The Southern Cross Medical Care Society 2014 Annual Report

The kiwifruit is one of the most nutritious fruits in the world. It's also high in fibre, which is great for your digestive system.

Contents

Overview

FOR THE YEAR ENDED 30 JUNE 2014

- Members continued to receive very good value from their Southern Cross Medical Care Society policies. For every dollar received in premium income, 90.4 cents was returned to members in claims for healthcare services.
- Southern Cross maintained a strong and stable financial position with reserves the equivalent of approximately seven months' worth of claims.
- For the 12th consecutive year, the Society's strong capital and competitive positioning resulted in an A+ (stable) financial strength rating from Standard and Poor's.
- The not-for-profit Society ended the year with a deficit of $1.1 million due to higher than expected claims costs in the last four months of the year.
- During the year the Society incurred a record $694.5 million in claims, up 8.7% on 2013 and earned $768.4 million in premiums, up 5.9%.
- Southern Cross covers 61% of New Zealanders who have health insurance and pays 72% of the country's health insurance claims.

Chairman's report

The 2014 financial year saw the Society continue to deliver excellent value for its members. For every $1 received in premiums, your not-for-profit Society returned 90.4 cents to members in claims.

This is a market leading rate of return. By comparison, data from the Health Funds Association shows that over the same period the rest of the industry returned an average of just 67.5 cents in claims for every $1 received in premium.

Delivering this level of value has resulted in a year-end deficit of $1.1 million. This was due to higher than expected claims costs for the year, driven predominantly by orthopaedic procedures and specialist consultations.

In the case of the Society, as a not-for-profit insurer with strong reserves, small deficits such as these can be absorbed without impacting the value we deliver to members.

That said, it is important for members to recognise that the Society, as a responsible insurer, must continue to aim for a small annual surplus – not only to maintain our long-term viability but also to maintain reserves for times of unexpected and severe claims cost volatility. A positive solvency margin is also required for licenced insurers as part of the standards set by the Reserve Bank of New Zealand.

For the 12th consecutive year, the Society's strong capital and competitive positioning resulted in an A+ (stable) financial strength rating from Standard and Poor's.

DELIVERING THE BEST VALUE

In total, the Society incurred a record $694.5 million in claims for healthcare services, up 8.7% on the previous year. This included claims for more than 155,000 elective surgical operations, 370,000 specialist consultations, 784,000 GP visits and 680,000 prescription medicines.

Premium income for the year totalled $768.4 million, up 5.9% on 2013.

As a not-for-profit organisation, any premium income not used to fund healthcare services is used for the benefit of members – either in running the Society itself; expanding the benefits available in our policies; improving services available to members; or strengthening reserves.

At year end, the Society's reserves sat at $394.3 million – the equivalent of around seven months of claims. This is within the target solvency range set by the Board. Reserves are also part of our investment portfolio which generated $18.5 million in investment income for the Society and its membership in 2014. It is this income that has been used to help sustain our high claims to premium ratio.

Careful management saw overheads for the year come in $0.7 million under budget at $93.5 million.

A LEADING ROLE IN AFFORDABLE HEALTHCARE

As New Zealand's leading health insurer, the Society is in a position to use its expertise and experience to positively influence the health environment on behalf of its members.

Due to rising demand for services, the public health system is coming under increasing financial pressure. If historic spending patterns continue, the New Zealand Institute of Economic Research estimates health will increase from 21% to 32% of all Government spending by 2050.

To avoid placing further stress on New Zealand's valued public services, it is important that the option of private health insurance, and private healthcare, remains affordable to a wide range of Kiwis and their employers. This is a key focus for the Society.

Although the Society is not concerned with generating profit, the continuing rise in claims costs is of concern because it directly impacts the premiums of our members.

GRAEME HAWKINS
CHAIRMAN OF THE BOARD

The number of claims is not something we can, or wish to, do much about. After all, we want our members to make the best use of their policies. But what we can help to manage is the cost of those claims – particularly increases that are out of line with market rates.

Our key tool for managing claims costs is the Southern Cross Affiliated Provider programme. Affiliated Providers include surgeons, specialists and facilities that provide certain procedures to members at agreed prices. Society CEO Peter Tynan discusses the programme's achievements and future plans in more detail on page 4.

MEMBERSHIP

Reflecting challenging economic conditions and an industry-wide trend, the small decline in membership numbers experienced over recent years continued. Membership at year end was 815,447, a 0.3% decrease on 2013 (compared to the rest of the industry which decreased 0.4%). There were slight membership dips in several age groups. However, there were also gains in the number of members aged 21-35 and those aged 65 and over.

SHARING EXPERTISE

As part of New Zealand's leading healthcare group the Society also has a role to play in helping to drive discussion and awareness around the challenges facing the health sector.

In May, Southern Cross Healthcare Group hosted a Think Tank aimed at finding solutions to the looming fiscal crisis in healthcare. Over 50 experts in their respective fields gathered to discuss and debate ideas.

Politics, at all levels, was overwhelmingly seen as the key barrier to implementing solutions necessary to resolve health funding issues. At its close, the Think Tank recommended an independent taskforce or similar be established to help shape long-term health policy and to drive the significant change needed. We are actively looking at the available options and working with others throughout the public and private sectors to pursue this initiative.

ACKNOWLEDGEMENTS

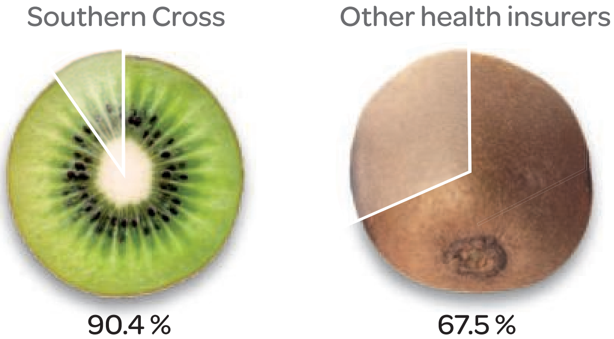
My thanks to the Board and staff for their hard work over the year. After six years with Southern Cross I will be retiring from the Board after this year's AGM. I wish the Board and incoming Chair, Greg Gent, all the very best.

