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Southern Cross Medical Care Society Group

2020 Annual Report – Consolidated Financial Statements

These Consolidated Financial Statements, together with the 2020 Annual Report Summary, constitute the Annual Report for the purposes of the Rules of the Society. For a copy of the Summary please visit southerncross.co.nz/annualreport

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The Southern Cross Medical Care Society Group

**Consolidated financial statements
for the year ended**

30 June 2020

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CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME AND CHANGES IN RESERVES

for the year ended 30 June 2020

	Note	2020 \$000	2019 \$000
Premium revenue	2,11	1,146,538	1,080,364
Less: outward reinsurance expense	11	(18)	-
Net premium revenue		1,146,520	1,080,364
Claims expense	2,5	(980,869)	(967,655)
Less: reinsurance recoveries		(9)	-
Less: third party recoveries		3,967	3,989
Net claims expense	5	(976,911)	(963,666)
Underwriting surplus		169,609	116,698
Operating expenses	9	(163,949)	(133,916)
Operating surplus/(deficit)		5,660	(17,218)
Net investment and other income	8	18,976	27,942
Interest expense	21	(223)	-
Surplus before taxation		24,413	10,724
Taxation	16	7,996	-
Surplus after taxation		32,409	10,724
Other comprehensive income		-	-
Total comprehensive income		32,409	10,724
Opening balance of reserves		438,751	428,027
Closing balance of reserves		471,160	438,751

The above consolidated statement of comprehensive income and changes in reserves should be read in conjunction with the accompanying notes.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION
as at 30 June 2020

	Note	2020 \$000	2019 \$000
Assets			
Cash and cash equivalents	10	39,538	10,034
Premium and other receivables	2,11	108,260	97,749
Investments	7	534,700	492,479
Property and equipment	12	5,749	7,165
Intangible assets	12	39,335	38,488
Right-of-use assets	13,21	3,754	-
Deferred tax assets	16	7,545	-
Total assets		738,881	645,915
Liabilities			
Payables and other liabilities	14	29,059	15,321
Employee benefits	15	11,167	9,297
Lease liabilities	13,21	4,086	-
Insurance contract liabilities	4	222,373	182,546
Deferred tax liabilities	16	1,036	-
Total liabilities		267,721	207,164
Net assets		471,160	438,751
Reserves		471,160	438,751

Authorised on behalf of the Board of Directors on 3 September 2020.

G W Gent
Chairman

C M Drayton
Director

The above consolidated statement of financial position should be read in conjunction with the accompanying notes.

CONSOLIDATED STATEMENT OF CASH FLOWS

for the year ended 30 June 2020

	Note	2020 \$000	2019 \$000
Cash flows from/(to) operating activities			
Premium revenue received		1,154,979	1,079,762
Interest received		7,624	8,341
Other income received		4,497	5,812
Payment of claims		(955,296)	(964,102)
Payments to employees		(61,843)	(57,520)
Payments to suppliers		(67,830)	(53,241)
Net cash flows from operating activities		82,131	19,052
Cash flows (to)/from investing activities			
Payments for property and equipment		(1,472)	(1,136)
Payments for intangible assets		(6,125)	(19,309)
Net (purchases)/sales of investments		(35,366)	2,902
Purchase of pet insurance business	20	(8,077)	-
Cash and cash equivalents acquired with the purchase of pet insurance business	20	3,411	-
Net cash flows to investing activities		(47,629)	(17,543)
Cash flows (to)/from financing activities			
Repayment of lease liabilities		(4,775)	-
Interest paid		(223)	-
Net cash flows to financing activities	21	(4,998)	-
Net increase in cash and cash equivalents		29,504	1,509
Opening cash and cash equivalents		10,034	8,525
Closing cash and cash equivalents		39,538	10,034
RECONCILIATION OF SURPLUS AFTER TAXATION TO NET CASH FLOWS FROM OPERATING ACTIVITIES			
Surplus after taxation		32,409	10,724
Adjustments for non-cash items included in surplus after taxation:			
Depreciation and amortisation	12,13a	18,362	16,235
Interest expense	13b,21	223	-
Impairment of assets	12	3,657	4,761
Net gains on investments at fair value through profit or loss	8	(6,855)	(13,460)
Changes in assets and liabilities:			
Premium and other receivables		4,369	(9,037)
Interest receivable		-	(329)
Payables and other liabilities		15,694	4,614
Net deferred taxation		(7,996)	-
Insurance contract liabilities		22,268	5,544
Net cash flows from/(to) operating activities		82,131	19,052

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

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 30 June 2020

1 BASIS OF ACCOUNTING

The notes to the financial statements contain detailed financial information and the accounting policies that are considered relevant and material to the understanding of the financial performance and financial position.

Additional signposting has been used throughout the notes to the financial statements to assist readers in understanding the key information in the financial statements.

Signpost



Basis of preparation



Accounting policy



Management judgements and estimates

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 primary activity is the provision of health insurance and its registered office is Level 1, EY Building, 2 Takutai Square 1010, Auckland.

The Society is a licenced insurer under the Insurance (Prudential Supervision) Act 2010. It is deemed to be a financial markets conduct reporting entity under Part 7 of the Financial Markets Conduct Act 2013 and therefore a Tier 1 reporting entity for financial reporting purposes.

The consolidated financial statements are for the Group comprising the Society and its subsidiaries: Southern Cross Insurance Services Limited, Southern Cross Health Services Limited, Southern Cross Pet Insurance Limited ("SCPIL") (formerly Southern Cross Healthcare Limited, non-trading) and Southern Cross Healthcare Limited (incorporated 29 July 2019, non-trading) (the "Group"). The Group acquired the pet insurance business from Southern Cross Benefits Limited on 31 January 2020 (refer to Note 20). Comparative financial statement amounts as at and for the year ended 30 June 2019 are nil for SCPIL as it commenced operating on 31 January 2020.

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 \$474.2 million (30 June 2019: \$446.2 million) represents the retained surpluses of the Society. Capital of the Group of \$471.2 million (30 June 2019: \$438.8 million) includes the net equity of the Society's insurance and non-insurance subsidiaries.

BASIS OF PREPARATION



The Society is a profit-oriented entity for financial reporting purposes.

The consolidated financial statements are:

- prepared in accordance with the statutory requirements of the Friendly Societies and Credit Unions Act 1982, the Financial Markets Conduct Act 2013 and the Insurance (Prudential Supervision) Act 2013.
- prepared in accordance with New Zealand generally accepted accounting practice ("NZ GAAP").
- in compliance with New Zealand equivalents to International Financial Reporting Standards ("NZ IFRS") and International Financial Reporting Standards ("IFRS").
- presented in New Zealand dollars ("NZD"), which is the Group's functional currency. All financial information has been rounded to the nearest thousand (\$000), unless otherwise stated.
- stated net of Goods and Services Tax ("GST"), with the exception of receivables and payables, which are stated inclusive of GST where applicable. The items in the cash flow statement are shown exclusive of GST.
- prepared using historical cost as the measurement basis except for investments and insurance contract liabilities, which are measured at fair value.

BASIS OF CONSOLIDATION



The Group controls an entity when it is exposed to, or has rights to variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. Subsidiaries are entities controlled by the Group. Where an entity is acquired by the Group during the financial year, the results of that entity are included in the Group financial statements from the date that control or significant influence commenced. Where an entity acquired by the Group was not under common control, the cost of an acquisition is measured as the fair value of the assets transferred, less the liabilities incurred. The difference between the net assets acquired and the consideration paid is recognised as goodwill. All intra-group balances and transactions are eliminated in preparing the Group financial statements.

ACCOUNTING POLICIES AND STANDARDS



Accounting policies have been applied on a basis consistent with that used in the previous year, with the exception of the adoption of new standards relevant to the Group as disclosed in Note 21. Certain comparative amounts have been reclassified to conform to the current year's presentation.

NOTES TO THE FINANCIAL STATEMENTS (continued)

for the year ended 30 June 2020

1 BASIS OF ACCOUNTING (continued)**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 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 2: COVID-19 pandemic
- Note 4: Insurance contract liabilities
- Note 6a: Insurance risk
- Note 12: Property and equipment and intangible assets
- Note 20: Purchase of pet insurance business

2 COVID-19 PANDEMIC

On 11 March 2020 the World Health Organisation announced that the coronavirus ("COVID-19") outbreak be classified as a pandemic. This has resulted in the New Zealand government introducing various measures to combat the outbreak, including travel restrictions, quarantines, closure on non-essential businesses and lock-down of the country.

