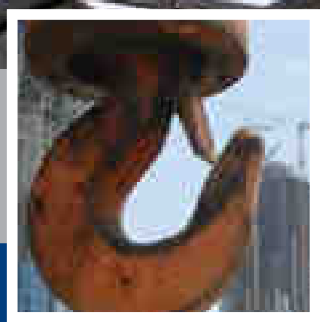
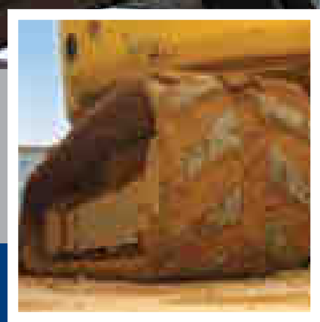
FEM

THE FEDERATED EMPLOYERS' MUTUAL ASSURANCE COMPANY LIMITED





Annual Report 2005

Contents

THE FEDERATED EMPLOYERS' MUTUAL ASSURANCE COMPANY LIMITED
Registration number: 1936/008971/06

Website address: www.fema.co.za

FEM
THE FEDERATED EMPLOYERS' MUTUAL ASSURANCE COMPANY LIMITED

Business

"every great achievement was once impossible"

FEM provides insurance cover to the construction industry alongside the State's Compensation Fund, which is managed by the Compensation Commissioner. This insurance compensates employees or their dependants following injury arising from occupational accidents and illness occasioned by industrial diseases.

FEM

Gives Away More For Health and Safety

FEM has, from its inception, been a firm supporter of health and safety in the construction industry. FEM promotes health and safety by granting an annual merit rebate to its policyholders. The annual merit rebates are a reward to policyholders that have had exceptional safety records for the year under review and can result in policyholders receiving up to fifty percent of their premium back. Annual functions are held nationally where silver awards of excellence are awarded to recognise the top performers for the year under review.

In 2005 the board of directors of FEM elected to grant a special "once-off" merit rebate award in addition to the normal annual merit rebate award. The criteria for this special merit rebate award was stepped up considerably as the aim was to reward the policyholders who over a five to ten year period consistently had exceptional health and safety records with FEM. Of the 2,513 policyholders considered for the special merit rebates, 465 qualified and received special merit rebates. In addition the qualifiers were ranked and the top fifty qualified for a special bronze award. The top overall performer was Dick Smith Construction who received the Gold award and the crystal trophy.

FEM paid out R 42 million in merit rebates and health and safety expenditure in 2005.

Dick Smith Construction

Dick Smith Construction has been operating since July 1973 and set up its main office in Phalaborwa in 1976. Phalaborwa having three different mines, demands very high safety standards which they have tried to surpass. To this end the mines approve hazard identification, risk assessments and safe work procedures prior to commencement of work. Prior to work commencement Site inductions are conducted and training on the proper use of PPE is done. The correct PPE is then issued and frequent inspections are done. Senior management views safety as a holistic process and involves all staff by rewarding them for safe work and by advertising their achievements. Dick Smith Construction believes that a good safety policy is imperative and any costs will be outweighed by the savings in avoiding injuries and lost time.

The Gold Award winners – Dick Smith Construction
Richard Fick (left) and Steve Lange (right)
FEM chairman Mr John Barrow (centre)

FEM encourages all policyholders to strive to achieve excellence in their health and safety efforts.

The report of the Chairman and the Managing Director

for the year ended 31 December 2005

We are pleased to report on the activities and results of The Federated Employers' Mutual Assurance Company Limited for 2005.

Business

The Federated Employers' Mutual Assurance Company Limited ("FEM") provides insurance cover to the construction industry alongside the State's Compensation Fund, which is managed by the Compensation Commissioner. This insurance compensates employees or their dependants following injury arising from occupational accidents and illness occasioned by industrial diseases.

Accounting Standards

In 2005, the South African Statements of Generally Accepted Accounting Practice were aligned with International accounting reporting standards, which has resulted in a change in the presentation and disclosure of the annual financial statements. Other than the changes resulting in the prior year adjustments disclosed in note 5, all other accounting policies are consistent with the previous year.

Overall Performance

In 2005, the company changed its accounting policy to account for all premium income in the year in which it is earned, rather than reported, thus resulting in a pipeline premium estimate being made. Prior year financial statements have been restated to account for the new policy and the impact of this has been disclosed in note 5a.

Net premium revenue for the year totalled R155,1 million, which is an increase of R29,7 million or 24% over the corresponding figure of R125,4 million for 2004.

Claims registered of 8,720 (2004: 8,096) have increased by 8% (2004: 9%) and medical claims paid have increased by 23% (2004: 17%), which is line with the growth in business of 24% (2004: 26%). Pensions paid have increased from R22,0 million to R23,2 million, or 6%.

The increase in the pensions liability in 2005 is R37,8 million compared with R68,7 million in 2004. The large increase in 2004 was as a result of the Compensation Commissioner awarding special increases ("Purchasing Power Parity" adjustments) to specified pensioners, and a small decrease in the net discount factor (See note 15.2).

The current year's movement in the pensions liability is as a result of:

- a decrease in the net discount rate of 1% (from 4% in 2004 to 3% in 2005) used in the valuation (See note 15.2); and
- a small increase in the average administration cost per pensioner due to staff restructuring within that department, therefore increasing the present value of the future liability.

The annual pension increase approved by the Compensation Commissioner, effective 01 April 2006 is 2%.

Total investment income, including net gains on financial assets, has increased by 47%, from R92,9 million in 2004 to R136,8 million in 2005 which is mainly attributable to an increase in net gains on financial assets of R 43,2 million.

Profit after tax for the year was R31,5 million (2004 restated: R12,0 million) – the significant increase is mainly as a result of the increase in net gains on financial assets. After the transfer of R3,8 million (2004 restated: R1,8 million) to the contingency reserve and the release of R37,3 million (2004: R40,4 million) in respect of the AIDS/claims/rehabilitation and special pensions reserves, the transfer to retained income amounted to R65,0 million (2004 restated: R50,6 million).

Highlights of the year under review

- *Premiums*

The company continues to record growth in premiums written, which can be attributed to the robust economy and continued low interest rates for the period, resulting in increased activity in the construction industry.

- *Information & technology*

FEM's computer systems continue to be enhanced to meet any new requirements and changes in the business environment. The systems are considered to be of a high standard and enable the provision of efficient services to policyholders and their employees, especially with the introduction of electronic communication with policyholders.

- *Claims management*

There has been a significant increase in claims paid this year, which is expected given the level of economic activity, especially in the construction industry, in South Africa. The continued engagement of professional claims managers to manage selected claims has proved once again to be a beneficial initiative.

- *Employment equity*

FEM is committed to meeting the targets of its employment equity plan, and is currently on target. In terms of the regulatory requirements, FEM submitted its first biennial report to the Department of Labour in October 2004 and the next report is due in October 2006.

- *Broad Based Black Economic Empowerment ("BEE") / Financial Sector Charter ("FSC")*

BEE and the FSC were introduced in late 2004 / early 2005. FEM management has noted the requirements of the FSC and is committed to meet the targets set out therein by 2008 and 2014. Processes are ongoing to achieve the requirements of the balanced scorecard. It should be noted that the FSC is a voluntary initiative, based on the requirements of the BEE Act, by the financial sector industry.

- *Corporate Governance*

It is our pleasure to report that the company is fully compliant with King II, as illustrated on pages 7 to 11 of the annual report.

Solvency margin - international basis

The international solvency margin is calculated as a percentage of net assets, per the financial statements, over net written premium. In 2005 the solvency margin has decreased slightly from 321% to 297% as a result of the increase in net premium income of 25%.