2014 also saw a change in operational leadership at Southern Cross. After 12 years as the CEO of Southern Cross Healthcare Group, Dr Ian McPherson stepped down at the end of June. He is continuing to work with the Board and Society in a strategic advisory role until 30 June 2015. The Board would like to thank Dr McPherson for his valued contribution to Southern Cross and his ongoing drive to ensure New Zealanders receive the best possible value in healthcare.

As always, I would also like to offer a sincere thank you to our members for your continued support.

Graeme Hawkins
Chairman

% of premiums paid in claims



What you claimed for

155,000 elective surgeries

370,000 specialist consultations

784,000 GP visits

680,000 prescriptions

Chief Executive Officer's report

On occasion, we are asked by the media: Is health insurance worth it?

For several years now the Government has highlighted increases in the number of publicly funded elective surgeries. While this is to be commended, their numbers don't tell the full story. Demand for health services is ever-increasing. The reality is that many patients do not meet the criteria that will allow them onto the waiting list for publicly-funded surgery to begin with.

For 815,447 Southern Cross members, health insurance removes this uncertainty. When healthcare issues arise, it can be a stressful and painful time. Our members tell us they value the peace of mind which comes from knowing that, should they require elective healthcare, they can access services without delay or financial stress.

As a not-for-profit insurer, we see it as our responsibility to deliver our members the best possible value from their health insurance.

Every year, the price members are charged for medical procedures goes up. As a result, what we pay in claims rises, and this in turn has a direct impact on premiums. We can't control the volume of procedures our members require (nor would we want to) or justifiable medical cost increases. But, on behalf of our members, we can tackle pricing that is unreasonable and provide better certainty around costs. The Affiliated Provider programme, launched in 1997, is central to this objective.

EXPANDING THE AFFILIATED PROVIDER PROGRAMME

Contracting with providers is part of a long-term strategy to keep premium increases lower than they otherwise would be by dampening down medical inflation. Healthcare funders worldwide are implementing similar strategies.

There are currently agreements in place throughout New Zealand covering over 1,000 providers across 20 specialities. At present, over 34% of all Southern Cross claims are paid to Affiliated Providers, and our aim is to grow this to 60% by 2016.

Driving the expansion of the programme has been a steady growth in the number of procedures specified as 'Affiliated Provider only' in Southern Cross health insurance policies. This means Southern Cross members on most plans are reimbursed for these procedures only if they are carried out by an Affiliated Provider. Ten new procedures were added to the category of 'Affiliated Provider-only' cover in the 2014 financial year and more will be added in the coming year.

Before making a procedure Affiliated Provider only, we do our best to ensure we have a good geographical spread of providers so that our members are not unduly impacted. Our approach is to contract with all providers on an inclusive rather than exclusive basis – so long as the provider is willing to charge reasonable fees.

We are aware that there is resistance by some providers to this programme. However, we believe if provider pricing goes unchecked, access to private healthcare options will become increasingly difficult for many New Zealanders.

OUR MEMBERS' VIEWS

Using an Affiliated Provider also offers extra convenience for members. Affiliated Providers organise prior approval and process the claim on the member's behalf. This means the member does not have to submit a claim, and is not out of pocket while the claim is being processed.

In September 2013, over 850 members were surveyed about the Affiliated Provider programme. 91% of those surveyed said they were happy with and support it or any programme that helps manage costs and makes claiming easier. 71% said they would rather travel up to three hours to see an Affiliated Provider than pay an extra $1,200 for a procedure.

PETER TYNAN
CHIEF EXECUTIVE OFFICER

USER-FRIENDLY POLICIES

The benefits in our policies are continually reviewed to ensure they remain useful and relevant. When updating policies, we consider changes in the healthcare environment, and striking the right balance between premium affordability and the needs of our members. For example, specialist consultation payments were previously made according to a maximum amount, per consultation. These benefits now provide for maximum reimbursement of between $4,000 to $5,000 per claims year, which is simpler and will improve the payment levels for most members.

PREMIUM AFFORDABILITY TO THE FORE

We also manage premium affordability by closely monitoring the cost and effectiveness of new medical technology, procedures and services.

There are some technologies which add significant cost to treatment, without a corresponding benefit for the patient. We do our best to assess these via international literature and from clinical advice, and in general, only offer cover where there is a very clear clinical benefit to our members at an acceptable cost.

Opposing 'cost shifting' from public healthcare services (funded through taxation) is another area we closely monitor due to its potential impact on premiums. For example, members declined ACC funding for accidents or treatment injury have access to a Southern Cross ACC review service. This not only ensures the cost of our members' treatment is met by the right organisation, but that members receive any additional entitlements under their ACC cover, such as earnings compensation, rehabilitation and home help.

In the 2014 financial year, the Society worked with 319 members to seek review from ACC, resulting in a cost recovery of $1.7 million. We saw an additional $83,000 in savings for treatment costs the Society did not fund because the review was successful before the members' surgeries took place. Shoulder and knee injuries continue to make up the majority of review cases we assist our members with.

Southern Cross also identified a further $2.8 million that had already 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 $244,000 where the procedure was identified as an ACC treatment injury before payment was made.

SERVICE INNOVATION

The Society is continually working to make managing health insurance easier and more convenient for our members. Enhancing our online capability is a major focus. Long-term our initiatives also aim to lower operational costs.