The pandemic has caused significant uncertainty in the global economy, however sensitivity analysis has shown the solvency position of the Society is resilient against a fall in equity values. As a result of the COVID-19 pandemic and the country lock-down measures, certain key inputs and assumptions that underpin insurance contract liabilities and revenue recognition have been re-assessed to reflect the change in claims behaviour and the broader economic uncertainty. Prior to 1 July 2020, the Society experienced a period of materially lower claims as a direct result of the country lock-down, volatility in membership numbers and premium revenue, and increased expenses due to the disruption caused by the pandemic. Amounts recognised in the financial statements have been adjusted to reflect management assessment of the impact of COVID-19 as at 30 June 2020. Based on scenario modelling, the Society's solvency ratio for the next 5 years has been assessed to remain above the minimum solvency capital as required by the RBNZ.

On 13 April 2020 the Board approved a \$50 million pledge to the Society's membership base in response to the impact Covid-19 had on its members and corporate group customers. The pledge took the form of a premium credit against each member's health insurance policy and the amount of the credit was based on policy premium for membership as at 1 April 2020. The \$50 million (inclusive of GST) premium credit has been fully applied against premium revenue for the year ended 30 June 2020, in the form of a reduced premium thus reducing premium revenue and premium receivable (refer to Note 11).

The lock-down measures in response to COVID-19 resulted in a decline in claims between March and May 2020, as many healthcare providers were unable to provide services. Due to uncertainty in current market conditions, and deferral of claims that are now expected to be incurred in the year ending 30 June 2021, as at 30 June 2020, provisions for outstanding claims liability and unexpired risk liability have been adjusted for known impacts in the central estimates and allowances made for the additional uncertainty in the risk margins. Refer to Note 4 for further details.

3 SOLVENCY

As licensed insurers, the Solvency Standard for Non-life Insurance Business ("the Solvency Standard") issued by the Reserve Bank of New Zealand ("RBNZ") requires both the Society and SCPIL to each retain a positive solvency margin, meaning that the actual solvency capital position exceeds the minimum required under the Solvency Standard.

The Society's 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 SCPIL Directors' policy for managing capital is to have a capital base to establish security for policyholders and enable SCPIL to conduct its business whilst maintaining financial soundness. SCPIL has a parental support resolution in place from the Society to support the pet insurance business. Both the Society and SCPIL have embedded in their capital management frameworks the necessary tests to ensure continuous and full compliance with the Solvency Standard.



The benchmark and target range for the capital position of the Society is to hold net tangible assets equivalent to 5 to 7 months of expected annual claims, and a minimum solvency ratio of 3.00. A solvency benchmark that is based on claims is relevant as the Society's reserves are used to pay claims. Net tangible assets at 30 June 2020 are equivalent to 5.1 months of claims (30 June 2019: 5.0 months of claims), which is within the target range under the benchmark.

NOTES TO THE FINANCIAL STATEMENTS (continued)


for the year ended 30 June 2020

3 SOLVENCY (continued)

The Society complied with RBNZ imposed capital requirements for the year ended 30 June 2020 (30 June 2019: In compliance).

	2020	2019
	\$m	\$m
Disclosures of Society solvency required by the Solvency Standard as issued by the RBNZ		
Solvency capital	426.6	407.7
Minimum solvency capital	137.0	125.1
Solvency margin	289.6	282.6
	2020	2019
Solvency ratio	3.11	3.26

On 23 April 2020, Standard & Poor's reaffirmed the Society's Insurer Financial Strength Rating at A+ (30 April 2019: A+), under its global insurance industry rating methodology.

 The target range for the capital position of SCPIL is a solvency ratio of 1.20 to 1.50. The policy in respect of capital management is regularly reviewed by the SCPIL Directors in line with the guidelines issued by the RBNZ.

SCPIL is a licenced insurer under the Insurance (Prudential Supervision) Act 2010 since 30 January 2020. SCPIL has complied with RBNZ imposed capital requirements from 30 January 2020 to 30 June 2020. On 3 February 2020, Standard & Poor's issued SCPIL's Insurer Financial Strength Rating at A, under its global insurance industry rating methodology.

As the Society is a licenced insurer with a licenced insurer subsidiary, these insurers must be consolidated for purpose of calculating and reporting the insurance group solvency, as follows:


	2020
	\$m
Disclosures of insurance group solvency required by the Solvency Standard as issued by the RBNZ	
Solvency capital	433.0
Minimum solvency capital	140.1
Solvency margin	292.9
	2020
Solvency ratio	3.09

NOTES TO THE FINANCIAL STATEMENTS (continued)

for the year ended 30 June 2020


4 INSURANCE CONTRACT LIABILITIES

Insurance contracts are defined as those containing significant insurance risk at the inception of the contract. All insurance policies issued by the Society and SCPIL are insurance contracts.

 Estimates of the outstanding claims and unexpired risk at 30 June 2020 have been determined by the Group's Appointed Actuary, John Smeed, a Fellow of the New Zealand Society of Actuaries. These were presented to the Directors in reports dated 24 August 2020. There were no qualifications to the reports. The calculations of the provisions for outstanding claims and unexpired risk each comply with both NZ IFRS 4 *Insurance Contracts*, and Professional Standard No.30: *Valuations of General Insurance Claims*, of the New Zealand Society of Actuaries.

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

	2020	2019
	\$000	\$000
Insurance contract liabilities		
Net provision for outstanding claims	76,799	64,399
Provision for unearned premium	119,646	104,330
Provision for unexpired risk	19,332	8,111
Other insurance provisions	1,276	625
Assessed claims payable	5,320	5,081
Total	222,373	182,546

 The net provision for outstanding claims is the central estimate of the present value of expected future payments for claims incurred but not settled at the balance date, less estimated reinsurance and third party recoveries. For the Society, the central estimate has been calculated using historical experience to determine the pattern of claims development. For SCPIL, a payments per active policy approach is adopted to value outstanding claims, where future claims payments are not inflated or discounted due to the short tail nature of the liabilities.

Estimation of the provision for outstanding claims includes an allowance for claims incurred but not reported, claims incurred but not enough reported, unpaid reported claims and future claims handling costs associated with paying claims. For the Society, an explicit allowance for third party recoveries of \$0.75 million has been made for expected Accident Compensation Corporation ("ACC") recoveries as at 30 June 2020, which has been netted off against liabilities (30 June 2019: \$0.75 million).

A risk margin has been added to reflect the inherent uncertainty in the central estimate. The risk margin considers both historic and future sources of volatility. For both Society and SCPIL, a risk margin of 10% of the central estimate was established as at 30 June 2020 (30 June 2019: Society, 7%). The risk margin was determined with the objective of achieving at least 75% probability of sufficiency of the provision for outstanding claims. Included within the 10% risk margins for Society and SCPIL is a 3% risk allowance to reflect the additional uncertainty in estimating the outstanding liability due to the impacts of the COVID-19 lock-down. Refer to Note 2.

	2020	2019
Outstanding claims risk margin		
Society	10%	7%
SCPIL	10%	n/a

Key assumptions for Society:

- i. Future patterns of claims development will be similar to historical patterns depending on the type of policy, type of claim and development month.
- ii. Monthly seasonality factors used for claims incurred. These are calculated from the 5 years' previous claims experience and range from 44% to 121% (30 June 2019: 69% to 114%) of the monthly average. The provision for outstanding claims is calculated separately for different claim types and therefore has different seasonality factors than the unexpired risk provision, which is calculated at a portfolio level. Seasonality adjustments have been made to the months between April and December 2020 to allow for estimated COVID-19 impacts, to reflect the expectation that benefit utilisation is likely to be higher in the months following lock-down. Refer to Note 2.
- iii. Historical claims inflation 5.5% p.a. (30 June 2019: 4.9%), 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 2019: 4%) of the underlying claims amounts based on an analysis of administration expenses.

The average weighted term from 30 June 2020 to the expected settlement date for claims included in the liability for outstanding claims is 57 days (30 June 2019: 59 days). Accordingly, expected future claims payments are not discounted due to the short tail nature of the liabilities.

Key assumptions for SCPIL:

- i. Future patterns of claims development will be similar to historical patterns depending on the type of policy, type of claim and development month.
- ii. Historical claims inflation of nil, based on previous claims experience.

Claims handling costs include internal and external costs incurred in connection with the settlement of claims. Internal costs include all direct expenses of the claims department and any part of the general administrative costs directly

The average weighted term from 30 June 2020 to the expected settlement date for claims included in the liability for outstanding claims is 4.3 months. Accordingly, expected future claims payments are not discounted due to the short tail nature of the liabilities.