Occupational health, safety and rehabilitation

Financial assistance amounting to nearly R3 million was provided to the health and safety programmes of the various building industry associations. Statistics reflect a steady decrease in the number of workers injured proportionate to the number insured, with the accident frequency rates steadily decreasing each year, with a slight increase in 2005 (1995: 7.77, 2000: 6.82).

A run-off table of accident frequencies for the past 5 years is presented below. FEM's claims registered cycle is normally 2½ years, and therefore 2004 and 2005 are subject to change, but compared to prior years there is a clear indication of the decrease over time.

	Underwriting year				
Accident frequency at financial year end	2001	2002	2003	2004	2005
2001	5.34	-	-	-	-
2002	6.04	4.78	-	-	-
2003	*6.08*	5.49	4.56	-	-
2004	6.09	*5.53*	5.14	4.42	-
2005	6.10	5.54	*5.18*	4.97	4.75

It is also pleasing to note that FEM made a large number of health and safety awards to employers in recognition of their efforts to promote health and safety among their workers. During 2005, R42 million was given back as a result of the normal and "special" once off merit rebate awards, and accident prevention expenditure.

We have been advised that the Workers' Rehabilitation Centres in Benoni and Durban continue to provide excellent rehabilitative treatment facilities for injured workers and we urge you to become familiar with the services offered by these centres should you fall within these areas.

Thanks

Ready co-operation and assistance continues to be received from the office of the Compensation Fund at all levels and we are particularly grateful to the Acting Commissioner for this support.

Our sincere thanks must go to our fellow directors for their continued advice and wise counsel throughout the year.

Finally, we thank the executive committee and staff of FEM for their devoted and excellent service during the year.

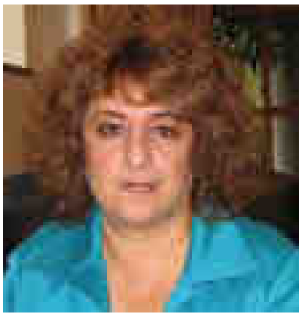
Prospects

FEM is strongly positioned to face the future challenges and remains committed to the provision of an effective and efficient compensation service to all our stakeholders. To all of them we extend our very best wishes for the time that lies ahead.

J A BARROW
Chairman
24 May 2006

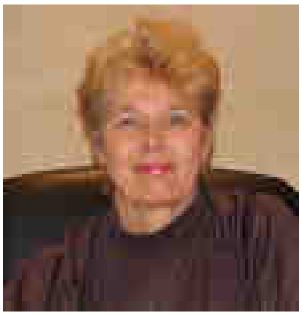
T T PUGH
Managing director

Management team



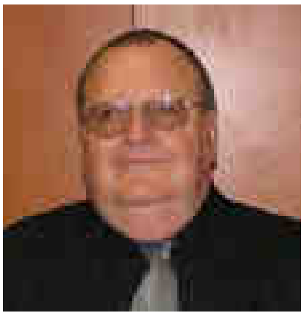
Thelma Pugh
Managing director

Ailsa Fox
Chief financial officer



Valerie Terry
Chief claims officer

Gys Mc Intosh
Chief information officer



Rod Saunders
Chief underwriting officer

Rob Spreadbury
Area manager (Inland)

Sakaria Shezi
Health & safety consultant

Ayesha Ismail
Chief human resources officer

Corporate Governance Statement

for the year ended 31 December 2005

The directors regard Corporate Governance as vitally important and are committed to applying principles necessary to ensure that good corporate governance is practised. These principles include discipline, independence, fairness, social responsibility and transparency. In this regard the directors endorse the code of corporate practice and conduct recommended in the King report. The Federated Employers' Mutual Assurance Company Limited ("the company") complies with the applicable recommendations of King.

By supporting these codes, the company demonstrates its commitment to the highest standards of integrity and ethical conduct in dealings with all its stakeholders. Monitoring the company's compliance with the King Code on Corporate Governance forms part of the audit and risk management committee charter.

The board of directors

At the end of the period under review there were ten directors (2004: Eleven) on the board, nine (2004: Ten) of whom are non-executive. The non-executive directors bring diversity and experience, insight and independent judgement on issues of strategy, performance, resources and standards of conduct. New appointments to the board are submitted to the board as a whole for approval, prior to appointment. The roles of the Chairman and the Managing director do not vest in the same person, and the Chairmen of the various board committees are non-executive directors.

The Chairman and Managing director provide leadership and guidance to the board, encourage proper deliberation on all matters requiring the board's attention and obtain optimum input from the other directors.

All directors have access to the advice and services of the company secretary, who is responsible to the board for ensuring that board procedures are followed. All directors are entitled to seek independent professional advice about the affairs of the company at the company's expense.

Executive directors have service contracts with the company containing normal notice periods. Non-executive directors have no service contracts with the company and in terms of the company's articles of association, one third of the directors retire by rotation and are eligible for re-election each year at the company's annual general meeting, and this year they are Messrs JA Barrow, H Ngakane and CE Saville.

Messrs GD Irons and JR Barrow were appointed as non-executive directors on 09 March 2005 and 17 March 2006 respectively. Mr DG Barrow resigned as director on 29 September 2005.

John Albert Barrow (67)

Mr JA Barrow is Chairman of Barrow Construction (Pty) Ltd. He is Chairman of FEM, a position to which he was appointed in 1986, after having served on the board since 1981.

Clifford Evan Saville (69)

Mr CE Saville retired as Managing director of the company and was simultaneously appointed as an independent non-executive director on 31 May 2004. He has 40 years insurance experience, worked at FEM for 22 years (he was appointed as Managing director in 2001) and served on the Compensation Fund board and chaired its audit committee.

Dr Herbert Ngakane (56)

Dr H Ngakane is a medical doctor who was appointed to the board in 2002. He has his own practice and brings medical expertise and advice to the board.

Geoffrey D Irons (54)

Mr GD Irons is the owner / director of GD Irons Construction (Pty) Ltd, which he formed in 1981. He has a BSc in Building Management.

John Robert Barrow (41)

Mr JR Barrow, Managing Director of Barrow Construction (Pty) Ltd, has joined the board of FEM with effect from 17 March 2006. He has a BSc in Civil Engineering and a BCom.

Director appointments made during a financial year are to be confirmed at the first annual general meeting following such appointment.

Executive and non-executive directors' emoluments are disclosed in note 28 to the annual financial statements.

The board of directors meet quarterly and has ultimate responsibility for strategic policy decisions, overall direction, control and performance. The board monitors management, ensuring that material matters are subject to board approval. The articles of association provide for material decisions, taken between meetings, to be confirmed by way of directors' resolutions.

Attendance at meetings during the year

Board and investment committee

	Mar	May	Aug	Nov
Non-executive directors				
JA Barrow (Chairman)	✓	✓	✓	✓
DG Barrow *(Resigned 29 September 2005)*	✓	-	✓	-
CS Jiyane	✓	✓	✓	✓
NF Maas	✓	✓	✓	✓
GD Irons *(Appointed 9 March 2005)*	-	-	✓	✓
Independent non-executive directors				
APH Jammine	✓	✓	✓	✓
H Ngakane	✓	✓	✓	✓
CE Saville	✓	✓	✓	✓
H Walker	-	✓	✓	✓
PL Wilmot	✓	✓	✓	✓
Executive directors				
TT Pugh (Managing)	✓	✓	✓	✓

To assist the board in discharging its collective responsibility for corporate governance, several committees have been established, to which certain of the board's responsibilities have been delegated. Each committee of the board operates in terms of a formal written charter and comprises non-executive directors only. The Chairmen of the board and each committee are elected annually after the annual general meeting.

Audit and risk management committee

The audit and risk management committee meets at least twice a year with management and the external and internal auditors. The external auditors have unrestricted access to the committee and the committee has unrestricted access to the company's management, employees, external and internal auditors and outside consultants.