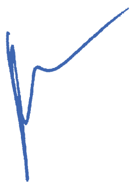
Our secure, online service 'My Southern Cross' now has over 53,000 registered users. Through their personal account members are able to view and update their contact details, apply for prior approval, track the progress of claims and choose to receive certain policy information online rather than by post. In December 2013, we added the ability to make a claim through My Southern Cross, creating more potential time and cost savings.

Southern Cross Health Society Easy-claim, an electronic claiming service exclusively for Southern Cross members, has also experienced strong expansion over the year.

Members can now claim using their member card, at over 850 healthcare providers. Easy-claim allows the provider to submit online claims on behalf of Southern Cross members for eligible healthcare services.

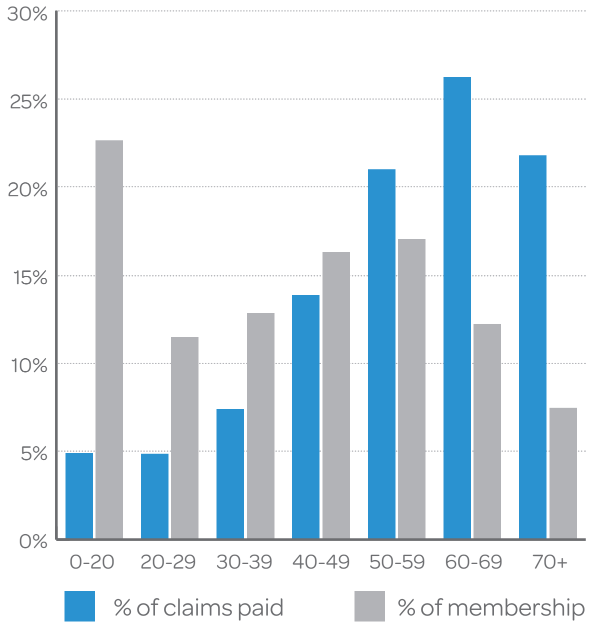
Providers across a range of specialties have signed up including pharmacies, audiology, dental, optometrist and physiotherapy. In the past year, the option to join Easy-claim was extended to GPs and to date over 40 have come on board.

To close, I would like to thank all members for their continued support. As a not-for-profit organisation, we are committed to ensuring you receive the best value and service from us.



Peter Tynan
Chief Executive Officer

The older we get, the more we claim



Affiliated Providers at a glance

Established in 1997

1,000 providers across 20 specialities

Represent 34% of all claims costs

Help mitigate impact of rising treatment costs on member premiums

Provider looks after prior approval and claim for members

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 2014 are:
Graeme S Hawkins (Chairman)
Dr Douglas D Baird
Catherine M Drayton
Carole B Durbin
Gregory W Gent
Elizabeth M Hickey
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 2014 are: Carole Durbin, Graeme Hawkins and Keith Taylor.

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), Catherine Drayton, Graeme Hawkins 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 – Keith Taylor (Chairman), Carole Durbin and Graeme Hawkins.

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. On 28 August 2013 the Audit Committee noted that KPMG were able to continue as external auditors under Rule 11.1, so were deemed to be reappointed for the year ending 30 June 2014.

LOANS TO DIRECTORS

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

Board of Directors

GRAEME HAWKINS

(BSC, BCom, ACA, DistFInstD)

Chairman

Graeme Hawkins has been a professional director for more than 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 Acting Chairman of 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

(BSc, MB, ChB, DipObst)

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 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 is also a Trustee of Southern Cross Health Trust.

CATHERINE DRAYTON

(BCom, LLB, FCA)

Catherine Drayton was elected to the Southern Cross Board in 2013. She is a professional, non-executive director on a variety of boards including engineering consultancy company BECA Group Limited, Christchurch International Airport and Ngai Tahu Holdings Corporation Limited. Past board appointments include Meridian Energy. Born, bred and resident in Christchurch, she is a member of the University of Canterbury Council and chair of the audit and risk committee for the Christchurch Earthquake Recovery Authority (CERA). Ms Drayton is a former partner in charge of assurance and advisory services for Pricewaterhouse Coopers in Central and Eastern Europe. She is a member of the NZ Institute of Chartered Accountants and sits on the Institute's board. Ms Drayton is also a Trustee of Southern Cross Health Trust.

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. Ms Durbin is also 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. Ms Durbin is also a Trustee of Southern Cross Health Trust.

Board of Directors (L to R)

Catherine Drayton, Doug Baird, Liz Hickey, Greg Gent, Graeme Hawkins, Keith Taylor. Inset: Carole Durbin

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.

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 a trustee of the University of Auckland Foundation, and a director of Diabetes New Zealand Inc. 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, and is a Fellow and past-President of the NZ Institute of Chartered Accountants. Ms Hickey is also a Trustee of Southern Cross Health Trust.

KEITH TAYLOR

(BSc, BCA, FIA, F Inst D)

Keith Taylor was elected to the Southern Cross Board in November 2010 and was appointed a Society Trustee in 2013. Mr Taylor 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 Holdings Limited and Speirs Group, and deputy chair of the Reserve Bank of New Zealand and the Earthquake Commission. He is a director of Port Marlborough and Butland Holdings, 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. Mr Taylor is also a Trustee of Southern Cross Health Trust.