NOTES TO THE FINANCIAL STATEMENTS (continued)

for the year ended 30 June 2020

4 INSURANCE CONTRACT LIABILITIES (continued)

Provision for outstanding claims

	Note	2020 \$000	2019 \$000
Provision for outstanding claims			
Central estimate of outstanding claims liability		67,797	58,592
Claims handling costs		2,784	2,344
Risk margin		6,975	4,213
Total		77,556	65,149
Reinsurance recoveries on outstanding claims			
Central estimate of reinsurance recoveries on outstanding claims liability		(7)	-
Total		(7)	-
Third party recoveries on outstanding claims			
Estimate of third party recoveries on outstanding claims liability		(750)	(750)
Total		(750)	(750)
Total net provision for outstanding claims		76,799	64,399

Reconciliation of movement in net provision for outstanding claims

Opening balance		64,399	63,196
Net pet insurance outstanding claims liabilities acquired	20	2,243	-
Amounts utilised during the year		(57,206)	(56,581)
Additional provision		1,582	1,799
Amounts provided during the year		62,725	55,327
Movement in claims handling costs		440	22
Movement in risk margin		2,616	636
Total		76,799	64,399

Provision for unexpired risk and liability adequacy test



Liability adequacy tests were performed to determine whether the provision for unearned premium is adequate to cover the present value of the expected future cash flows, plus a risk margin, from the current insurance contracts. For Society, gross earned premiums from insurance contracts are recognised evenly over the current billing period of the contract, which is considered to be in line with the pattern of the incidence of risk. For SCPIL, the liability for unearned premiums arises from premiums received for risks that have not yet expired. The provision is released evenly over the duration of the pet insurance premium and is recognised as premium income. For both Society and SCPIL, the future cash flows are future claims, associated claims handling costs and other administration costs.

If the present value of the expected future cash outflows exceeds the provision for unearned premium then the provision for unearned premium is deemed to be deficient. Any deficiency is recognised as an expense in the statement of comprehensive income. The Society provision for unexpired risk has been calculated as the projected premium deficiency for current in-force business until the next policy billing date on or after 1 July 2020 and a deficiency as at 30 June 2020 (30 June 2019: deficiency) has been recognised in the statement of financial position as a provision of unexpired risk. For SCPIL, the provision for unexpired risk has been calculated as the projected premium deficiency for current in-force business until the next policy anniversary date on or after 1 July 2020. As at 30 June 2020, the liability adequacy test identified a surplus, therefore no deficiency in the unearned premium liability has been recognised.

	2020 \$000	2019 \$000
Society provision for unexpired risk		
Present value of expected future cash flows for claims and expenses	120,016	108,386
Risk margin	7,201	4,335
Unearned premiums	(107,885)	(104,330)
Write-down of deferred acquisition costs	-	(280)
Total	19,332	8,111
SCPIL liability adequacy test		
Present value of expected future cash flows for claims and expenses	9,255	
Risk margin	1,035	
Unearned premiums	(11,762)	
Surplus	(1,472)	

NOTES TO THE FINANCIAL STATEMENTS (continued)

for the year ended 30 June 2020

4 INSURANCE CONTRACT LIABILITIES (continued)

The calculation of the risk margins has been based on an analysis of the volatility of historical claims experience within the time period covered by the unearned premiums together with future sources of volatility. For Society, a risk margin of 6% of the present value of expected future cash flows has been applied at 30 June 2020 (30 June 2019: 4%), including an additional 2% allowance for uncertainty in estimating the impact of COVID-19 on the future claims liability due to the unknown future private health utilisation level. For SCPIL, a risk margin of 15% of the present value of expected cash flows has been applied at 30 June, including an additional 5% allowance for uncertainty associated with COVID-19. The risk margins were determined with the objective of achieving at least 75% probability of sufficiency of the provision for unexpired risk.

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

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

	2020	2019
Premium liabilities risk margin		
Society	6%	4%
SCPIL	15%	n/a

Key assumptions for Society:

- i. Future claims development will be similar to historical patterns by the type of policy, type of claim and development month.
- ii. Monthly seasonality factors used for claims incurred. These were calculated from the 5 years' previous claims experience, and range from 65% to 119% (30 June 2019: 73% to 112%) of the monthly average. The provision for outstanding claims is calculated separately for different claim types and therefore has different seasonality factors than the provision for unexpired risk, which is calculated at a portfolio level. Seasonality adjustments have been made to the months between April and December 2020 to allow for estimated COVID-19 impacts, to reflect the expectation that benefit utilisation is likely to be higher in the months following lock-down.
- iii. Expenses based on the business plan for 2020/21.

Key assumptions for SCPIL:

- i. Future claims development will be similar to historical patterns by the type of policy, type of claim and development month.
- ii. Expenses based on the business plan for 2019/20.

	Note	2020	2019
		\$000	\$000
Provision for unearned premium			
Opening balance		104,330	97,565
Net pet insurance unearned premium acquired	20	9,885	-
Premiums written in the year		1,151,969	1,087,129
Premiums earned during the year		(1,146,538)	(1,080,364)
Total		119,646	104,330

Premiums billed but unearned are recorded as a provision for unearned premium in the statement of financial position.

5 NET CLAIMS EXPENSE

The net claims expense represents payments made on claims and the movements in the provisions for outstanding claims and unexpired risk. Details of processes and assumptions used in calculating the provisions are disclosed in Note 4.

	2020	2019
	\$000	\$000
Net claims expense		
Claims incurred relating to risks borne in current financial year	961,062	963,050
Reinsurance recoveries relating to risks borne in current financial year	(10)	-
Claims incurred relating to risks borne in previous financial years	1,563	1,799
Reinsurance recoveries relating to risks borne in previous financial years	19	-
Movement in provision for claims handling costs	440	22
Movement in risk margin	2,616	636
Net claims incurred	965,690	965,507
Movement in provision for unexpired risk	11,221	(1,841)
Total	976,911	963,666


NOTES TO THE FINANCIAL STATEMENTS (continued)

for the year ended 30 June 2020

6 RISK MANAGEMENT

The Group is exposed to a number of risks in the normal course of business, specifically insurance risk, credit risk, liquidity risk, market risk and operational risk. The Directors and management recognise the importance of having effective risk management and have put in place a comprehensive risk management program.

a. Insurance risk

 The Group is exposed to insurance risk through its health and pet insurance activities. The key risk is that of claims costs varying significantly from the assumptions made in the setting of premium rates and putting pressure on the solvency and liquidity of the Group.

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

The primary objective in managing insurance risk is 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 organisation if there is adverse deviation in experience. Key policies and methods for mitigating insurance risk include:

- Each year, as part of the planning process, the Boards and the Senior Leadership Teams ("SLT") review the underwriting and pricing performance.
- Underwriting policies and processes which evaluate new risks and offer terms that do not endanger the portfolio.
- Policy terms and conditions which clearly specify which health care and pet care costs are reimbursed and claims management procedures which ensure those terms and conditions are adhered to in claims administration.
- A long-term pricing strategy and guidelines adopted by the Boards which supports pricing based on underlying risk.
- Regular monitoring of financial and operating results.
- Maintaining a target solvency margin in excess of the minimum required by the standard established by the RBNZ. The solvency margin ensures the Society and Pet are able to withstand a period of adverse insurance or investment experience and still maintain a satisfactory financial position (refer to Note 3).
- Cash flow projection model designed to forecast major inflow and outflow items.
- A minimum liquidity reserve buffer is maintained in excess of anticipated cash flow requirements.

ii. Society sensitivity to insurance risk

The volatility of claims at a portfolio level has been low relative to other types of insurance contracts. The low volatility is due to:

- The benefits in the health insurance contracts providing cover primarily for medically necessary yet elective health care services.
- Obligations arise under the health insurance contracts when health care services are provided and the provision of health care services is constrained by supply of private medical practitioners and medical facilities. This constraint on claims experience is different than other forms of insurance contracts where obligations do not depend on service provision, i.e. property insurance.
- ACC and public sector health care provision of both acute, accident and elective health services. Many of the highest cost and highly variable medical care claims are funded by other sources.
- Management's policies and processes for managing insurance risk, as listed above.

iii. SCPIL sensitivity to insurance risk

The scope of insurance risk for the pet insurance business is managed by the terms and conditions of the policy. The main insurance benefits involves the reimbursement of medical and surgical expenses depending upon the plan product terms and conditions. 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.


iv. 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.

The pet insurance business in New Zealand represents a small and not well diversified risk base, therefore, the concentration of risk by type of insurance and geographic region cannot be avoided. Insurance risks are well diversified within the pet insurance portfolio with claims costs spread across many different types of medical procedures and health events, and animal demographics. There is no significant exposure to individual large claims.

b. Financial risks

i. Credit risk

 Credit risk is the potential risk of loss arising from the failure of a debtor or counterparty to meet their contractual obligations.

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

The Group maintains policies which are used to manage the exposure to credit risk. Limits on counter-party exposures have been set and are monitored on an ongoing basis. The credit quality of investment 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 2020 in excess of policy (30 June 2019: Nil).