The audit and risk management committee, which operates in accordance with a written charter authorised by the board, provides assistance to the board with regard to:

- ensuring compliance with applicable legislation and the requirements of regulatory authorities;
- compliance with the company's code of ethics;
- matters relating to financial and internal control, accounting policies, reporting and disclosure;
- the scope, adequacy and effectiveness of the systems of internal control and the annual audit;
- review and approval of external and internal audit plans, findings, problems, reports and fees; and
- monitoring and review of all tax compliance activities.

From a risk perspective, the responsibility of the committee is to oversee the quality, integrity and reliability of the company's risk management function. The committee has also been delegated the task of reviewing and assessing the integrity and quality of the control systems and ensures that risk policies and strategies are effectively managed.

From an audit perspective, the committee assists the board by performing an objective and independent review of the organisation's finance and accounting control mechanisms.

The audit and risk management committee performs its function through close liaison and communication with management, and the internal and external auditors.

The audit and risk management committee addressed its responsibilities properly in terms of the charter during the 2005 financial year.

Attendance at meetings during the year

	March	July
PL Wilmot (Chairman)	✓	✓
DG Barrow	✓	✓
H Walker	✓	✓

Mr DG Barrow resigned from the board on 29 September 2005, and is to be replaced with Mr NF Maas from the first audit and risk management committee meeting in 2006, to be held in March.

Remuneration committee

The remuneration committee meets at least once a year. The remuneration committee advises the board on remuneration policies, packages and other terms of employment for all directors and senior executives. Its specific terms of reference also include recommendations to the board in matters relating, inter-alia, to staff remuneration policies, incentive schemes, executive salaries and directors' fees and retirement funds. The committee may seek advice from independent professional advisors. The committee meets only once a year unless otherwise required.

Attendance at meeting during the year

	November
H Walker (Chairman)	✓
JA Barrow	✓
APH Jammine	✓

Investment committee

The investment committee comprises the full board, which meets quarterly. The investments are managed by Investec Asset Managers, who manage the portfolio in terms of a mandate approved by the board. The fund manager reports to, and discusses the investment performance and future activities with the investment committee on a quarterly basis.

Executive committee

The Managing director, Mrs TT Pugh, chairs the executive committee, which comprises all Chief Officers.

The committee is responsible for implementing the strategies and policies determined by the board, managing the business affairs of the company, prioritising the allocation of capital and technical human resources and establishing best management practices.

The committee is also responsible for management appointments and monitoring their performance.

The present committee comprises:

- TT Pugh (managing director)
- A Fox (chief financial officer)
- A Ismail (chief human resources officer)
- GM Mc Intosh (chief information officer)
- VPA Terry (chief claims officer)
- RA Saunders (chief underwiting officer)

Risk management and internal control

The board of directors acknowledges that it is responsible for the total process of risk management, recognising enterprise-wide risks to which the company is exposed and ensuring that the proper policies of control and mitigation are put in place. Management is continuously developing and enhancing its risk and control procedures to improve the mechanisms for identifying and monitoring risks.

The directors recognise their responsibility for internal, financial and operating controls and the monitoring of their effectiveness, including communicating appropriate risk and control policies throughout the organisation. Ethical behaviour, compliance with legislation and sound accounting practice underpin the internal control process. The audit and risk management committee is responsible for identifying, evaluating and managing significant risks on a regular basis.

The financial and operating controls are designed to provide assurance regarding the integrity and reliability of the annual financial statements and to adequately safeguard, verify and maintain accountability of the company's assets. However, no matter how well designed, these controls can be circumvented and therefore provide only reasonable and not absolute assurance with respect to the reliability of financial information and annual financial statement presentation.

The operating policies include a documented organisational structure and division of responsibility, established policies and procedures, including a Code of Ethics to foster a strong ethical climate, which are communicated throughout the company. It also includes the careful selection, training and development of people.

The Managing director and chief financial officer are responsible for designing and maintaining the operation of the financial and operating controls and for their ongoing appropriateness. They consider that the systems are appropriately designed to provide reasonable, but not absolute, assurance that the assets are safeguarded against material loss or unauthorised use and that transactions are properly authorised and recorded.

Internal audit monitors the operation of the underwriting, claims and pensions internal control systems and reports findings and recommendations to management and to the audit and risk management committee. Corrective action is taken to address control deficiencies and other opportunities for improving the system as they are identified.

Annual financial statements

Management prepare the annual financial statements and other information in the annual report, which is approved by the board. The directors are responsible for ensuring they are prepared in a manner that fairly presents the financial position and the results of the operations and cash flows of the company for the year ended 31 December 2005.

The annual financial statements set out on pages 14 to 51 have been prepared in accordance with South African Statements of Generally Accepted Accounting Practice. They are based on appropriate accounting policies, which are consistently applied in all material aspects, except where otherwise stated, and are supported by reasonable and prudent judgements and estimates. Adequate accounting records have been maintained throughout the year under review.

The external auditors are responsible for carrying out an independent examination of the annual financial statements in accordance with International Standards on Auditing, and for reporting whether they are fairly presented. The auditors' report is set out on page 14 of these annual financial statements.

The external auditors were given unrestricted access to all financial records and related data, including minutes of all meetings of shareholders, the board of directors, and committees of the board. Management believe that all representations made to the independent auditors during their audit are valid and appropriate.

Going concern

The going concern basis has been adopted in preparing the annual financial statements. Based on forecasts and available cash resources, the directors have every reason to believe that the company will have adequate resources to continue to meet its obligations for the foreseeable future.

A business continuity and disaster recovery plan has been developed and documented.

Ethical standards

The company has a Code of Ethics, which has been fully endorsed by the board and applies to all directors and employees. The Code is regularly reviewed and updated as necessary to ensure it reflects the highest standards of behaviour and professionalism.

In summary, the Code requires that at all times all company personnel act with the utmost integrity and objectivity and in compliance with the letter and spirit of both the law and company policies. Failure by employees to act in terms of the Code results in disciplinary action.

The Code is discussed with each new employee as part of his/her induction training, and all employees are asked to sign an annual declaration confirming their compliance with the Code.

A "whistle-blowing" facility exists for reporting of non-adherence to the Code of Ethics or ethics-related matters.

The directors believe that ethical standards are being met and fully support the ethics programme.

External auditors independence

PricewaterhouseCoopers Inc. ("PwC") are the external auditors of FEM. In 2005 FEM utilised the services of PwC in respect of certain accounting advice and the non-audit fees incurred totalled R33 thousand ("k") (2004: Rnil) (see note 22.3).

Employment equity

An employment equity plan has been in operation for some considerable time and is overseen by the Managing director and a staff-elected employment equity committee. Accordingly, we have ensured that our employment policies, practices and working environment are non-discriminatory.

In terms of the regulatory requirements FEM submitted its five-year plan in 2002 and in October 2004, submitted its first annual report to the Department of Labour; FEM is currently on target to meet the requirements of the Employment Equity Act.

We are pleased to report that 80% (2004: 84%) of our vacancies have been filled with candidates from designated groups against our target of 70%. Due to low staff turnover, the focus of accelerated development programmes has been protracted, but we have identified succession planning as crucial and staff from designated groups have been identified to be fast-tracked and developed in an endeavour to be placed in key positions in the organisation.

Statement
of responsibility by the Board of Directors

for the year ended 31 December 2005

The directors are responsible for the integrity and fair presentation of the financial statements of The Federated Employers' Mutual Assurance Company Limited which is prepared by management. The financial statements presented on pages 14 to 51 have been prepared in accordance with South African Statements of Generally Accepted Accounting Practice, and include amounts based on judgements and estimates made by management.

The directors consider that in preparing the financial statements they have used the most appropriate accounting policies, consistently applied and supported by reasonable and prudent judgements and estimates, and that all South African Statements of Generally Accepted Accounting Practice that they consider to be applicable have been followed. The directors are satisfied that the information contained in the financial statements fairly presents the results of operations for the year and the financial position of the company at year-end. Management prepared the other information included in the annual report and the directors are responsible for both its accuracy and its consistency with the financial statements.

