦ Southern Cross Health Trust ("Health Trust")	Parent of the Company
♦ Southern Cross Hospitals Limited ("Hospitals")	100% subsidiary of Parent
♦ Southern Cross Primary Care ("Primary Care")	100% subsidiary of Parent
♦ Southern Cross Medical Care Society ("Society")	Related party to Parent
♦ Fusion Insurance Services Limited	50% Joint Venture of the Company
♦ Activa Health Limited ("Activa")	Subsidiary of Society

All these related entities have 30 June balance dates, except for Fusion Insurance Services Limited, which has a 31 December balance date.

The Company, the Hospitals and the Society are separate legal entities which work together in certain areas such as information technology, legal, payroll, HR, and finance, under fully costed service level agreements which dictate the expectations of each entity. In 2013, such costs to the Company totalled $1,071,000 (2012: $970,000).

Any other costs incurred by one entity on behalf of another are reimbursed monthly.

The Society charges the Company a fee of $225,000 which is included under the fully costed service level agreements for enabling marketing opportunities to its membership (2012: $225,000). The Company purchased health insurance for its employees from the Society, to the value of $52,000 (2012: $46,000).

During the year, the Company sold an investment at market value of $1,015,000 to the Society and made cash advances of $700,000 to the Health Trust.

The pet insurance business is operated by the Society under a management contract with the Company. The total value of Society charges for the year were $1,196,000 (2012: $447,000). These costs are charged on an incurred basis.

The amount of transactions with related parties are:

	2013 $000	2012 $000
Purchases		
Society	2,319	1,462
Sales		
Society	1,015	-

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NOTES TO THE FINANCIAL STATEMENTS cont'd
for the year ended 30 June 2013

18 Related parties cont'd

The amount of outstanding balances with related parties are:

	2013 $000	2012 $000
Balances due from related parties		
Accounts receivable - related parties		
Health Trust	120	-
Intercompany advances - receivable		
Health Trust	700	-

	2013 $000	2012 $000
Balances due to related parties		
Accounts payable - related parties		
Society	83	130

All related party balances with the exception of the intercompany advance are repayable on normal trading terms and are unsecured. The intercompany advance to the Health Trust, is unsecured, non-interest bearing and has no defined terms of repayment.

b. Remuneration of Directors and key management personnel

Remuneration of Directors

The Company did not pay any Directors' fees for 2013 (2012: nil). The Company provides Directors with directors' and officers' liability insurance cover for liabilities to other parties that may arise from their positions as directors.

Remuneration of key management personnel (Excluding Directors remuneration)

	2013 $000	2012 $000
Salaries and other short-term benefits	772	743
	772	743

Key management personnel include the chief executive officer and senior executives. The Company does not provide loans, advances or post-employment benefits to key management personnel. At each reporting date there are amounts outstanding to key management personnel comprising salaries, earned leave and short-term incentives.

NOTES TO THE FINANCIAL STATEMENTS cont'd
for the year ended 30 June 2013

19 Reconciliation of net surplus with net cash flows from operating activities

	2013 $000	2012 $000
Profit/(loss) after taxation	977	4,588
Add/(less) non-cash items:		
Depreciation	138	164
Amortisation of intangible assets	649	464
Foreign currency exchange movement	72	(5)
Foreign currency translation reserve movement	(975)	(250)
Movement in valuation of investments	(67)	131
Add/(less) movements in working capital items:		
Premiums and other receivables	(200)	(268)
Payables	(228)	(147)
Provision for outstanding claims	(385)	(2,276)
Provision for unearned premium	1,771	386
Employee benefits	(86)	127
Net cash flows from operating activities	1,666	2,914

20 Credit rating

On 03 July 2013 Standard & Poor's reaffirmed the Company's Insurer Financial Strength Rating of A+. This signifies the insurer "has strong financial security characteristics".

21 Financial Soundness

The Reserve Bank of New Zealand (RBNZ) awarded a full licence to the Company in February 2013 in line with the Insurance (Prudential Supervision) Act 2010.