Director meeting attendance for the year ended 30 June 2014

	Society Board	AGM	Trustees	Strategic Workshops	Audit Committee	Remuneration Committee	Nomination Committee	Investment Committee	Group Strategic Meetings
GS Hawkins	9	1	4	1	6	2	5	4	9
Dr DD Baird	9	1		1		2	5		9
Ms CM Drayton	5			1	3				5
Ms CB Durbin	9	1	4	1		2	5	4	9
GW Gent	9	1		1		2	4		9
EM Hickey	9	1		1	6		3		9
PJ Meyer	4	1	2		3			2	4
KB Taylor	9	1	2	1	6			4	9

CM Drayton appointed as a Director on 5 December 2013, and to the Audit Committee on 11 February 2014

PJ Meyer retired as a Director and Trustee on 5 December 2013

KB Taylor appointed as a Trustee on 5 December 2013

Financial statements

The Southern Cross Medical Care Society

STATEMENTS OF COMPREHENSIVE INCOME
for the year ended 30 June 2014

	NOTE	GROUP		SOCIETY	
		2014 $000	2013 $000	2014 $000	2013 $000
Premium revenue		768,410	725,483	768,410	725,483
Net claims expense	4	694,484	639,053	694,484	639,053
Underwriting surplus		73,926	86,430	73,926	86,430
Operating expenses	5	92,965	87,022	93,540	86,234
Operating (deficit)/surplus		(19,039)	(592)	(19,614)	196
Net investment and other income	6	18,649	21,939	18,548	21,910
(Deficit)/surplus before taxation		(390)	21,347	(1,066)	22,106
Taxation	7	–	–	–	–
(Deficit)/surplus after taxation		(390)	21,347	(1,066)	22,106
Other comprehensive income		–	–	–	–
Total comprehensive (deficit)/surplus for the year		(390)	21,347	(1,066)	22,106

The accompanying notes form part of these financial statements

STATEMENTS OF CHANGES IN RESERVES
for the year ended 30 June 2014

2014	GROUP Retained Surpluses $000	GROUP Total Reserves $000	SOCIETY Retained Surpluses $000	SOCIETY Total Reserves $000
Opening balance	394,733	394,733	395,374	395,374
Total comprehensive deficit:				
Deficit after taxation	(390)	(390)	(1,066)	(1,066)
Other comprehensive income	–	–	–	–
Total comprehensive deficit	(390)	(390)	(1,066)	(1,066)
Closing balance	394,343	394,343	394,308	394,308

2013	GROUP Retained Surpluses $000	GROUP Total Reserves $000	SOCIETY Retained Surpluses $000	SOCIETY Total Reserves $000
Opening balance	373,386	373,386	373,268	373,268
Total comprehensive surplus:				
Surplus after taxation	21,347	21,347	22,106	22,106
Other comprehensive income	–	–	–	–
Total comprehensive surplus	21,347	21,347	22,106	22,106
Closing balance	394,733	394,733	395,374	395,374

The accompanying notes form part of these financial statements

STATEMENTS OF FINANCIAL POSITION
as at 30 June 2014

	NOTE	GROUP 2014 $000	GROUP 2013 $000	SOCIETY 2014 $000	SOCIETY 2013 $000
Assets					
Cash and cash equivalents		1,966	2,258	1,827	2,130
Premium and other receivables	8	69,941	64,897	70,054	65,392
Investments	9	489,604	492,035	489,552	492,034
Investment in subsidiaries	10	–	–	–	–
Property and equipment	11	12,744	11,452	12,744	11,452
Intangible assets	12	15,917	11,259	15,917	11,259
Total assets		590,172	581,901	590,094	582,267
Liabilities					
Payables	13	22,017	18,252	21,974	17,977
Employee benefits	14	7,746	9,362	7,746	9,362
Insurance contract liabilities	15	166,066	159,554	166,066	159,554
Total liabilities		195,829	187,168	195,786	186,893
Net assets		394,343	394,733	394,308	395,374
Reserves		394,343	394,733	394,308	395,374

For and on behalf of the Board

G S Hawkins, **Chairman** Date: 2 September 2014

E M Hickey, **Director** Date: 2 September 2014

The accompanying notes form part of these financial statements

The Southern Cross Medical Care Society

STATEMENTS OF CASH FLOWS
for the year ended 30 June 2014

	NOTE	GROUP 2014 $000	GROUP 2013 $000	SOCIETY 2014 $000	SOCIETY 2013 $000
Cash flows from/(to) operating activities					
Premium revenue		769,424	725,905	769,424	725,905
Interest received		20,875	21,141	20,872	21,137
Other income		173	173	75	148
Payment of claims		(691,948)	(639,170)	(691,948)	(639,170)
Payments to employees		(43,232)	(38,697)	(43,232)	(38,579)
Payments to suppliers		(43,309)	(42,521)	(43,270)	(42,231)
Net cash flows from operating activities	19	11,983	26,831	11,921	27,210
Cash flows from/(to) investing activities					
Proceeds from sale of property and equipment		265	405	265	5
Payments for property and equipment		(5,699)	(799)	(5,699)	(799)
Payments for intangible assets		(7,589)	(4,910)	(7,589)	(4,910)
Net receipts/(payments) for investments		748	(22,961)	799	(22,962)
Net cash flows to investing activities		(12,275)	(28,265)	(12,224)	(28,666)
Net decrease in cash and cash equivalents		(292)	(1,434)	(303)	(1,456)
Opening cash and cash equivalents		2,258	3,692	2,130	3,586
Closing cash and cash equivalents		1,966	2,258	1,827	2,130

The accompanying notes form part of these financial statements

NOTES TO THE FINANCIAL STATEMENTS
for the year ended 30 June 2014

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 as at, and for the year ended 30 June 2014. The consolidated financial statements are for the Group comprising the Society and its subsidiaries: Southern Cross Health Services Limited, Southern Cross Healthcare Limited (non-trading) and Activa Health Limited (non-trading), 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 2 September 2014.

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 15: Insurance contract liabilities
- Note 16: Actuarial information
- Note 17: Risk management
- Note 21: 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.

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".

1. STATEMENT OF ACCOUNTING POLICIES (CONTINUED)

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

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 17 "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.

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.

1. STATEMENT OF ACCOUNTING POLICIES (CONTINUED)

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.

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.

1. STATEMENT OF ACCOUNTING POLICIES (CONTINUED)

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.

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 OR AMENDED FINANCIAL REPORTING STANDARDS ADOPTED DURING THE PERIOD

NZ IFRS 13 - Fair Value Measurement (2012) sets out improvements to the definition of fair value and also sets out a single framework for measuring fair value and requires new disclosures. This standard became effective from 1 July 2013 and did not have a material impact on the Group and Society's financial statements.