The directors have responsibility for ensuring that accounting records are kept. The accounting records should disclose with reasonable accuracy the financial position of the company to enable the directors to ensure that the financial statements comply with the relevant legislation, and present fairly the results of operations and financial position of the company. The company operates in a sound control environment, which is well documented and regularly reviewed. This incorporates risk management and internal control procedures, which are designed to provide reasonable, but not absolute, assurance that assets are safeguarded and the risks facing the business are being controlled. There were no breakdowns in controls in this financial period.

The going-concern basis has been adopted in preparing the financial statements. The directors have no reason to believe that the company will not be a going concern in the foreseeable future based on forecasts and available cash resources. These financial statements support the viability of the company.

The company has adhered to the Code of Corporate Practices and Conduct.

The company's external auditors, PricewaterhouseCoopers Inc., audited the financial statements, and their report is presented on page 14.

The financial statements were approved by the board of directors on 24 May 2006 and are signed on its behalf by:

J A BARROW
Chairman

T T PUGH
Managing director

24 May 2006

Certificate
by the Company Secretary
for the year ended 31 December 2005

As Company Secretary, I hereby confirm, in terms of the Companies Act, 1973, that for the year ended 31 December 2005, the company has lodged with the Registrar of Companies all such returns as are required of a public company in terms of the Act, and that all such returns are true, correct and up to date.

E J WILLIS
Secretary
24 May 2006

Independent Auditors' Report

for the year ended 31 December 2005

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF THE FEDERATED EMPLOYERS' MUTUAL ASSURANCE COMPANY LIMITED

We have audited the annual financial statements of The Federated Employers' Mutual Assurance Company Limited set out on pages 15 to 51 for the year ended 31 December 2005. These financial statements are the responsibility of the company's directors. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with International Standards on Auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures included in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements fairly present, in all material respects, the financial position of the company at 31 December 2005 and the results of its operations and cash flows for the year then ended in accordance with South African Statements of Generally Accepted Accounting Practice and in the manner required by the Companies Act of South Africa.

PricewaterhouseCoopers Inc.

PRICEWATERHOUSECOOPERS INC.
Registered Auditor

24 May 2006
JOHANNESBURG

Directors' report

for the year ended 31 December 2005

The directors have pleasure in submitting their report, which forms part of the audited annual financial statements of the company for the year ended 31 December 2005.

Nature of business

The company was established as a mutual insurer in 1936 and, on the introduction of the Workmen's Compensation Act, 1941, was granted a licence to transact workmen's compensation insurance for the building industry. Its business operations are essentially confined to the insurance of employers against their liabilities under the Compensation for Occupational Injuries and Diseases Act, 1993 and extends to any employer falling within Class V of the Commissioner's industrial classifications for the building and construction industry.

In terms of the articles of association of the company, shareholding is restricted to policyholders.

Operating and financial review

The company continues to record growth in premium revenue, which can be attributed to the improved economy and continued low interest rates, resulting in increased activity in the construction industry.

	Movement %	2005 R'000	2004 R'000
Insurance results			
Net premium revenue (Note 18)	24%	155,070	125,449
Claims (excluding pensions) less reinsurance recoveries (Note 21)	70%	(85,886)	(50,400)
New pensions awarded (funded by premiums)	(39%)	(17,531)	(28,558)
Administration expenses	(11%)	(25,951)	(29,234)
Accident prevention expenses	27%	(6,093)	(4,809)
Profit before pensions and rebates	**58%**	**19,609**	**12,448**
Pensions paid and net movement in pensions liability (excluding new awards above) (Note 21)	(30%)	(43,455)	(62,100)
Loss before rebates	**(52%)**	**(23,846)**	**(49,652)**
Rebates paid and provided - normal (Note 15.4)	102%	(57,307)	(28,330)
Rebates paid and provided - special (Note 15.4)	100%	(9,216)	-
Underwriting loss for the year	**16%**	**(90,369)**	**(77,982)**

As can be seen on the previous page, the company reports a profit before pensions paid and net movement in the pensions liability, and rebates paid and provided. The underwriting losses are mainly attributed to the fact that the discretionary rebates and the cost of maintaining the pensioners (monthly pensions paid and movement in the valuation of the pensions liability) is supported by investment income, which does not form part of the calculation in determining the underwriting result.

Key statistics relating to the financial position and income for the year are set out below:

	Change %	2005 R'000	2004 R'000
Financial position			
Total assets	**20%**	**1,040,586**	**869,892**
Available-for-sale financial assets	36%	892,096	657,892
Short term investments	(35%)	67,704	104,120
Cash & cash equivalents	(54%)	26,822	58,610
Total liabilities	**23%**	**560,995**	**454,466**
Outstanding claims	40%	104,331	74,506
Capitalised value of pensions	14%	311,001	273,222
Provision for rebates (non-current & current)	56%	79,148	50,716
Capital and reserves	**15%**	**479,591**	**415,426**
Operating results			
Net premium revenue	24%	155,070	125,449
Investment income	1%	56,864	56,137
Net gains on available-for-sale financial assets	118%	79,890	36,727
Net claims and benefits, and rebates	26%	(213,395)	(169,388)
Expenses	(16%)	(35,142)	(41,715)
Profit before tax	**500%**	**43,287**	**7,210**

Full details of the company's financial results are set out in the financial statements and notes thereto on pages 18 to 51.

Post balance sheet events and contingent liabilities

The directors are not aware of any post balance sheet events that would have a material effect on the financial statements at 31 December 2005, or require disclosure.

The company has no contingent liabilities.

Share capital

There were no changes in the authorised and issued capital of 500,000 shares of 2 cents each during the year under review.

The shares of the company are owned by the policyholders, except for "floating capital" which is held by The Federated Employers' Trust Limited to allow for ease of entrance and exit of policyholders.

Dividends

In terms of clause 26.1 of the company's articles of association, shareholders are not entitled to any dividends or distribution of the assets of the company, either during the life of the company or upon its liquidation.

Directors' interests in contracts

No material contracts in which the directors have an interest were entered into in the current year other than the transactions detailed in Note 26.2 to the financial statements.

Directors

Details of directors' remuneration are set out in Note 28 to the financial statements.

The following were directors of the company during the financial year:

JA Barrow (Chairman)	Non-executive	
TT Pugh	Managing director	
DG Barrow	Non-executive	*Resigned 29 September 2005*
JR Barrow	Non-executive	*Appointed 17 March 2006*
GD Irons	Non-executive	*Appointed 09 March 2005*
APH Jammine	Independent non-executive	
CS Jiyane	Non-executive	
NF Maas	Non-executive	
Dr H Ngakane	Independent non-executive	
CE Saville	Independent non-executive	
H Walker	Independent non-executive	
PL Wilmot	Independent non-executive	

In accordance with the articles of association of the company, Messrs JA Barrow, H Ngakane and CE Saville will retire from office at the forthcoming annual general meeting and are eligible for re-election.

Director appointments made during a financial year are to be confirmed at the first annual general meeting following such appointment. The appoinments of Messrs JR Barrow and GD Irons are to be confirmed at the forthcoming meeting.

The audit and risk management committee comprised PL Wilmot (Chairman), DG Barrow and H Walker.

The remuneration committee comprised H Walker (Chairman), JA Barrow and APH Jammine.

Secretary

The secretary of the company is Ms EJ Willis.

Business Address:	**Postal Address:**
1st Floor, Block B	Private Bag 87109
65 Central Street	Houghton
Houghton	2041
2198	

Auditors

PricewaterhouseCoopers Inc. will continue in office in accordance with Section 270(2) of the Companies Act in South Africa.