NOTES TO THE FINANCIAL STATEMENTS (continued)

for the year ended 30 June 2020

6 RISK MANAGEMENT (continued)

b. Financial risks (continued)

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

	2020	2019
	\$000	\$000
Money market		
AA	169,326	173,223
A	100,062	73,817
BBB	42,873	35,345
	312,261	282,385
Unit trusts		
Non-rated (Global bonds, weighted average rating of the underlying investments is A, 30 June 2019: AA-)	108,483	103,233
Non-rated (Global equities)	58,279	51,255
Non-rated (Global real estate)	27,559	27,444
Non-rated (Global listed infrastructure)	28,118	28,162
	222,439	210,094
Total	534,700	492,479



The maximum exposure to credit risk at the end of the reporting period is the amount of financial assets stated in the statement 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 2019: AA-).

Premium receivables are due from a very large number of counter-parties, ranging from large corporates to individual members and policyholders. Analysing these by credit quality would not be feasible, as the majority of counter-parties will be non-rated. Credit risk for premium receivables is considered low as the Group is able to terminate or suspend policies for non-payment, at the Group's discretion.

ii. Liquidity risk



The Group is exposed to ongoing operational drawdowns 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 unexpected levels of claims and expenses.

	2020	2019
	\$000	\$000
Contractual maturities of investments		
0-6 months	402,306	363,973
7-12 months	114,134	122,415
Current	516,440	486,388
1-2 years	15,285	6,091
2-5 years	2,975	-
Non-current	18,260	6,091
Total	534,700	492,479

Financial liabilities are all short term. Investments can usually be liquidated at any time, under normal market conditions, to settle liabilities.

The 0-6 months maturity category includes unit trusts of \$222.4 million (30 June 2019: \$210.1 million), as these investments could be liquidated at short notice.

NOTES TO THE FINANCIAL STATEMENTS (continued)

for the year ended 30 June 2020

6 RISK MANAGEMENT (continued)

c. Market risks

i. Interest rate risk



The Group invests in both fixed and variable rate investments 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.

The cash flows from the Group's investment in bank deposits, commercial paper and floating rate notes are susceptible to changes in interest rates.

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 the statement of comprehensive income for each period.

	2020	2019
	\$000	\$000
	Impact on profitability	
Fair value - interest rate sensitivity on money market investments		
Exposure	312,261	282,385
Impact of change in interest rates:		
Increase by 100 basis points	(1,797)	(1,507)
Decrease by 100 basis points	1,819	1,263

ii. Unit price risk



Unit price risk is the risk that the fair value of investments in unit trusts will change as a result of changes in unit prices. The Group holds all of its investments in unit trusts at fair value through profit and loss.

	2020	2019
	\$000	\$000
	Impact on profitability	
Fair value - unit price sensitivity on unit trust investments		
Exposure	222,439	210,094
Impact of change in unit prices:		
Increase by 10%	22,244	21,009
Decrease by 10%	(22,244)	(21,009)

iii. Foreign currency risk.



The Group does not have material exposure to foreign currency risk through its insurance operations. On a net basis the foreign currency risk on investments in unit trusts is substantially hedged into NZD. In operating these funds, inherent currency risk exposure arises. The Group does not apply hedge accounting.

There are no significant liabilities denominated in foreign currencies.


NOTES TO THE FINANCIAL STATEMENTS (continued)

for the year ended 30 June 2020

6 RISK MANAGEMENT (continued)

c. Market risks (continued)

iv. Fair values of financial instruments and financial liabilities

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

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

 **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.


	Level 1 \$000	Level 2 \$000	Level 3 \$000	Total \$000
30 June 2020				
Investments	-	534,700	-	534,700
Total	-	534,700	-	534,700
30 June 2019				
Investments	-	492,479	-	492,479
Total	-	492,479	-	492,479

d. Operational risk

Operational risk is defined as the risk of loss (including financial, non-financial and lost opportunities) resulting from inadequate or failed internal processes, people and systems or from external events.

Management of the Group's operational risk is a continual cyclic process. This process is documented in the respective Society and SCPIL Risk Management frameworks, and includes risk identification, analysis, evaluation and implementation of risk controls, which results in acceptance, mitigation, or avoidance of risk.

7 INVESTMENTS

 Investments are recognised on the date they are originated and 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. Changes in fair value are recognised in the statement of comprehensive income. The credit quality, contractual maturities, and fair value hierarchies of investments are disclosed in Note 6.

	2020 \$000	2019 \$000
Investments		
Bonds	20,111	17,141
Bank deposits	275,151	236,179
Commercial paper	1,999	-
Floating rate notes	15,000	29,065
Unit trusts - global bonds	108,483	103,233
Unit trusts - global equities	58,279	51,255
Unit trusts - global real estate	27,559	27,444
Unit trusts - global listed infrastructure	28,118	28,162
Total	534,700	492,479

NOTES TO THE FINANCIAL STATEMENTS (continued)

for the year ended 30 June 2020

8 NET INVESTMENT AND OTHER INCOME



Fees and other income are recognised on an accrual basis. Interest income is recognised using the effective interest method.

Fair value gains and losses on financial assets at fair value through profit or loss are recognised through the statement of comprehensive income in the period in which they arise.

	2020	2019
	\$000	\$000
Net investment and other income		
Interest income	7,624	8,670
Net gains on investments at fair value through profit or loss	6,855	13,460
Net investment income	14,479	22,130
Fee and other income	4,497	5,812
Total	18,976	27,942

9 OPERATING EXPENSES

	2020	2019
	\$000	\$000
Operating expenses consist of:		
Policy acquisition	10,811	9,400
Policy administration	53,307	49,052
Claims administration	13,418	11,213
Other operating expenses	86,413	64,251
Total	163,949	133,916

Other operating expenses consist of expenses incurred for information technology, human resources, occupancy, governance, finance, actuarial, management, depreciation and amortisation. The increase in other operating expenses is largely due to increased expenditure on information technology projects.

	Note	2020	2019
		\$000	\$000
Included within operating expenses are the following specific items:			
Auditor's remuneration:			
• audit of annual financial statements of the Group		263	176
• review of interim financial statements of the Group		62	46
• audit of annual insurer solvency return of the Group		81	39
• review of half year insurer solvency return of the Group		23	23
• accounting impact assessment		-	6
Employee benefits expense		62,195	56,882
Contributions to defined contribution plan		1,518	1,446
Operating leases		-	5,218
Depreciation charge on right-of-use assets	21	4,352	-
Short term lease expense	21	12	-
Depreciation		2,888	5,428
Amortisation		11,122	10,807
Losses on disposal of property and equipment		-	50
Impairment loss on intangible assets		3,657	4,711
(Decrease)/increase in provision for bad and doubtful debts		(48)	116

10 CASH AND CASH EQUIVALENTS



Cash and cash equivalents comprise cash on hand and current account balances in bank accounts, which are readily convertible to cash, with original maturities of less than three months, and are carried at amortised cost as they are subject to an insignificant risk of changes in value.

NOTES TO THE FINANCIAL STATEMENTS (continued)

for the year ended 30 June 2020

11 PREMIUM AND OTHER RECEIVABLES



For Society, gross earned premiums from insurance contracts are recognised evenly over the current billing period of the contract, which is considered to be in line with the pattern of the incidence of risk. For SCPIL, gross earned premiums from insurance contracts are recognised evenly over the annual contract period, which is considered to be in line with the pattern of incidence of risk. For both Society and SCPIL, revenue is recognised on the date from which the policy is effective. Premium and other receivables are stated at their cost less any impairment losses, using an expected credit losses model. Impairment losses for uncollectible premiums are written off against premium revenue in the year in which they are incurred. The recoverability of reinsurance recoveries receivable is assessed at the reporting date and impairment is recognised where there is objective evidence that the Group may not receive the amounts due to it and these amounts can be reliably measured. Premium and other receivables are classified as financial assets at amortised cost.

Premium and other receivables are current assets. The fair values of premium and other receivables approximate the carrying amounts.

	Note	2020 \$000	2019 \$000
Premium and other receivables			
Premium receivable	2	92,361	84,820
Other receivables		15,899	12,929
Total		108,260	97,749

12 PROPERTY AND EQUIPMENT AND INTANGIBLE ASSETS



Property and equipment and intangible assets are measured at cost, less accumulated depreciation or amortisation and impairment losses.

Capital expenditure on all projects is initially recorded as work in progress. On completion of the project the asset is transferred to the appropriate asset category when the project will generate future economic benefits. For computer software development, 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. Work in progress is not depreciated or amortised.

As discussed in Note 20, the Group acquired intangible assets of \$5,309,000 representing customer base and portfolio-in-force upon acquisition of the pet insurance business from Southern Cross Benefits Limited on 31 January 2020. Goodwill arising on acquisition totalled \$4,192,000.



Depreciation and amortisation are recognised to allocate the assets' costs, net of any residual amounts, over their estimated useful lives. The assets' useful lives are reviewed and adjusted if appropriate at each balance date. An asset's carrying amount is written down to its recoverable amount if it is considered that the carrying amount is greater than its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units ("CGU")).