Other new reporting standards, amendments to standards and interpretations that became effective in the current financial year were not applicable to the Group and Society or had no impact on these financial statements.

3. 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 2014, and have not been applied in preparing these financial statements:

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

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 2017. 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.

4. NET CLAIMS EXPENSE

	GROUP		SOCIETY	
	2014 $000	2013 $000	2014 $000	2013 $000
Claims incurred relating to risks borne in current financial year	692,417	638,655	692,417	638,655
Claims incurred relating to risks borne in previous financial years	1,236	(1,568)	1,236	(1,568)
Movement in provision for claims handling costs	55	725	55	725
Movement in risk margin	72	82	72	82
Net claims incurred	693,780	637,894	693,780	637,894
Movement in provision for unexpired risk	704	1,159	704	1,159
	694,484	639,053	694,484	639,053

NOTES TO THE FINANCIAL STATEMENTS (continued)
for the year ended 30 June 2014

5A. OPERATING EXPENSES

Operating expenses include	GROUP 2014 $000	GROUP 2013 $000	SOCIETY 2014 $000	SOCIETY 2013 $000
Auditor's remuneration:				
– Audit and review of financial statements	210	208	210	208
– Other services	45	72	45	72
Depreciation	3,205	3,119	3,205	3,119
Amortisation of intangible assets	3,487	2,793	3,487	2,793
Directors' fees	359	361	359	361
Employee benefits expense	41,616	39,521	41,616	39,403
Contributions to defined contribution plan	56	55	56	55
Rental of premises	4,525	4,524	4,524	4,524
Provision for impairment (gain)/loss on amounts receivable from subsidiaries	–	–	585	336
(Gains)/losses on disposal of property and equipment	806	(3)	806	(3)

Auditor's remuneration for other services disclosed above consists of reviewing solvency returns, accounting and advisory services and, in the year ended 30 June 2013, AGM vote scrutineering .

5B. OPERATING EXPENSES

Operating expenses consist of	GROUP 2014 $000	GROUP 2013 $000	SOCIETY 2014 $000	SOCIETY 2013 $000
Policy acquisition	10,918	9,223	10,918	9,223
Policy administration	30,875	30,889	30,875	30,889
Claims handling	10,685	10,011	10,685	10,011
Other operating expenses	40,487	36,899	41,062	36,111
	92,965	87,022	93,540	86,234

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

NOTES TO THE FINANCIAL STATEMENTS (continued)
for the year ended 30 June 2014

6. NET INVESTMENT AND OTHER INCOME

	GROUP		SOCIETY	
	2014 $000	2013 $000	2014 $000	2013 $000
Interest income	20,160	21,577	20,156	21,574
Net gains/(losses) on investments at fair value through profit or loss	(1,683)	210	(1,683)	210
Fee and other income	172	152	75	126
	18,649	21,939	18,548	21,910

7. TAXATION

	GROUP	
Reconciliation of effective tax rate	2014 $000	2013 $000
Net (deficit)/surplus before tax	(390)	21,347
Income tax payable at the domestic tax rate of 28%	(109)	5,977
Effect of exempt deficit/(surplus)	135	(6,284)
Tax effect of change in unrecognised temporary differences	(56)	(13)
Tax on current year deficit/(surplus) for which no deferred tax asset was recognised	30	320
	–	–

The aggregate amount of temporary differences arising in the subsidiaries for which a deferred tax asset has not been recognised is $144,000 at 30 June 2014 (30 June 2013: $344,000).

The Group has unrecognised tax losses carried forward of $32,107,000 at 30 June 2014 (30 June 2013: $32,000,000).

8. PREMIUM AND OTHER RECEIVABLES

	GROUP		SOCIETY	
	2014 $000	2013 $000	2014 $000	2013 $000
Premium accounts receivable	58,028	54,746	58,028	54,746
Interest receivable	3,434	4,150	3,434	4,150
Other accounts receivable	7,739	5,318	7,735	5,289
Amounts owed by related parties	738	655	855	1,179
Asset disposal proceeds receivable	2	28	2	28
	69,941	64,897	70,054	65,392

The fair value of premium and other receivables approximates the carrying amount.

Premium and other receivables is a current asset.

NOTES TO THE FINANCIAL STATEMENTS (continued)
for the year ended 30 June 2014

9. INVESTMENTS

	GROUP 2014 $000	GROUP 2013 $000	SOCIETY 2014 $000	SOCIETY 2013 $000
At fair value through profit or loss				
New Zealand Government stock	509	527	509	527
State owned enterprise bonds	7,106	20,402	7,106	20,402
Local authority stock	18,577	47,515	18,577	47,515
Other bonds	49,672	55,575	49,672	55,575
Bank deposits, commercial paper and floating rate notes	413,740	368,016	413,688	368,015
	489,604	492,035	489,552	492,034
Current assets	334,250	319,655	334,198	319,654
Non-current assets	155,354	172,380	155,354	172,380
	489,604	492,035	489,552	492,034

10. 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 7 May 2013, the Society Directors resolved to discontinue the Activa product provided by Activa Health Limited effective as at 30 June 2013. There was no material effect on the Society's financial statements.