Balance sheet as at 31 December 2005

	Notes	2005 R'000	2004 R'000
Assets			
Non-current assets		**895,245**	660,444
Furniture, equipment and motor vehicles	6	**3,149**	2,552
Available-for-sale financial assets	7	**892,096**	657,892
Reinsurance assets	8	**8,303**	5,938
Current assets		**137,038**	203,510
Tax overpaid		**11,451**	12,888
Insurance assets	9	**16,283**	14,671
Other receivables	10	**14,753**	13,221
Related parties	26.1	**25**	-
Short-term investments	11	**67,704**	104,120
Cash and cash equivalents	2.5	**26,822**	58,610
Total assets		**1,040,586**	869,892
Equity and liabilities			
Capital and reserves		**479,591**	415,426
Ordinary share capital	12	**10**	10
Other reserves	13	**124,756**	125,564
Retained income		**354,825**	289,852
Deferred tax liability	14.1	**26,207**	13,550
Insurance liabilities		**527,803**	424,421
Outstanding claims	15.1	**104,331**	74,506
Capitalised value of pensions	15.2	**311,001**	273,222
Provision for unearned premiums	15.3	**28,439**	22,180
Provision for rebates - non-current	15.4	**43,511**	27,292
Provision for rebates - current	15.4	**35,637**	23,424
Reinsurance liabilities	15.5	**4,884**	3,797
Current liabilities		**6,985**	16,495
Accounts payable	16	**6,067**	15,607
Related parties	26.1	**-**	34
Provisions	17	**918**	854
Total equity and liabilities		**1,040,586**	869,892

Income statement for the year ended 31 December 2005

	Notes	2005 R'000	2004 R'000
Premium revenue	18	**173,767**	141,413
Premium revenue ceded to reinsurers	18	**(18,697)**	(15,964)
Net premium revenue	18	**155,070**	125,449
Investment income	19	**56,864**	56,137
Net realised gains on financial assets	20	**79,890**	36,727
Net income		**291,824**	218,313
Insurance claims & benefits - claims	21	**93,243**	56,874
Insurance claims & benefits - pensions	21	**60,986**	90,658
Insurance claims & benefits recovered from reinsurers	21	**(7,357)**	(6,474)
Rebates paid & provided	15.4	**66,523**	28,330
Net claims & benefits, and rebates		**213,395**	169,388
Administration expenses	22	**25,951**	29,234
Asset management expenses		**3,098**	7,672
Accident prevention expenses		**6,093**	4,809
Expenses		**248,537**	211,103
Profit before tax		**43,287**	7,210
Income tax (expense) / credit	14.2	**(11,861)**	4,751
Profit for the year		**31,426**	11,961

Statement of changes in equity

for the year ended 31 December 2005

	Share capital	Retained income	Statutory contingency reserve	Special pensions reserve	AIDS/ claims/ rehabilitation reserve	Asset revaluation reserve	TOTAL
	R'000	R'000	R'000	R'000	R'000	R'000	R'000
Year ended 31 December 2003	10	235,357	10,310	57,814	20,000	36,828	360,319
Prior year adjustment (Note 5a)	-	2,741	861	-	-	-	3,602
Prior year adjustment (Note 5b)	-	1,108	-	-	-	(1,064)	44
At beginning of year (restated)	10	239,206	11,171	57,814	20,000	35,764	363,965
Profit for the year	-	11,961	-	-	-	-	11,961
Transfer to contingency reserve	-	(1,772)	1,772	-	-	-	-
Transfer from special pensions reserve	-	40,457	-	(40,457)	-	-	-
Net movement in fair value of available-for-sale financial assets	-	-	-	-	-	39,500	39,500
Balance at 31 December 2004 (restated)	**10**	**289,852**	**12,943**	**17,357**	**20,000**	**75,264**	**415,426**
Balance at 1 January 2005	**10**	**289,852**	**12,943**	**17,357**	**20,000**	**75,264**	**415,426**
Profit for the year	-	31,426	-	-	-	-	31,426
Transfer to contingency reserve	-	(3,810)	3,810	-	-	-	-
Transfer from special pensions reserve	-	17,357	-	(17,357)	-	-	-
Transfer from AIDS/claims/ rehabilitation reserve	-	20,000	-	-	(20,000)	-	-
Net movement in fair value of available-for-sale financial assets	-	-	-	-	-	32,739	32,739
Balance at 31 December 2005	**10**	**354,825**	**16,753**	**-**	**-**	**108,003**	**479,591**

	Notes	2005 R'000	2004 R'000
Cash flows from operating activities			
Cash (used in) / generated from operations	23.1	**(32,947)**	32,347
Income tax paid	23.2	**(8,181)**	(8,267)
Net cash (used in) / generated from operating activities		**(41,128)**	24,080
Cash flows from investing activities			
Purchases of available-for-sale financial assets		**(274,953)**	(254,299)
Disposals of available-for-sale financial assets		**286,102**	262,409
Purchase of furniture, equipment & motor vehicles		**(1,969)**	(392)
Proceeds from sale of furniture, equipment & motor vehicles		**158**	16
Proceeds from sale of non-capital equipment		**2**	-
Net cash used in investing activities		**9,340**	7,734
Net (decrease) / increase in cash and cash equivalents		**(31,788)**	31,814
Cash and cash equivalents at beginning of year		**58,610**	26,796
Cash and cash equivalents at end of year	2.5	**26,822**	58,610

1. General information

The company is a public company, incorporated and domiciled in South Africa and is licensed as a Short-Term insurer by the Financial Services Board.

2. Summary of significant accounting policies

The following are the principal accounting policies of the company, which have been applied on a basis consistent with the previous year, unless otherwise stated. Refer to note 5 regarding changes in accounting policies resulting in prior year adjustments.

2.1. Basis of presentation

The annual financial statements are prepared in accordance with South African Statements of Generally Accepted Accounting Practice ("GAAP"). The financial statements are prepared under the historical cost basis as modified by the revaluation of certain financial assets and liabilities.

The preparation of financial statements in conformity with GAAP requires the use of certain critical accounting estimates. It also requires management to exercise judgement in the process of applying the company's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements, are disclosed in Note 3.

All amounts in the financial statements are shown in thousands of Rands, rounded to the nearest thousand, unless otherwise stated.

2.2. Furniture, equipment and motor vehicles

Furniture, equipment and motor vehicles are stated at historical cost less accumulated depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items. All repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

Depreciation is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives as follows:

- Furniture & fittings 5 – 10 years
- Motor vehicles 4 – 5 years
- Computer equipment 3 years

The assets' residual values and useful lives are reviewed at each balance sheet date and adjusted as appropriate. Where the carrying amount of an asset is greater than its estimated recoverable amount, it is written down immediately to its recoverable amount. Gains and losses on disposal of furniture, equipment and motor vehicles are determined by comparing proceeds with carrying amounts, and are included in the income statement.

2.3. Financial assets

The company's financial assets can be split into three categories – investments, reinsurance assets and other receivables.

Investments

Investments are classified as available-for-sale financial assets. Management determines the classification of its investments at initial recognition and re-evaluates this at each reporting date.

Available-for-sale financial assets

Recognition & measurement

Available-for-sale assets are non-derivative financial assets that are not classified in any of the other categories as defined in AC133, and comprise equity and debt securities. Available-for-sale financial assets are intended to be held for an indefinite period of time, but may be sold in response to liquidity or other needs.

These investments are initially recognised at cost, including transaction costs, and are subsequently carried at fair value. The fair values of quoted equities are based on current bid prices and quoted bonds are based on market value. Unrealised gains and losses arising from changes in the fair value are recognised in equity.

When these investments are sold or impaired, the accumulated fair value adjustments are released from equity and included in the income statement as net realised gains / losses on financial assets.