Assets	Estimated useful lives				
• Computer equipment	4 - 7 years				
• Office equipment	3 - 7 years				
• Leasehold improvements	2 - 12 years				
• Customer base	16 years				
• Portfolio-in-force	1 year				
• Goodwill	Indefinite				
• Computer software	3 - 7 years				

a. Property and equipment	Computer equipment \$000	Office equipment \$000	Leasehold improvements \$000	Work in progress \$000	Total \$000
As at 30 June 2019					
Cost	18,697	3,951	10,793	-	33,441
Accumulated depreciation and impairment	(14,222)	(3,451)	(8,603)	-	(26,276)
Opening net book value as at 1 July 2019	4,475	500	2,190	-	7,165
Additions	587	-	-	2,032	2,619
Disposal - cost	(1,147)	-	-	-	(1,147)
Depreciation	(1,413)	(212)	(1,263)	-	(2,888)
Closing net book value as at 30 June 2020	2,502	288	927	2,032	5,749
As at 30 June 2020					
Cost	18,137	3,951	10,793	2,032	34,913
Accumulated depreciation and impairment	(15,635)	(3,663)	(9,866)	-	(29,164)
Closing net book value as at 30 June 2020	2,502	288	927	2,032	5,749

NOTES TO THE FINANCIAL STATEMENTS (continued)

for the year ended 30 June 2020

12 PROPERTY AND EQUIPMENT AND INTANGIBLE ASSETS (continued)

b. Intangible assets	Customer base \$000	Portfolio-in-force \$000	Goodwill \$000	Computer software \$000	Work in progress \$000	Total \$000
As at 30 June 2019						
Cost	-	-	-	81,072	6,442	87,514
Accumulated amortisation and impairment	-	-	-	(49,026)	-	(49,026)
Opening net book value as at 1 July 2019	-	-	-	32,046	6,442	38,488
Additions	-	-	-	-	6,125	6,125
Acquired with purchase of pet insurance business (refer Note 20)	3,761	1,548	4,192	-	-	9,501
Transfers	-	-	-	7,633	(7,633)	-
Disposal - cost	-	-	-	(5,182)	-	(5,182)
Disposal - accumulated amortisation	-	-	-	5,182	-	5,182
Amortisation	(284)	(1,022)	-	(9,816)	-	(11,122)
Impairment	-	-	-	(2,389)	(1,268)	(3,657)
Closing net book value as at 30 June 2020	3,477	526	4,192	27,474	3,666	39,335
As at 30 June 2020						
Cost	3,761	1,548	4,192	83,523	4,934	97,958
Accumulated amortisation and impairment	(284)	(1,022)	-	(56,049)	(1,268)	(58,623)
Closing net book value as at 30 June 2020	3,477	526	4,192	27,474	3,666	39,335

Customer base



Customer base relates entirely to the pet insurance business acquired on 31 January 2020 (refer to Note 20), and represents the value of a customer base acquired, through its ability to generate future cash flows from retained business. It is recognised as an intangible asset when a business is acquired and when the criteria for recognition are met. A customer base is initially recognised at cost, which is the fair value at the acquisition date, and subsequently carried at cost less accumulated amortisation and any accumulated impairment losses. The capitalised costs are amortised on a diminishing value basis, net of any residual amounts, over the period when future economic benefits are expected to flow to the Group. Useful life represents management's estimate of the period of time over which the asset is expected to generate future cash flows from the pet lives insured and customers acquired. Amortisation is recognised using a systematic allocation of the expected retention of insured pet lives acquired at 31 January 2020. The retention of insured pet lives acquired is used for the purposes of assessing impairment and remaining useful life.

The recoverable amount of the cash-generating unit ("CGU") is determined based on value-in-use calculations, determined by discounting the future cash flows to be generated from the CGU. These calculations use discounted cash flow projections based on past experience, actual operating results and profit forecasts approved by management as part of the operating budget and forecast process. The discounted cash flow model has used a 16 year projection with a terminal value, a discount rate of 12.5%, and annual growth rates for insured pets lives and customer base acquired.



Key assumptions underlying the valuation relate to management's assessment of new business growth, claims cost escalation, premium increases and operating expenses. Management utilised local market data as well as Society expertise and experience to validate key assumptions. The key assumptions described above may change as economic and market conditions change. The Group estimates that reasonably possible changes in these assumptions are not expected to cause the recoverable amount of the CGU to decline below the carrying amount.

Portfolio-in-force



Portfolio-in-force relates entirely to the pet insurance business acquired on 31 January 2020 (refer to Note 20), and represents the difference between the fair value of acquired insurance liabilities, and the fair value of the future claim and administration obligations arising in respect of those contracts. A portfolio-in-force is initially recognised at cost, which is the fair value at the acquisition date, and subsequently carried at cost less accumulated amortisation and any accumulated impairment losses. The capitalised costs are amortised on a diminishing value basis, net of any residual amounts, over the period when future economic benefits are expected to flow to the Group.

Goodwill



Goodwill relates entirely to the pet insurance business acquired on 31 January 2020 (refer to Note 20). The cost of an acquisition is measured as the fair value of the total identifiable net assets acquired. On acquisition of a business combination, the excess of purchase consideration over the fair value of identifiable net assets acquired is recognised as goodwill. Following initial recognition, goodwill is not amortised as it has an indefinite useful life, but is tested for impairment annually and is assessed at each reporting date for indicators of impairment. For the purposes of impairment testing, goodwill is allocated to the CGU. No impairment losses on goodwill were recognised during the year to 30 June 2020.

NOTES TO THE FINANCIAL STATEMENTS (continued)
for the year ended 30 June 2020

13 LEASES

a. Right-of-use assets	Note	Motor vehicles \$000	Premises \$000	Total \$000
As at 30 June 2019				
Cost		-	-	-
Accumulated depreciation		-	-	-
Opening net book value as at 1 July 2019		-	-	-
Net impact of change in accounting policy	21	532	6,700	7,232
Additions		292	719	1,011
Disposals		-	(137)	(137)
Depreciation		(268)	(4,084)	(4,352)
Closing net book value as at 30 June 2020		556	3,198	3,754

As at 30 June 2020				
Cost		824	7,282	8,106
Accumulated depreciation		(268)	(4,084)	(4,352)
Closing net book value as at 30 June 2020		556	3,198	3,754

b. Lease liabilities	Note	Motor vehicles \$000	Premises \$000	Total \$000
As at 30 June 2019				
Cost		-	-	-
Accumulated interest expense and principal repayments		-	-	-
Opening net book value as at 1 July 2019		-	-	-
Net impact of change in accounting policy	21	532	7,455	7,987
Additions		292	719	1,011
Disposals		-	(137)	(137)
Interest expense		39	184	223
Principal repayment		(294)	(4,704)	(4,998)
Closing net book value as at 30 June 2020		569	3,517	4,086

As at 30 June 2020				
Cost		824	8,037	8,861
Accumulated interest expense		39	184	223
Accumulated principal repayment		(294)	(4,704)	(4,998)
Closing net book value as at 30 June 2020		569	3,517	4,086

14 PAYABLES AND OTHER LIABILITIES



Payables and other liabilities are current liabilities, stated at cost.

	2020 \$000	2019 \$000
Payables and other liabilities		
Trade creditors and accruals	19,714	9,416
Amounts due to policyholders	9,345	5,905
Total	29,059	15,321

NOTES TO THE FINANCIAL STATEMENTS (continued)

for the year ended 30 June 2020

15 EMPLOYEE BENEFITS

a. Short term benefits



Employee benefits represent the current obligations to employees in respect of outstanding salaries, leave entitlements and other short term 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, with consideration 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.

b. Post employment benefits



The Group's obligation for post employment benefits 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.

	2020	2019
	\$000	\$000
Employee benefits		
Short term benefits	9,281	7,396
Post employment benefits	1,886	1,901
Total	11,167	9,297

16 TAXATION



The Society is exempt from income tax due to its status as a friendly society, however, its subsidiaries are subject to income tax. Deferred tax expense is recognised in respect of temporary differences between the carrying amount of assets and liabilities in the financial statements and the amounts used for taxation purposes. Deferred tax assets are only recognised to the extent it is probable they will be utilised. As at 30 June 2019, the Group had aggregate temporary differences arising in the subsidiaries for which a deferred tax asset had not been recognised of \$35,552,000. With the acquisition of the pet insurance business during the year ended 30 June 2020 (refer to Note 20), the Group anticipates that future taxable profits are now probable, and deferred tax assets of \$7,545,000 have been recognised as at 30 June 2020. The comparative financial statement amounts as at and for the year ended 30 June 2019 are nil.

Income tax



Tax expense comprises deferred tax, calculated using the tax rate enacted or substantively enacted at balance date and any adjustments to tax payable in respect of prior years. Deferred tax is recognised in respect of temporary differences between the carrying amounts of assets and liabilities in the financial statements and the amounts for taxation purposes.