11. PROPERTY AND EQUIPMENT

	GROUP				
	Computer equipment $000	Other fixed assets $000	Leasehold improvements $000	Work in progress $000	Total $000
At 30 June 2014					
Cost	21,216	3,522	10,309	153	35,200
Accumulated depreciation	(18,554)	(1,332)	(2,570)	–	(22,456)
Closing balance	2,662	2,190	7,739	153	12,744
Reconciliation of movement in property and equipment					
Opening balance	2,738	1,885	6,248	581	11,452
Additions	1,305	1,036	3,076	153	5,570
Transfers from work in progress	278	–	303	(581)	–
Disposals	–	(215)	(858)	–	(1,073)
Depreciation	(1,659)	(516)	(1,030)	–	(3,205)
Closing balance	2,662	2,190	7,739	153	12,744

	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 cost	23,159	2,596	8,306	481	34,542
Opening accumulated depreciation	(19,291)	(561)	(1,206)	–	(21,058)
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

NOTES TO THE FINANCIAL STATEMENTS (continued)
for the year ended 30 June 2014

11. PROPERTY AND EQUIPMENT (CONTINUED)

SOCIETY	Computer equipment $000	Other fixed assets $000	Leasehold improvements $000	Work in progress $000	Total $000
At 30 June 2014					
Cost	21,216	3,522	10,309	153	35,200
Accumulated depreciation	(18,554)	(1,332)	(2,570)	–	(22,456)
Closing balance	2,662	2,190	7,739	153	12,744
Reconciliation of movement in property and equipment					
Opening balance	2,738	1,885	6,248	581	11,452
Additions	1,305	1,036	3,076	153	5,570
Transfers from work in progress	278	–	303	(581)	–
Disposals	–	(215)	(858)	–	(1,073)
Depreciation	(1,659)	(516)	(1,030)	–	(3,205)
Closing balance	2,662	2,190	7,739	153	12,744

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 cost	23,159	2,596	8,306	481	34,542
Opening accumulated depreciation	(19,291)	(561)	(1,206)	–	(21,058)
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

Other fixed assets include motor vehicles and office equipment.

Property and equipment is a non-current asset.

12. INTANGIBLE ASSETS

	GROUP		
	Computer software $000	Work in progress $000	Total $000
At 30 June 2014			
Cost	46,936	2,311	49,247
Accumulated amortisation	(33,330)	–	(33,330)
Closing balance	13,606	2,311	15,917
Reconciliation of movement in intangible assets			
Opening balance	8,404	2,855	11,259
Additions	6,208	1,937	8,145
Transfers from work in progress	2,481	(2,481)	–
Amortisation	(3,487)	–	(3,487)
Closing balance	13,606	2,311	15,917

	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 cost	34,025	2,275	36,300
Opening accumulated amortisation	(27,158)	–	(27,158)
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

12. INTANGIBLE ASSETS (CONTINUED)

	SOCIETY		
	Computer software $000	Work in progress $000	Total $000
At 30 June 2014			
Cost	46,936	2,311	49,247
Accumulated amortisation	(33,330)	–	(33,330)
Closing balance	13,606	2,311	15,917
Reconciliation of movement in intangible assets			
Opening balance	8,404	2,855	11,259
Additions	6,208	1,937	8,145
Transfers from work in progress	2,481	(2,481)	–
Amortisation	(3,487)	–	(3,487)
Closing balance	13,606	2,311	15,917

	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 cost	33,916	2,275	36,191
Opening accumulated amortisation	(27,049)	–	(27,049)
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

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.

13. PAYABLES

	GROUP		SOCIETY	
	2014 $000	2013 $000	2014 $000	2013 $000
Accounts payable	18,546	14,888	18,503	14,613
Deferred income - lease inducement	3,471	3,364	3,471	3,364
	22,017	18,252	21,974	17,977
Current	18,945	15,322	18,902	15,047
Non-current	3,072	2,930	3,072	2,930
	22,017	18,252	21,974	17,977

14. EMPLOYEE BENEFITS

	GROUP		SOCIETY	
	2014 $000	2013 $000	2014 $000	2013 $000
Employee entitlements	4,266	5,762	4,266	5,762
Employee benefits	1,180	1,150	1,180	1,150
Post-employment benefits	2,300	2,450	2,300	2,450
	7,746	9,362	7,746	9,362
Current	4,586	5,934	4,586	5,934
Non-current	3,160	3,428	3,160	3,428
	7,746	9,362	7,746	9,362

15. INSURANCE CONTRACT LIABILITIES

	GROUP		SOCIETY	
	2014 $000	2013 $000	2014 $000	2013 $000
Provision for outstanding claims (refer note 15a)	76,833	75,321	76,833	75,321
Provision for unearned premium (refer note 15c)	79,381	74,915	79,381	74,915
Provision for unexpired risk (refer note 15d)	9,172	8,468	9,172	8,468
Other insurance provisions	680	850	680	850
	166,066	159,554	166,066	159,554

15. INSURANCE CONTRACT LIABILITIES (CONTINUED)

a. Provision for outstanding claims

	GROUP		SOCIETY	
	2014 $000	2013 $000	2014 $000	2013 $000
Central estimate of outstanding claims liability	70,331	68,946	70,331	68,946
Claims handling costs	2,843	2,788	2,843	2,788
Risk margin	3,659	3,587	3,659	3,587
Closing balance	76,833	75,321	76,833	75,321

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		SOCIETY	
	2014 $000	2013 $000	2014 $000	2013 $000
Opening balance	75,321	73,608	75,321	73,608
Amounts utilised during the year	(68,226)	(64,440)	(68,226)	(64,440)
Additional provision/(reversal of unused provision)	1,236	(1,568)	1,236	(1,568)
Amounts provided during the year	68,375	66,914	68,375	66,914
Movement in claims handling costs	55	725	55	725
Movement in risk margin	72	82	72	82
Closing balance	76,833	75,321	76,833	75,321

c. Reconciliation of movement in provision for unearned premium

	GROUP		SOCIETY	
	2014 $000	2013 $000	2014 $000	2013 $000
Opening balance	74,915	72,828	74,915	72,828
Premiums written in the year	772,876	727,570	772,876	727,570
Premiums earned during the year	(768,410)	(725,483)	(768,410)	(725,483)
Closing balance	79,381	74,915	79,381	74,915