Investments are derecognised when the rights to receive cashflows from investments have ceased or where they have been transferred and the company has also transferred substantially all risks and rewards of ownership.

Impairment

The company assesses at each balance sheet date whether there is objective evidence that an available-for-sale financial asset is impaired, including a significant or prolonged decline in the fair value of the security below its cost. If any such evidence exists, the cumulative loss - measured as the difference between the acquisition cost and current fair value, less any impairment loss on the financial asset previously recognised in profit or loss – is removed from equity and recognised in the income statement.

Reinsurance assets

Receivables arising from reinsurance contracts are accounted for as described in note 2.6 and are reviewed for impairment as part of the impairment review of other receivables.

Other receivables

Other receivables are carried at cost, which approximates fair value.

Receivables arising from insurance contracts, including but not limited to policyholder balances and pipeline premium, are classified in this category, but disclosed separately on the balance sheet as "Insurance assets", and are designated as fair value through income.

Impairment

The company assesses, at each balance sheet date, whether there is objective evidence that a receivable or group of receivables is impaired. Such receivables are impaired, and impairment losses are incurred, only if there is objective evidence of impairment as a result of one or more events that have occurred after initial recognition of the assets ("loss event") and that loss event/s has an impact on the estimated future cashflows of the asset, that can be reliably estimated. Objective evidence that such an asset(s) is impaired includes observable data that comes to the attention of the company.

The assets may be impaired individually or assessed as a group of assets. If there is objective evidence that an impairment loss has been incurred, an impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The carrying amount is reduced through an allowance account and the loss is recognised in the income statement.

2.4 Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the balance sheet only when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis or to realise the asset and settle the liability simultaneously.

2.5 Short term investments and Cash & cash equivalents

Cash and cash equivalents includes cash in hand and deposits held at call with banks, which includes petty cash, the operational bank account and the investment settlement bank account.

Short-term investments are other short-term highly liquid investments and comprise money market unit trusts.

2.6 Insurance contracts

The company issues insurance policies in respect of benefits payable to employees injured on duty, in terms of the Compensation for Occupational Injuries and Diseases Act ("COID Act") and operates under licence to the Compensation Commissioner. These benefits include, but are not limited to, medical costs, temporary loss of income, permanent disablement, sundry costs and pensions, as defined in the COID Act.

Recognition and measurement

Premium

Premium income (estimated premium and pipeline premium) is recognised in the financial period that the risk incepts. The statutory period of insurance cover is from 01 March to 28 February i.e. annual business. Premium income is shown net of allowances for impairments and write offs.

a) Estimated premium

Policyholders project their employees' wages for the insurance period and, based on COIDA rates, an estimated premium for that period is determined. At the end of the period of insurance, the policyholder reports actual wages, which will determine the actual premium. The variance between the estimated premium and actual premium is referred to as "adjustment to estimates".

b) Pipeline premium

This refers to the above-mentioned "adjustment to estimates" i.e. premium which has been "earned" in the current financial period, but will only be reported by the policyholders in the next financial period. In the subsequent financial period, when the actual premium adjustment is ascertained, the pipeline premium provision is reversed.

Pipeline premiums have been calculated as a percentage of current years estimated premium, currently 10%. The percentage used is based on prior year's history and economic factors, specifically relating to the construction industry including the current shortage of skills and materials. (See note 5a – Change in accounting policy: Prior year adjustment).

Unearned premiums are carried forward and are those proportions of the written premiums that relate to risks that have not expired at the end of the financial year. The proportions unearned are calculated on the 1/365th basis.

Claims & benefits

The company has two main categories of claims and benefits, as detailed below:

a) Capitalised value of pensions

The capitalised value of pensions ("CVP") liability is the present value of future pension liabilities and administration expenses, net of any investment income that may be earned. The liability is based on assumptions as to future pension increases, mortality and morbidity, management expenses and investment income, which are reviewed for reasonableness by management on an annual basis.

This liability is recalculated at each balance sheet date, using the assumptions above. Independent actuarial valuations of the CVP are carried out annually and adjusted for any changes in the assumptions. Adjustments to the liability are charged to income as incurred.

b) Claims

Claims and loss adjustment expenses are charged to income as incurred, based on the estimated liability for compensation. They include all costs incurred and arise from events that have occurred up to the balance sheet date, even if they have not yet been reported to the company. The company does not discount its liabilities for unpaid claims.

Liabilities for unpaid claims are calculated based on an estimated average cost per claim for each underwriting year. The incurred but not reported claims ("IBNR") are based on estimated unreported claims.

The average cost per claim is based on the actual claims paid and awards made, and estimated outstanding costs (based on the latest and most reliable information available), and the number of claims registered.

Liability adequacy test in respect of claims and benefits

At each balance sheet date, liability adequacy tests are performed to ensure the adequacy of the insurance liabilities. In performing these tests, current best estimates of future cashflows and administration expenses, as well as investment income, are used. Any deficiency is immediately charged to income.

Reinsurance

The contract entered into by the company with reinsurers under which the company is compensated for losses meets the insurance classification requirements in this note, and are classified as reinsurance contracts held.

Reinsurance recoveries are the benefits to which the company is entitled to under its reinsurance contract in respect of claims and benefits incurred. The amounts recoverable are dependent on the expected claims and benefits, as described above, and are calculated in accordance with the terms and conditions of the reinsurance agreement.

Reinsurance assets are the unsettled amounts due and payable by the reinsurers in respect of reinsurance recoveries to which the company is entitled to under its reinsurance contract. These assets consist of short-term balances due from reinsurers, which are classified as other receivables, and longer-term receivables, which are classified as reinsurance assets.

Reinsurance premium (Premium revenue ceded) are the premiums payable in respect of the reinsurance contract, including the anticipated liability in respect of pipeline premiums and are recognised as an expense when incurred. In certain cases retrospective reinsurance premiums are paid (reinstatement premiums), which are charged to income as incurred.

Reinsurance liabilities are premiums outstanding in respect of the reinsurance contract.

The company assesses its reinsurance assets for impairment on an annual basis. If there is objective evidence that the reinsurance asset is impaired, the company reduces the carrying amount of the asset to its recoverable amount and recognises that impairment in the income statement. The company gathers the objective evidence that a reinsurance asset is impaired, and accounts for the impairment loss using the same process adopted for other receivables. These processes are described in Note 2.3.

Rebates

Rebates are paid to policyholders with low claims experiences, specifically to recognise and reward health and safety.

Rebates are paid 2½ years after the inception of an underwriting period. The amount paid is based primarily on the policyholder's claims experience in respect of that underwriting year, and calculated as a percentage of premium paid.

In each underwriting year a provision for rebates, to be paid in 2½ years, is made. The provision is calculated at 25% (2004: 20%) of premium income, and any shortfall / excess in the provision is charged / released to income in the year of payment.

Receivables and payables related to insurance contracts

Receivables and payables are recognised when due. These include amounts due to and from policyholders, including, but not limited to, premiums, refunds and rebates. If there is objective evidence that an insurance receivable is impaired, the company reduces the carrying amount of the receivable to its recoverable amount and recognises that impairment in the income statement.

2.7 Deferred income tax

Deferred income tax is provided in full using the liability method, on temporary differences arising between the tax basis of assets and liabilities and their carrying amounts in the financial statements. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantively enacted by the balance sheet date and are expected to apply when the related deferred income tax asset or liability is realised or settled respectively.

Deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

2.8 Employee benefits

a) Pension obligations

The company operates a defined contribution pension plan. Under a defined contribution plan the company pays contributions to a publicly administered pension insurance plan on a mandatory, contractual or voluntary basis. The contributions are recognised as an employee benefit expense when they are due. The company has no legal or constructive obligations to pay further contributions if the fund does not hold sufficient assets to pay all employees the benefits relating to employee service in the current and prior periods.

2.9 Provisions

Provisions are recognised when the company has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made.