	2020
	\$000
Reconciliation of income tax to surplus before taxation	
Surplus before taxation	24,413
Income tax at the domestic tax rate of 28%	6,836
Tax effect of Society exempt income	(7,839)
Tax effect of recognised group losses	(7,545)
Tax effect of current year unrecognised losses	2,155
Tax effect of permanent differences	2
Tax effect of temporary differences	(1,149)
Tax effect of group loss offsets	(456)
Total income tax benefit	(7,996)

NOTES TO THE FINANCIAL STATEMENTS (continued)

for the year ended 30 June 2020

16 TAXATION (continued)

Deferred tax



The Group has accumulated tax losses carried forward of \$41,620,000 at 30 June 2020 (30 June 2019: \$35,552,000), of which the Society has accumulated tax losses carried forward of \$nil (30 June 2019: nil). The Group has unrecognised tax losses carried forward of \$14,672,000 (30 June 2019: \$35,552,000).

	Note	2020 \$000
Deferred tax comprises temporary differences attributable to:		
Deferred tax assets		
Losses available for offset against future taxable income		7,545
Total deferred tax assets		7,545
Expected to crystallise within 12 months		854
Expected to crystallise in greater than 12 months		6,691
Total deferred tax assets		7,545
Movements in deferred tax assets		
Opening balance at 1 July 2019		-
Initial recognition of losses available for offset against future taxable income		8,001
Group loss offsets recognised in the statement of comprehensive income		(456)
Closing deferred tax assets as at 30 June 2020		7,545
Deferred tax liabilities		
Intangible assets		(1,122)
Payables and other liabilities		86
Total deferred tax liabilities		(1,036)
Expected to crystallise within 12 months		(228)
Expected to crystallise in greater than 12 months		(808)
Total deferred tax liabilities		(1,036)
Movements in deferred tax liabilities		
Opening balance at 1 July 2019		-
Net deferred tax liabilities recognised on acquisition	20	(1,487)
Intangible assets temporary differences recognised in the statement of comprehensive income		365
Other temporary differences recognised in the statement of comprehensive income		86
Closing deferred tax liabilities as at 30 June 2020		(1,036)

17 RELATED PARTIES

a. Identity of related parties:	Relationship	Balance Date
• The Southern Cross Medical Care Society ("Society")	Parent	30 June
• Southern Cross Health Services Limited ("Health Services")	100% subsidiary of Society	30 June
• Southern Cross Insurance Services Limited ("SCISL")	100% subsidiary of Society	30 June
• Southern Cross Pet Insurance Limited ("SCPIL", formerly "Southern Cross Healthcare Limited")	100% subsidiary of Society	30 June
• Southern Cross Healthcare Limited (non-trading)	100% subsidiary of Society	30 June
• Southern Cross Health Trust ("Trust")	Related party of Society	30 June
• Southern Cross Benefits Limited ("SCBL")	100% subsidiary of Trust	30 June
• Southern Cross Hospitals Limited ("Hospitals")	100% subsidiary of Trust	30 June
• Directors of The Southern Cross Medical Care Society	Certain Directors are Trustees of Trust	-



The Society and the Trust are separate legal entities with no shared parent or shareholding. They are however deemed to be related parties for the purposes of these financial statements. Prior to acquisition from SCBL on 31 January 2020, the Society had significant influence over the financial and operating policy and claims of the pet insurance business through its subsidiary SCISL. All entities provide their normal services to other group entities on normal commercial terms. However, some goods and services are purchased by the Group and other related parties on a combined basis, and are on-charged to other related parties at cost. The Society contracts healthcare services on behalf of its members from all providers, including Hospitals, on a contestable and contractual basis, which are not included in the table below, as these are services paid on behalf of members.

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 (30 June 2019: Nil).

NOTES TO THE FINANCIAL STATEMENTS (continued)

for the year ended 30 June 2020

17 RELATED PARTIES (continued)

	Note	2020 \$000	2019 \$000
Total amount of transactions with other related parties			
Sale of services		6,208	7,104
Purchase of services		1,063	813
Acquisition of pet insurance business from SCBL	20	8,077	-
Total outstanding balances with other related parties			
Receivables		264	588
Payables		107	81

b. Remuneration of Directors

A friendly society has trustees to hold its assets. The trustees for the year were C M Drayton, G W Gent and G R W France and they did not receive any fees for this.

The Society provides Society and SCPIL 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. Other operating expenses in relation to governance are met by the Society, except for SCPIL who bears the cost for other operating expenses relating to SCPIL governance. The Society and SCPIL do not provide loans or advances to directors or trustees. Where directors of the Society are also directors of the Society's subsidiaries, they do not receive any fees for these appointments, with the exception of SCPIL, where fees are paid to directors.

All directors, excluding M Misur, M J Gardiner and M L James, have medical insurance policies with the Society. No SCPIL directors have pet insurance policies with SCPIL.

Director	Society					Total Remuneration Amount
	Board Amount	Audit & Risk Committee Amount	Investment Committee Amount	Remuneration Committee Amount	Nominations Committee Amount	
Actual directors' remuneration paid by the Society for the year ended 30 June 2020 was as follows:						
C M Drayton ³	58,000	4,500 Chair	1,250	1,000	500	65,250
G W Gent ¹	116,000 Chair	-	-	-	-	116,000
G R W France	58,000	-	5,000 Chair	1,000	-	64,000
E M Hickey ²	29,000	3,000 Chair	1,250	-	-	33,250
M Jordan ²	29,000	1,500	-	1,000	500	32,000
P Leightley ²	29,000	-	-	-	-	29,000
M Misur ²	34,201	-	-	1,000	500	35,701
J M Raue	58,000	-	-	4,000 Chair	500	62,500
K B Taylor	58,000	3,000	-	-	500	61,500
Total	469,201	12,000	7,500	8,000	2,500	499,201

¹ G W Gent did not receive any fees for being a member of the Audit and Risk, Investment, Remuneration or Nominations Committees.

² E M Hickey and P Leightley retired 31 December 2019. M Misur was appointed 29 November 2019. M Jordan was appointed 1 January 2020.

³ E M Hickey was chair of the Audit and Risk Committee until 31 December 2019. C M Drayton was appointed 1 January 2020.

The annual fee pool limit of \$499,800 remained at the limit approved by Society members at the Annual General Meeting in December 2017.

NOTES TO THE FINANCIAL STATEMENTS (continued)

for the year ended 30 June 2020

17 RELATED PARTIES (continued)

b. Remuneration of Directors (continued)

From 31 January 2020, remuneration was paid by SCPIL to directors of SCPIL.

Director	SCPIL		Total Remuneration Amount
	Board Amount	Audit & Risk Committee Amount	
Actual directors' remuneration paid by SCPIL the year ended 30 June 2020 was as follows:			
N J Astwick	-	-	-
M J Gardiner	6,264	1,044	7,308
M L James	10,440	-	10,440
J M Raue	6,264	-	6,264
Total	22,968	1,044	24,012

Director	Society					Total Remuneration Amount
	Board Amount	Audit & Risk Committee Amount	Investment Committee Amount	Remuneration Committee Amount	Nominations Committee Amount	
Actual directors' remuneration paid by the Society for the year ended 30 June 2019 was as follows:						
C M Drayton	58,000	3,000	-	2,000	1,000	64,000
G W Gent ¹	116,000	-	-	-	-	116,000
G R W France	58,000	-	5,000	2,000	-	65,000
E M Hickey	58,000	6,000	2,500	-	-	66,500
P Leightley	58,000	-	-	-	-	58,000
J M Raue	58,000	-	-	4,000	-	62,000
K B Taylor	58,000	3,000	-	-	1,000	62,000
Total	464,000	12,000	7,500	8,000	2,000	493,500

¹ G W Gent did not receive any fees for being a member of the Audit and Risk, Investment, Remuneration or Nominations Committees.

NOTES TO THE FINANCIAL STATEMENTS (continued)

for the year ended 30 June 2020

17 RELATED PARTIES (continued)

c. Remuneration of key management personnel



Key management personnel are the members of the Society Leadership Team. SCPIL has no direct employees and therefore no key management personnel. 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.

	2020	2019
	\$000	\$000
Salaries and other short-term benefits	3,604	3,375
Post-employment benefits	100	89
Net long-term employee benefits provision movement	(6)	17

Chief Executive Officer ("CEO") remuneration

Over the course of the financial year, the CEO of the Society earned a base salary of \$739,749 (30 June 2019: \$719,600). The amount of total short-term performance-related incentive provided as at 30 June 2020 was \$160,000 (30 June 2019: \$162,600). The final amount of \$152,000 will be paid in the 2021 financial year (30 June 2019: \$162,600 paid in the 2020 financial year). As a member of KiwiSaver, the CEO received contribution from the Society of \$36,775 during 2020 (30 June 2019: \$35,402). In addition, the CEO received other non-cash short-term benefits of \$11,365 during 2020 (30 June 2019: \$10,388).