15. INSURANCE CONTRACT LIABILITIES (CONTINUED)

d. Provision for unexpired risk

	GROUP		SOCIETY	
	2014 $000	2013 $000	2014 $000	2013 $000
Present value of expected future cash flows for claims and expenses	85,528	80,567	85,528	80,567
Risk margin	3,421	3,223	3,421	3,223
Unearned premiums	(79,381)	(74,915)	(79,381)	(74,915)
Write-down of deferred acquisition costs	(396)	(407)	(396)	(407)
Closing balance	9,172	8,468	9,172	8,468

e. Reconciliation of movement in provision for unexpired risk

	GROUP		SOCIETY	
	2014 $000	2013 $000	2014 $000	2013 $000
Opening balance	8,468	7,309	8,468	7,309
Reversal of opening balance	(8,468)	(7,309)	(8,468)	(7,309)
Net liability for unexpired risk recognised during the year	6,147	5,652	6,147	5,652
Risk margin	3,421	3,223	3,421	3,223
Write-down of deferred acquisition costs	(396)	(407)	(396)	(407)
Closing balance	9,172	8,468	9,172	8,468

16. ACTUARIAL INFORMATION

Estimates of the outstanding claims and unexpired risk as at 30 June 2014 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 18 August 2014. 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. 4.1: Valuations of General Insurance Claims, 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 2014, 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.

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 2014 (30 June 2013: $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 2014 (30 June 2013: 5%). The risk margin was determined with the objective of achieving at least 75% probability of sufficiency of the outstanding claims provision.

16. ACTUARIAL INFORMATION (CONTINUED)

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 69% to 115% (30 June 2013: 71% to 113%) of the monthly average.
3. Historical claims inflation 7.5% p.a. (30 June 2013: 7.0%), 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 2013: 4%) of the underlying claims amounts based on an analysis of administration expenses.

The average weighted term from 30 June 2014 to the expected settlement date for claims included in the liability for outstanding claims is 73 days (30 June 2013: 75 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 2014.

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 2014 (30 June 2013: 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. 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 73% to 112% (30 June 2013: 74% to 111%) of the monthly average.
3. Expenses based on the business plan for 2014/15, 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.

17. 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 21).

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 16.

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 2014 (2013: nil) in excess of policy.

17. RISK MANAGEMENT (CONTINUED)

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

	GROUP 2014 $000	GROUP 2013 $000	SOCIETY 2014 $000	SOCIETY 2013 $000
AAA	–	266	–	266
AA	312,603	289,778	312,551	289,777
A	96,190	93,812	96,190	93,812
BBB	57,993	53,535	57,993	53,535
Non-rated	22,818	54,644	22,818	54,644
	489,604	492,035	489,552	492,034

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 2013: 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 2014 $000	GROUP 2013 $000	SOCIETY 2014 $000	SOCIETY 2013 $000
On call	8,806	7,027	8,754	7,026
0-6 months	215,818	186,372	215,818	186,372
7-12 months	109,626	126,257	109,626	126,257
1-2 years	52,414	62,729	52,414	62,729
2-5 years	94,765	96,473	94,765	96,473
Beyond 5 years	8,175	13,177	8,175	13,177
	489,604	492,035	489,552	492,034

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.

17. RISK MANAGEMENT (CONTINUED)

c. Market risks

I. Foreign currency risk

At 30 June 2014, the Group had assets of $277,000 and no liabilities denominated in foreign currencies (30 June 2013: assets of $292,000 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 investment in bank deposits, commerical paper and floating rate notes are susceptible to changes in interest rates. The following analysis shows the impact of a change in interest rates on the cash flows (comparative information has been restated to comply with the current year presentation):

	GROUP AND SOCIETY	
	2014 $000	2013 $000
Impact of increase in interest rates by 100 basis points on cash flows	3,028	2,643
Impact of decrease in interest rates by 100 basis points on cash flows	(3,028)	(2,643)

(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	
	2014 $000	2013 $000
Impact of increase in interest rates by 100 basis points on surplus or deficit before taxation	(2,300)	(2,792)
Impact of decrease in interest rates by 100 basis points on surplus or deficit before taxation	2,345	2,859

(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.

17. RISK MANAGEMENT (CONTINUED)

	GROUP			
	Level 1 $000	Level 2 $000	Level 3 $000	Total $000
30 June 2014				
New Zealand Government stock	509	–	–	509
State owned enterprise bonds	–	7,106	–	7,106
Local authority stock	–	18,577	–	18,577
Other bonds	–	49,672	–	49,672
Bank deposits, commercial paper and floating rate notes	8,806	404,934	–	413,740
Total investments	9,315	480,289	–	489,604

	GROUP			
	Level 1 $000	Level 2 $000	Level 3 $000	Total $000
30 June 2013				
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

17. RISK MANAGEMENT (CONTINUED)

	SOCIETY			
	Level 1 $000	Level 2 $000	Level 3 $000	Total $000
30 June 2014				
New Zealand Government stock	509	–	–	509
State owned enterprise bonds	–	7,106	–	7,106
Local authority stock	–	18,577	–	18,577
Other bonds	–	49,672	–	49,672
Bank deposits, commercial paper and floating rate notes	8,754	404,934	–	413,688
Total investments	9,263	480,289	–	489,552

	SOCIETY			
	Level 1 $000	Level 2 $000	Level 3 $000	Total $000
30 June 2013				
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

Investments were independently valued by Bancorp Treasury Services Limited at 30 June 2014 and 30 June 2013. 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 2013: level 1).

18. 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") (non-trading)	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.

During the last financial year ended 30 June 2013, the Society charged Benefits a fee for enabling marketing opportunities to the membership and purchased an investment bond from Benefits for $1,015,000, 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 $10,680,000 (30 June 2013: $10,095,000).