Leave pay

Employee's entitlement to annual leave is recognised when it accrues to employees. A provision is made for the estimated liability for annual leave as a result of services rendered by employees up to the balance sheet date.

2.10 Revenue recognition

a) Investment income

Investment income on financial assets: debt securities is recognised using the effective interest method, which is a method of calculating the amortised cost of a financial asset and of allocating the interest income over the relevant period. The effective interest rate is the rate that discounts estimated future cash receipts through the expected life of the financial asset. The calculation includes all fees, transaction costs and premiums or discounts on the instrument. Previously the amortisation of the premium / discount, was charged / credited to equity through the fair value adjustment, and now this amount is charged / credited to income as part of interest income on debt securities. (Refer to note 5b – Change in accounting policy: Prior year adjustment).

Investment income on money market instruments (cash & cash equivalents and short term investments) is recognised in the income statement as earned i.e. the accruals basis.

b) Dividend income

Dividend income for financial assets: equities is recognised when the right to receive payment is established – this is the ex-dividend date for equity securities.

2.11 Leases

Operating leases

Leases of assets under which the lessor effectively retains all the risks and benefits of ownership are classified as operating leases. Payments made under operating leases are charged to the income statement on a straight-line basis over the period of the lease.

When an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognised as an expense in the period in which termination takes place.

2.12 Statutory contingency reserve

In terms of the reserving requirements of the Short-term Insurance Act of 1998, FEM is required to hold 10% of gross premiums written less approved reinsurance as a statutory contingency reserve. The required reserve is reviewed annually and adjusted as appropriate. The utilisation of this reserve, in the event of a catastrophe, is subject to the approval of the Registrar of Short-Term Insurance.

3. Critical accounting estimates and judgements in applying accounting policies

The company makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

a) *The ultimate liability arising from claims made under insurance contracts:*

The estimation of the ultimate liability arising from claims made under insurance contracts is the company's most critical accounting estimate. There are several sources of uncertainty that need to be considered in the estimate of the liability that the company will ultimately pay for such claims. These uncertainties will also have a direct impact on the reinsurance assets:

- Liabilities for unpaid claims are calculated based on an estimated average cost per claim for each underwriting year (see note 2.6). Due to the nature of the claims (injuries and long tail), uncertainty exists regarding the future costs. The impact of HIV / AIDS on claims and benefits is accounted for when calculating the average cost of a claim.
- Liabilities in respect of incurred but not reported claims (IBNR), are based on the average claims cost as detailed above and the estimated, unreported number of claims for the current and previous year only. The unreported claims are calculated based on history and may differ from the actual number of claims reported.
- The capitalised value of pensions ("CVP") liability is the present value of future pension liabilities and administration expenses, net of any investment income that may be earned (see note 2.6). The liability is based on assumptions as to future pension increases, mortality & morbidity, management expenses and investment income, which are reviewed by management on an annual basis for reasonableness, and results in uncertainty regarding the future liabilities:
    - o Future pension increases are assumed to be at the current CPI (Consumer Price Index);
    - o Mortality & morbidity are based on the most recent South African life expectancy tables, including an adjustment in respect of the impact of AIDS / HIV and the level of disablement in respect of employees;
    - o Future management expenses are based on the forthcoming year's budget, and are determined as an average cost per pensioner. Future increases in respect of management expenses are assumed at CPI +1%;
    - o Future investment income is based on the effective interest yield of nominated Government bonds (currently the R157 and inflation-linked bonds, being the R189 and R197) as at the financial year-end.

A sensitivity analysis in respect of a change in the net discount factor and the impact of HIV / AIDS, is presented in note 15.2 (page 43).

b) *The ultimate liability arising in respect of rebates:*

Rebates are provided for in the year in which premium is written (see note 2.6). The rebate provision is based on a percentage of premium income. The percentage used is based on management intention in that financial year, but the ultimate payment of rebates may differ from the original provision. The amount payable is at the discretion of the company.

The percentage used is reviewed annually and adjustments to previous provisions are made as necessary.

c) *Pipeline premium and all related financial liabilities:*

Pipeline premium has been calculated as a percentage of estimated premium (see note 2.6). The percentage used is based on management's judgement, using history and other industry information available, but the ultimate premium received in respect of pipeline premiums may differ from the original provision. All related liabilities, reinsurance, unearned premium liability, rebates and deferred tax, are subject to the same uncertainty.

Differences between the actual premium adjustment and pipeline premium are accounted for in the following financial period, once reported by policyholders. The percentage used is reviewed annually.

Sensitivity analysis

Below is the impact on profit for the year if the 10% currently provided is actually 5% or 15%

	2005 R'000	2004 R'000
The impact on profit after tax at 10% (as provided)	604	890
The impact on profit after tax at 5%	302	445
Variance from 10%	(302)	(445)
The impact on profit after tax at 15%	906	1,335
Variance from 10%	302	445

d) *Impairment of available-for-sale equity financial instruments:*

The company determines that available-for-sale equity financial assets are impaired when there has been a significant or prolonged decline in the fair value below its cost. This determination of what is significant or prolonged requires judgement. In making this judgement the company evaluates, among other factors, the normal volatility in share price, the financial health of the investee, industry and sector performance, changes in technology, and operational and financing cashflow.

Had all the declines in fair values below cost been considered significant or prolonged, the company would have suffered an additional loss of R60 k in its 2005 (2004: R3,9 million) financial statements, being the transfer of the total equity reserve for unrealised losses to the income statement.

4. Management of risk

4.1. Insurance risk

The company issues insurance policies in respect of benefits payable to employees injured on duty, in terms of the COID Act and operates under licence to the Compensation Commissioner. These benefits include, but are not limited to, medical costs, temporary loss of income, permanent disablement, sundry costs and pensions, as defined in the COID Act.

Medical costs include all medical expenditure (e.g. hospitalisation, consultations and medication) incurred as a result of an injury on duty.

Temporary loss of income refers to payments made in respect of the loss of wages as a result of being off work.

Permanent disablement is a lump sum payout to workmen as a result of a defined permanent injury / disability, which is not severe enough to prevent the individual from working again, but rather compensation for the minor injury / disablement.

Sundry costs relate to all other expenditure, as defined in the COID Act, which are incurred as a result of the work injury.

Disability pensions are paid to employees who are disabled as a result of the work-related injury or disease, and are paid until the pensioner dies.

Pensions are paid to the dependant(s) (widows and children) of employees who have died as a result of a work-related injury or disease. The pensions paid to widows are paid until the widow dies, and pensions to children are paid until the child turns 18.

The risk under an insurance contract is the possibility that the insured event occurs and the uncertainty of the amount of the resulting claim. By the very nature of an insurance contract, the risk is random and therefore unpredictable.

Where the theory of probability is applied to pricing and provisioning, the principal risk that the company faces under its insurance contracts is that the actual claims and benefit payments exceed the premiums charged. This could occur because of the frequency or severity of claims and benefits are greater than estimated. Insurance events are random and the actual number of claims and benefits will vary from year to year from the estimates using established statistical techniques.

Factors that aggravate insurance risk include lack of risk diversification in terms of type and amount of risk, geographical location and the type of industry covered.

Workers Compensation Insurance

The company only covers one type of insurance risk, namely workers compensation, for the construction industry (Class V) throughout South Africa. The company has unlimited exposure in respect of claims and benefits, which vary depending on the severity and nature of the accident and injury. The premium rates are determined by the Compensation Commissioner ("CC"), which are reviewed and recalculated on an annual basis. Class V has various "sub-classes" / industry classifications, each with their own rate. To date the rates determined by the CC have been adequate to cover the cost of claims and pensions awarded by the company.

Risks

The most significant risk to the company at present is the lack of skills in the construction industry, coupled with the high level of construction activity within South Africa, exposing the company to an increase in the number of accidents, and therefore injuries, on duty.