The CEO has a long-term incentive plan relating to achieving specific performance targets by 30 June 2021 which is payable as a lump sum on achievement. Depending on the level of performance achieved against set targets, potential payments that the Board may award in respect of the 3-year period, at its discretion, range from 0% to 60.75% of the CEO's base salary of \$700,000 as at 1 July 2018.

18 EMPLOYEE REMUNERATION

The following table discloses the number of employees and former employees of the Society, who received remuneration and other allowances during the financial year. Remuneration represents actual payments made during the financial year and includes base salary, bonuses, redundancy and termination payments.

\$	2020	2019
	Number of employees	
<100,000	632	641
100,001 - 110,000	34	37
110,001 - 120,000	29	18
120,001 - 130,000	29	23
130,001 - 140,000	17	17
140,001 - 150,000	14	16
150,001 - 160,000	10	7
160,001 - 170,000	9	5
170,001 - 180,000	3	7
180,001 - 190,000	4	3
190,001 - 200,000	6	2
200,001 - 210,000	8	4
210,001 - 220,000	1	1
220,001 - 230,000	1	2
230,001 - 240,000	1	1
240,001 - 250,000	3	2
280,001 - 290,000	-	2
290,001 - 300,000	-	1
300,001 - 310,000	1	-
310,001 - 320,000	-	1
330,001 - 340,000	-	2
350,001 - 360,000	1	-
370,001 - 380,000	1	-
390,001 - 400,000	1	-
400,001 - 410,000	1	-
880,001 - 890,000	-	1
910,001 - 920,000	1	-
Total	807	793
Headcount as at balance date	700	663

NOTES TO THE FINANCIAL STATEMENTS (continued)

for the year ended 30 June 2020

19 COMMITMENTS, CONTINGENCIES AND SUBSEQUENT EVENTS**a. Operating lease commitments**

Under NZ IAS 17 *Leases*, leases were defined as an operating lease where they did not transfer substantially all the risks and rewards incidental to ownership.

Payments made under operating leases were recognised in the statement of comprehensive income on a straight-line basis over the term of the lease. Any inducement payments received as part of a lease agreement were deferred and recognised on a straight-line basis over the term of the lease. Refer to Note 21 for the impact of changes in financial reporting standards for leases adopted from 1 July 2019, and to Note 13 where the lease right-of-use assets and lease liabilities are disclosed.

	2020	2019
	\$000	\$000
Future minimum lease payments under non-cancellable operating leases		
Within 1 year	-	5,942
Between 1 and 2 years	-	6,086
Between 2 and 5 years	-	15,711
Greater than 5 years	-	44,856
Total	-	72,595

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

The Society entered into an agreement to lease new premises in Auckland in November 2018 for a lease term of 12 years, commencing October 2020.

b. Other commitments

The Group had contractual commitments for the acquisition of property and equipment and intangible assets of \$4,241,000 at 30 June 2020 (30 June 2019: \$6,564,000).

c. Contingent liabilities

The Group had no contingent liabilities at 30 June 2020 (30 June 2019: Nil).

20 PURCHASE OF PET INSURANCE BUSINESS

On 31 January 2020, SCPIL purchased the assets and liabilities relating to the pet insurance business from SCBL and SCISL. Since the purchase of the pet insurance business by SCBL in 2012, the day to day oversight and management of the pet insurance business has been outsourced to the Society, via its subsidiary SCISL. The Group has acquired the pet insurance business because it combines ownership within the Society with the existing management operation of the business. SCBL is a 100% owned subsidiary of Southern Cross Health Trust, which is a related party of the Society (refer to Note 17).

The assets and liabilities acquired from SCBL were purchased via an Asset Sale Agreement for \$8,077,000. An independent valuation of the business was obtained for the purchase price. The acquisition of the control of the business from SCBL meets the definition of a business combination under NZ IFRS 3 *Business Combinations*, but does not meet the criteria of common control.

The fair value amounts of the assets and liabilities acquired are determined to be equivalent to the carrying value at the date of acquisition, except for customer base and portfolio-in-force.

Estimates of the fair value of the acquired insurance contract liabilities have been determined by an external actuary at the date of acquisition.

NOTES TO THE FINANCIAL STATEMENTS (continued)

for the year ended 30 June 2020

20 PURCHASE OF PET INSURANCE BUSINESS (continued)

The fair values of the identifiable assets and liabilities of the pet insurance business acquired are outlined below.

	Total \$000
Assets	
Cash and cash equivalents	3,411
Premium and other receivables	9,450
Intangible assets	5,309
Total assets	18,170
Liabilities	
Payables and other liabilities	670
Insurance contract liabilities	12,128
Deferred tax liabilities	1,487
Total liabilities	14,285
Total identifiable net assets at fair value	3,885
Goodwill arising on acquisition*	4,192
Purchase consideration transferred	8,077

*No reconciliation of the carrying amount of goodwill is provided on the basis the Group has no opening goodwill.

Analysis of cash flows on acquisition

Net cash acquired with the subsidiary (included in cash flows from investing activities)	3,411
Cash paid	(8,077)
Net cash flow on acquisition	(4,666)

Goodwill acquired is not deductible for tax purposes.

For the year ended 30 June 2020, SCPIL contributed revenue of \$8,413,000 and loss after taxation of \$457,000 to the Group's results. If the acquisition date for the business combination had been at the beginning of the reporting period, SCPIL would have contributed revenue of \$18,670,000 and profit after taxation of \$357,000 to the Group's results.

21 CHANGES IN FINANCIAL REPORTING STANDARDS



New accounting standards adopted on 1 July 2019

The consolidated financial statements include the first time adoption of NZ IFRS 16 *Leases* ("NZ IFRS 16"), applicable for the Group for annual reporting periods beginning on or after 1 January 2019.

NZ IFRS 16 replaced NZ IAS 17 *Leases* ("NZ IAS 17"). The Group elected to apply the new standard only to those contracts previously identified as leases under NZ IAS 17, as permitted by the practical expedient transition provisions in NZ IFRS 16. The standard sets out the principles for the recognition, measurement, presentation and disclosure of leases and requires lessees to account for all leases under a single on-balance sheet model.

Under NZ IAS 17, a lessee was required to make a distinction between finance and operating leases. Under NZ IFRS 16, a contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. The new standard requires lessees to recognise a right-of-use asset (representing its right to use the underlying asset) and a liability for future payments (representing its obligation to make lease payments) arising from all lease contracts, except for optional exemptions for either certain short-term leases or leases of low value assets. Lessees are required to recognise a finance charge on the liability and a depreciation charge on the asset which may affect the timing of the recognition of expenses on leased assets. The new standard may result in a higher interest expense in the earlier years of the lease, and a lower interest expense in the later years of a lease compared to a straight-line operating lease expense. This change mainly impacts the premises and motor vehicles that the Group previously accounted for as operating leases.

The Group elected to apply the new standard using the modified retrospective approach, with no restatement of comparative information. Discount rates are applied to portfolios of leases with reasonably similar characteristics. The Group applied the optional exemptions for short-term and low value asset leases, and elected not to include at transition those leases for which the lease term ends within 12 months of the date of initial application. The costs associated with those leases are instead included within the disclosure of short-term lease expense in the consolidated financial statements for the year ending 30 June 2020.

On initial application of the standard, the Group recognised a right-of-use asset and a lease liability at the lease commencement date. The right-of-use asset was initially measured at cost, less any lease incentive received, and is subsequently depreciated using the straight-line method from commencement date to the end of the lease term. The lease liabilities were measured at the present value of remaining lease payments, less any lease incentives receivable, discounted using an incremental borrowing rate. If the interest rate implicit in the lease cannot be readily determined, the lessee uses the lessee's incremental borrowing rate. The Group uses an individual discount rate for each portfolio of leases with reasonably similar characteristics, representing the weighted average incremental borrowing rates applied to lease liabilities recognised at the date of initial application. The discount rate used is a proxy rate as the Society is not entitled to borrow money as a friendly society.

NOTES TO THE FINANCIAL STATEMENTS (continued)

for the year ended 30 June 2020

21 CHANGES IN FINANCIAL REPORTING STANDARDS (continued)

Under NZ IFRS 16, right-of-use assets are tested annually for impairment in accordance with NZ IAS 36 *Impairment of Assets*. This replaces the previous requirement to recognise a provision for onerous lease contracts.

The impacts of adoption are disclosed as follows:

On transition to NZ IFRS 16, the Group recognised and presented separately in the statement of financial position an additional \$7,232,000 of right-of-use assets, and \$7,987,000 of lease liabilities.