The minimum solvency capital the Company is required to retain under the Solvency Standard for Non-life Insurance Business issued by the RBNZ, is per the table below. The Company has adopted a formal capital management plan to maintain a strong capital base and satisfy capital adequacy standards as prescribed by APRA for the Australian branch and the RBNZ. Additional solvency margins of $2.5 million (2012: $2.9 million) for the Company and AUD $1.6 million (2012: AUD $1.5 million) for the Branch have been determined by the Directors as sufficient for maintaining financial soundness.

During the year the Company has complied with all externally imposed capital requirements.

Actual solvency capital at 30 June 2013 for the Australia branch was AUD $7,303,672 (2012: AUD $6,789,500) calculated in accordance with APRA requirements. Minimum solvency capital required to be retained by the Branch to satisfy APRA requirements is AUD $5 million.

KPMG

NOTES TO THE FINANCIAL STATEMENTS cont'd
for the year ended 30 June 2013

21 Financial Soundness cont'd

Solvency capital requirements for the Company is detailed below.

	2013 $000	2012 $000
Minimum solvency capital	7,374	5,541
Actual Solvency capital	9,987	8,700
Solvency Margin	2,613	3,159

22 Lease commitments

The company entered into an agreement in August 2010 to lease new premises for 12 years commencing October 2010. The commitments under operating leases in respect of payments due to be made in the following years are:

	2013 $000	2012 $000
Within 1 year	370	360
Between 1 and 2 years	381	370
Between 2 and 5 years	1,223	1,181
Greater than 5 years	2,024	2,448
	3,998	4,359

23 Capital commitments

The Company had no capital commitments at 30 June 2013 (2012: Nil).

24 Contingent liabilities

The Company has the following contingent liabilities at 30 June 2013 and 2012.

The Company has a standby letter of credit arrangement as a requirement of its merchant acquiring facility in Australia. The maximum value of this facility is $200,000 Australian dollars. The letter of credit expires in January 2014 but has the ability to be extended annually (2012: $200,000 Australian dollars).

The Company has a bank bond in place as a requirement of the lease agreement for the new premises. The maximum value of this bond is currently $400,000 (2012: $450,000) and it reduces in value on 1 October 2013 to $350,000.

Davies Financial and Actuarial Limited

20th August 2013

To: The Directors
Southern Cross Benefits Limited

From: Peter Davies
Appointed Actuary

Re: Southern Cross Benefits Limited: Report as at 30th June 2013 under Sections 77 and 78 of the Insurance (Prudential Supervision) Act 2010

You have asked me to prepare this report in terms of the above sections of the Act, and I would like to comment further as follows:

1. I have reviewed the actuarial information included in the audited accounts for Southern Cross Benefits Limited as at 30th June 2013. "Actuarial information" includes the following:

   - claim provisions and unexpired risk / unearned premium provisions;
   - solvency calculations in terms of the RBNZ Solvency Standard;
   - balance sheet and other information allowed for in the calculation of the company's solvency position; and
   - disclosures regarding the methodology and assumptions used for calculating claim provisions, unexpired risk provisions, and other disclosures.

2. No limitations have been placed on my work.

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Telephone (09) 489-3551
Facsimile: (09) 489-6613
e-mail: pdavies@actuary.co.nz
home page: www.actuary.co.nz

3. I am independent with respect to Southern Cross Benefits Limited as defined under professional standard ISA (NZ) 620 of the New Zealand Institute of Chartered Accountants.

4. I have been provided with all information that I have requested in order to carry out this review.

5. In my view the actuarial information contained in the financial statements has been appropriately included, and the actuarial information used in the preparation of the financial statements has been appropriately used.

6. The company (including its Australian branch) exceeded the minimum capital requirement of the RBNZ solvency standard for non-life insurers as at 30th June 2013, and is projected to exceed the minimum requirement at all times over the next three years.

I would be very happy to answer any queries concerning this report.

Yours sincerely

Peter

Peter Davies B.Bus.Sc., FIA, FNZSA
Appointed Actuary

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