The amount of transactions between the Group entities are:

	PAYABLES		RECEIVABLES	
	2014 $000	2013 $000	2014 $000	2013 $000
Society	–	–	–	56
Activa	–	56	–	–

The outstanding balances between the Group entities are:

	PAYABLES		RECEIVABLES	
	2014 $000	2013 $000	2014 $000	2013 $000
Society	–	–	117	524
Health Services	59	58	–	–
Activa	58	466	–	–

18. RELATED PARTIES (CONTINUED)

The amount of transactions with other related parties are:

	GROUP		SOCIETY	
	2014 $000	2013 $000	2014 $000	2013 $000
Sale of services	6,750	6,597	6,750	6,597
Purchase of services	121	242	121	242
Purchase of investments	–	1,015	–	1,015

The outstanding balances with other related parties are:

	GROUP		SOCIETY	
	2014 $000	2013 $000	2014 $000	2013 $000
Balances outstanding on sales	761	757	761	757
Balances outstanding on purchases	23	102	23	102

b. Remuneration of Directors

Directors' fees paid by the Society for the year ended 30 June 2014 were as follows:

	2014 Amount $	2013 Amount $
Director		
Dr D D Baird	45,250	45,250
C M Drayton - appointed 5 December 2013	24,547	–
C B Durbin	49,000	49,000
G W Gent	45,250	45,250
G S Hawkins (Chairman)	80,000	80,000
E M Hickey	47,000	47,000
P J Meyer - retired 5 December 2013	20,823	48,500
K B Taylor	47,250	46,000
Trustee		
C B Durbin	–	–
G S Hawkins	–	–
P J Meyer - retired 5 December 2013	–	–
K B Taylor - appointed 5 December 2013	–	–

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.

NOTES TO THE FINANCIAL STATEMENTS (continued)
for the year ended 30 June 2014

18. RELATED PARTIES (CONTINUED)

c. Remuneration of key management personnel

	GROUP		SOCIETY	
	2014 $000	2013 $000	2014 $000	2013 $000
Salaries and other short-term benefits	2,842	2,721	2,842	2,721
Post-employment benefits	86	74	86	74

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.

19. RECONCILIATION OF NET SURPLUS/(DEFICIT) WITH NET CASH FLOWS FROM OPERATING ACTIVITIES

	GROUP		SOCIETY	
	2014 $000	2013 $000	2014 $000	2013 $000
Net surplus/(deficit) after taxation	(390)	21,347	(1,066)	22,106
Add/(less) non-cash items:				
Depreciation	3,205	3,119	3,205	3,119
Amortisation of intangible assets	3,487	2,793	3,487	2,793
Provision for impairment loss on amounts receivable from subsidiaries	–	–	585	336
Add items classified as investing activities:				
(Gains)/losses on disposal of property and equipment	806	(3)	806	(3)
Net (gains)/losses on investments at fair value through profit or loss	1,683	(210)	1,683	(210)
Movement in receivables and payables relating to investing activities	(425)	(691)	(1,012)	(627)
Add/(less) movements in working capital items:				
Receivables	(5,045)	(1,207)	(4,662)	(1,943)
Payables	3,764	(4,141)	3,997	(4,185)
Other insurance provisions	(170)	40	(170)	40
Employee benefits	(1,615)	825	(1,615)	825
Provision for outstanding claims	1,512	1,713	1,512	1,713
Provision for unearned premium	4,467	2,087	4,467	2,087
Provision for unexpired risk	704	1,159	704	1,159
Net cash flows from operating activities	11,983	26,831	11,921	27,210

20. CREDIT RATING

On 2nd July 2013 Standard & Poor's reaffirmed the Society's Insurer Financial Strength Rating at A+ under its new global insurance industry rating methodology. On 20 February 2014, Standard & Poor's again reaffirmed the Society's Insurer Financial Strength Rating at A+. This signifies the insurer "has strong financial security characteristics".

21. 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 $394.3 million (2013: $395.4 million) represents the retained surpluses of the Society. Capital of the Group of $394.3 million (30 June 2013: $394.7 million) includes the reserves of the Society's non-insurance subsidiaries set out in Note 1.

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 positive solvency margin, meaning that the actual solvency capital position exceeds the minimum required under the solvency standard.

During the year ended 30 June 2014 the Society complied with all externally imposed capital requirements. At 30 June 2014 the solvency ratio (actual solvency capital divided by minimum solvency capital required) was 5.25 and the solvency margin was $306.3 million.

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 2014 this margin was 38.81% 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.

22. LEASE COMMITMENTS

At 30 June 2014 commitments under operating leases in respect of payments due to be made in the following years were:

	GROUP		SOCIETY	
	2014 $000	2013 $000	2014 $000	2013 $000
Within 1 year	5,501	5,543	5,501	5,543
Between 1 and 2 years	5,251	5,050	5,251	5,050
Between 2 and 5 years	15,322	14,806	15,322	14,806
Greater than 5 years	18,667	14,267	18,667	14,267
	44,741	39,666	44,741	39,666

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 Society entered into a variation in relation to the agreement to lease the Auckland premises in April 2014 for a lease term of 9 years, commencing 1 April 2014, thereby extending the term of the original agreement to lease by 2 years. 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.

23. CAPITAL COMMITMENTS

The Group had capital commitments of $540,000 at 30 June 2014 (2013: $2,276,000).

24. CONTINGENT LIABILITIES

The Group had no contingent liabilities at 30 June 2014 (2013: 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 40. The financial statements comprise the statements of financial position as at 30 June 2014, 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 40:

- 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 2014 and of the financial performance and cash flows of the Society and the Group 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 the Society as far as appears from our examination of those records.

KPMG

4 September 2014
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 2014

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 2014 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 being a provider of actuarial services.

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 2014 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 2014 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 the purpose for which it is intended.

Yours sincerely

J M Smeed.

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

Anita Samu.

Anita Samu
Fellow of the New Zealand Society of Actuaries

2 September 2014

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0800 800 181

Southern Cross
Health Society