The carrying amounts of the Group's right-of-use assets and lease liabilities and movements during the interim reporting period are as follows:

	Right-of-use assets			Lease liabilities
	Motor vehicles	Premises	Total	Total
	\$000	\$000	\$000	\$000
As at 1 July 2019	532	7,455	7,987	7,987
Lease incentives received prior to transition	-	(755)	(755)	-
Net value on initial recognition	532	6,700	7,232	7,987
Additions	292	719	1,011	1,011
Disposals	-	(137)	(137)	(137)
Depreciation	(268)	(4,084)	(4,352)	-
Interest expense	-	-	-	223
Payments	-	-	-	(4,998)
As at 30 June 2020	556	3,198	3,754	4,086

2020
\$000

Maturity analysis of undiscounted lease liabilities

Within 1 year	2,347
Between 1 and 2 years	1,062
Between 2 and 5 years	762
Greater than 5 years	83
Total	4,254

1 July 2019
\$000

Impact on financial statements

Operating lease commitments at 30 June 2019 as disclosed in the Group's consolidated financial statements	72,595
Discounted using the incremental borrowing rate at 1 July 2019	7,951

The difference is due to a lease commencing in October 2020, with initial annual lease payments of \$4,396,000 (subject to annual increases of 3%), which was considered an operating lease commitment as at 30 June 2019, but for which a right-of-use asset and corresponding lease liability will not be recognised until October 2020.



New accounting standards not yet effective

There are a number of standards, amendments and interpretations which have been approved but are not yet effective. The Group expects to adopt these when they become due for adoption. The impact of these is still to be determined. The most significant of these is NZ IFRS 17 *Insurance Contracts* ("NZ IFRS 17").

NZ IFRS 17 will replace NZ IFRS 4 *Insurance Contracts* for annual periods beginning on or after 1 January 2023. This means that the Group will be required to produce comparative financial information with effect from 1 July 2022 and a first set of full year financial statements under the new standard for the year ending 30 June 2024. IFRS17 project activities commenced. Impact assessments have been completed and activities are underway to consider options to respond to the changes that will be required to systems, processes and controls. Significant impact on systems is not expected: changes to the core system will be limited but opportunities will be considered on a cost/ benefit basis to make improvements to systems and processes. The Group will pursue the application of the Premium Allocation Approach, given the short term nature of medical and pet insurance products. The new standard establishes principles for the recognition, measurement, presentation and disclosure of insurance contracts issued. Disclosure and measurement under NZ IFRS 17 differs significantly from NZ IFRS 4, and the impact of this standard on the Group is still to be determined.



Independent Auditor's Report

To the members of The Southern Cross Medical Care Society

Report on the consolidated financial statements

Opinion

In our opinion, the accompanying consolidated financial statements of The Southern Cross Medical Care Society and its subsidiaries (the "Group") on pages 1 to 25:

- i. present fairly in all material respects the Group's financial position as at 30 June 2020 and its financial performance and cash flows for the year ended on that date; and
- ii. comply with New Zealand Equivalents to International Financial Reporting Standards and International Financial Reporting Standards.

We have audited the accompanying consolidated financial statements which comprise:

- the consolidated statement of financial position as at 30 June 2020;
- the consolidated statements of comprehensive income and changes in reserves, and cash flows for the year then ended; and
- notes, including a summary of significant accounting policies and other explanatory information.



Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (New Zealand) ("ISAs (NZ)"). We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

We are independent of the Group in accordance with Professional and Ethical Standard 1 (Revised) Code of Ethics for Assurance Practitioners issued by the New Zealand Auditing and Assurance Standards Board and the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (the "IESBA Code"), and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code.

Our responsibilities under ISAs (NZ) are further described in the Auditor's Responsibilities for the audit of the consolidated financial statements' section of our report.

Our firm has also provided other services to the Group in relation to the audit of the year-end solvency returns, review of the consolidated interim financial statements and the half-year solvency return. Subject to certain restrictions, partners and employees of our firm also deal with the Group on normal terms within the ordinary course of trading activities of the business of the Group. These matters have not impaired our independence as auditor of the Group. The firm has no other relationship with, or interest in, the Group.



Materiality

The scope of our audit was influenced by our application of materiality. Materiality helped us to determine the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and on the consolidated financial statements as a whole. The materiality for the consolidated financial statements as a whole was set at \$8,775,000 determined with reference to a benchmark of the Group's net assets. We chose the benchmark because, in our view, net assets is a key indicator of the Group's solvency and its ability to pay claims which is a primary area of focus for users of the consolidated financial statements.



Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the consolidated financial statements in the current period. We summarise below those matters and our key audit procedures to address those matters in order that the members as a body may better understand the process by which we arrived at our audit opinion. Our procedures were undertaken in the context of and solely for the purpose of our statutory audit opinion on the consolidated financial statements as a whole and we do not express discrete opinions on separate elements of the consolidated financial statements.

Key changes in the assessment of audit risks

COVID-19

The COVID-19 pandemic has created significant additional risks across a number of areas of the business, particularly the assessment of the insurance contract liabilities. The expected claims experience is inherently more uncertain due to changes in claims incidence and potential delays in receipt of claims notifications from policyholders. While the key audit matter "Valuation of insurance contract liabilities", detailed below, is unchanged from what would have been disclosed without COVID-19, the underlying audit risk has increased which impacted the extent and nature of audit evidence that we had to gather, specifically in relation to the key actuarial assumptions and judgements applied.

The key audit matter

How the matter was addressed in our audit and findings

Valuation of insurance contract liabilities

Refer to note 4 to the consolidated financial statements.

Valuation of the Group's provision for outstanding claims requires significant judgement from management and the Group's externally appointed actuarial specialist.

Our audit procedures included:

- testing the Group's IT systems and controls over claims, including the reconciliation of data from underlying systems to the data used in the actuary's valuation;
- testing a sample of claims to check whether they had the appropriate level of authorisation and support;
- with support from our actuarial specialists, assessing the work of the Group's Appointed Actuary in estimating the future claims costs on claims incurred prior to 30 June 2020 including:
 - the appropriateness of the valuation methodology, estimates and assumptions, against relevant accounting and actuarial standards;
 - the appropriateness of key assumptions including claims frequency, payment patterns and claims inflation against benchmark information; and
 - comparing previous estimates to actual claims development in the current year (i.e. performing a hindsight analysis).

We did not identify material exceptions from procedures performed, and found the judgements and assumptions, including those adopted in response to COVID-19, to be balanced and consistent with our understanding of the Group.



Other information

The directors, on behalf of the Group, are responsible for the other information included with the Group's consolidated financial statements. Other information includes the Appointed Actuary's report issued under section 78 of the Insurance (Prudential Supervision) Act 2010. Our opinion on the consolidated financial statements does not cover any other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Use of this independent auditor's report

This independent auditor's report is made solely to the members as a body. Our audit work has been undertaken so that we might state to the members those matters we are required to state to them in the independent auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the members as a body for our audit work, this independent auditor's report, or any of the opinions we have formed.

Responsibilities of the directors for the consolidated financial statements

The directors, on behalf of the Group, are responsible for:

- the preparation and fair presentation of the consolidated financial statements in accordance with generally accepted accounting practice in New Zealand (being New Zealand Equivalents to International Financial Reporting Standards) and International Financial Reporting Standards;
- implementing necessary internal control to enable the preparation of a consolidated set of financial statements that is fairly presented and free from material misstatement, whether due to fraud or error; and
- assessing the ability to continue as a going concern. This includes disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless they either intend to liquidate or to cease operations, or have no realistic alternative but to do so.



x **Auditor's responsibilities for the audit of the consolidated financial statements**

Our objective is:

- to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error; and
- to issue an independent auditor's report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs NZ will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error. They are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

A further description of our responsibilities for the audit of these consolidated financial statements is located at the External Reporting Board (XRB) website at:

<http://www.xrb.govt.nz/standards-for-assurance-practitioners/auditors-responsibilities/audit-report-1/>

This description forms part of our independent auditor's report.

The engagement partner on the audit resulting in this independent auditor's report is Kay Baldock.

For and on behalf of

KPMG

KPMG
Auckland

9 September 2020



Actuarial and Insurance Consultants

8 September 2020

The Directors
Southern Cross Medical Care Society
Auckland

Dear Directors

Review of Actuarial Information Contained in Financial Statements as at 30 June 2020

Finity Consulting Pty Limited (Finity) has been asked by Southern Cross Medical Care Society (the Society) to carry out a review of the 30 June 2020 Actuarial Information contained in the financial statements and used in their preparation and to provide an opinion as to the appropriateness of this information. John Smeed is an employee of Finity and is the Appointed Actuary to the Society. Finity has no relationship with the Society apart from being a provider of actuarial services.

The Society'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 2020 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 their preparation, or the determination of the solvency position for the Society as at 30 June 2020 is inappropriate. No limitations were placed on us in performing our review and all data and information requested was provided.

In our opinion the Society has maintained a solvency margin in excess of the minimum required as at the balance date.

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

Yours sincerely

John Smeed
Appointed Actuary

Anagha Pasche

Fellows of the New Zealand Society of Actuaries

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