In respect of costs incurred in the rehabilitation of the injured worker, the company is also exposed to the effect of HIV / AIDS in respect of recovery periods – the longer the period of recovery the higher the costs incurred, or, due to the inability to recover fully, a pension may be awarded; this risk may be alleviated by the introduction of antiretroviral drugs & AIDS / HIV awareness campaigns.

The risk of fraudulent claims and or pensions is mitigated by good systems of internal controls and segregation of duties within the claims departments. All claims reported and registered are matched / linked to in-force policies and good communication with the policyholders (employers of injured employees) exists. A pension can only be created if a claim has been registered, and thereafter we are exposed to fraud in respect of:

- *Identity fraud* e.g. a pensioner dies (and the family does not inform FEM) and an individual obtains a false identity document ("ID") and presents themselves as this pensioner. This risk is reduced by comparing ID documents on file to the fictitious pensioner's ID.
- *Unreported deaths* e.g. an individual dies and the family does not inform FEM and therefore FEM continues paying the monthly pension. This risk exists for a maximum period of 12 months as annual life certificate

confirmations are requested, together with a copy of the individual's ID. If the necessary documentation is not received by 30 June each year, the pension is suspended.

The company is bound by the rates and benefits of the Compensation Commissioner, in conjunction with the provisions of the COID Act. The risk of rates and benefits being mismatched is low and the company has a good working relationship with the Compensation Office.

Management of risks

Rates are reviewed annually based on costs incurred and accidents registered relative to the premium income generated.

FEM is on a drive to promote health and safety in the construction industry and, where required, assists policyholders to improve their safety via site visits, training, sponsorships etc. FEM also recognises excellent safety records via its rebate programme (see note 2.6) and in 2005 recognition of extraordinary safety records was given (see note 15.4 and special rebates report on page 2).

Sources of uncertainty in the estimation of future claim payments

Claims are payable on a claims-occurrence basis and therefore the company is liable for all insured events that occurred during the period of insurance, even if the loss is only discovered after the end of the contract term. Accidents are generally reported within the year incurred (87%), and by the end of the following year, 99% of accidents have been reported. Claims payments however, take longer with between only 50% and 60% of costs being paid in the year of the accident, and up to 90% being paid by the end of the following year. As a result, the estimation of outstanding costs is based on the best available information and knowledge at each year-end. Given the uncertainty as a result of the factors above, it is likely that the final outcome will be different from the original liabilities (outstanding estimates and IBNR) raised. The pensions liability is also exposed to assumptions made at the end of each year. A sensitivity analysis of these assumptions is provided in the pension liability note (Note 15.2). (See note 3 regarding areas of judgement).

Claims and benefits

Claims and benefits, including the number of accidents per region, are tabled below.

	Claims costs	*Pensions awarded*	*Accidents registered*
	R'000	R'000	
2005			
Johannesburg	27,750	10,221	3,167
Cape Town	17,653	4,113	3,299
Durban	6,692	2,609	1,278
Pretoria	11,323	588	976
Total	**63,418**	**17,531**	**8,720**
2004			
Johannesburg	22,647	12,980	3,175
Cape Town	17,744	4,730	2,965
Durban	6,151	4,734	1,205
Pretoria	4,856	6,114	751
Total	**51,398**	**28,558**	**8,096**

4.2. Financial risk

The company is exposed to financial risk through its financial assets, financial liabilities, reinsurance assets and insurance liabilities. The key financial risk is that the proceeds from its financial assets are not sufficient to cover the obligations arising from its insurance contracts. The main components are interest rate risk, equity price risk and credit risk.

4.2.1. Interest-rate risk

The company holds just over 50% of its available-for-sale financial assets in debt securities (Government Bonds and Public Utility Bonds) and substantial investments in cash & cash equivalents and money market unit trusts. The return on these instruments, and the market value of debt securities are affected by fluctuations in interest rates.

Excluding the movement in the pensions liability and rebates provision, which is discretionary, the company currently covers all insurance claims and benefits from operational cash, and therefore is not dependent on investment income to sustain the insurance operations.

The pensions liability is actuarially valued on an annual basis, which is impacted by the future anticipated interest return – see note 15.2.

4.2.2. Credit risk

The company has exposure to credit risk, which is the risk that a counterparty will be unable to pay amounts in full when due. Key areas of exposure are:

- reinsurers' share of insurance liabilities,
- amounts due from reinsurers' in respect of claims payments already made, and
- amounts due from policyholders.

Reinsurers

The credit worthiness of reinsurers is considered on an annual basis by reviewing their financial strength before finalising any contract. The company's reinsurance liabilities are covered by four diverse reinsurers.

Policyholders

The premium written is distributed nationally, among varying employers' classified as Class V in terms of the Compensation Commissioner's industrial classification table.

4.2.3. Liquidity risk

The company is exposed to daily calls on its available cash resources, mainly from short term claims. Liquidity risk is the risk that cash resources are not available to pay claims when due. The company ensures that adequate levels of cash are available immediately without incurring penalties.

4.2.4. Equity price risk

This is the risk that the company will not realise the value of its equity securities, which may impact the company's ability to meet liabilities. In terms of the company's licence from the Compensation Commissioner, a minimum value of investments, to cover all insurance liabilities, must be invested in low-risk / no-risk instruments, and therefore all equity securities are considered "excess" assets.

5. Change in accounting policies – Prior year adjustments

a) Providing for pipeline premiums and all related expenses and liabilities

During 2005 the company changed its accounting policy in respect of the recognition of premium income. In previous periods, premium income reported in the income statement was the total of the current year estimated premium reported by policyholders and any differences between booked premiums for prior years and those previously recognised i.e. adjustments to prior year estimated premium.

FEM has now decided to account for each financial period's future "adjustment to estimates" in the current financial period i.e. the year in which the risk incepts. Management considers that the new policy is preferable as it ensures the full premium attributable to a financial period is accounted for in that period, and is matched to the claims incurred. The following liabilities and related expenses, and equity reserves have been impacted by the change in accounting policy:

- Reinsurance premium due and ceded;
- Unearned premium liability and the related income statement movement;
- Non-current rebates provision and expense in the income statement;
- Deferred tax liability and tax charge; and
- Contingency reserve to be held in terms of the Short-term Insurance Act, 1998.

The change in accounting policy has been applied retrospectively, and the comparative figures for 2004 have been restated. The effect of the changes in the above-mentioned balances in respect of 2004 and prior years is summarised on page 32.

Balance sheet	2004 as previously reported	2003 & prior years' adjustment	2004 prior year's adjustment	**2004 Restated**
Assets				
Pipeline premiums	-	9,601	2,372	**11,973**
Equity				
Retained income	284,155	2,741	1,538	**288,434**
Contingency reserve	12,730	861	(648)	**12,943**
Liabilities				
Non-current rebates provision	24,898	1,920	474	**27,292**
Deferred tax liability	10,593	1,544	382	**12,519**
Deferred tax – temporary differences	(17,625)	1,544	382	**(15,699)**
Deferred tax – asset revaluation	28,218	-	-	**28,218**
Unearned premium provision	20,245	1,552	383	**22,180**
Reinsurance premium liability	2,571	983	243	**3,797**

Income statement	2003 and prior years' impact	2004 as previously reported	2004 change in policy adjustment	**2004 Restated**
Premium income	9,601	143,019	2,372	**145,391**
Movement in unearned premium provision	(1,552)	(3,595)	(383)	**(3,978)**
Net premium revenue	8,049	139,424	1,989	**141,413**
Reinsurance ceded	(983)	(15,721)	(243)	**(15,964)**
Provision for rebates	(1,920)	(27,856)	(474)	**(28,330)**
Tax	(1,544)	6,453	(382)	**6,071**
Net profit after tax	**3,602**	**10,761**	**890**	**11,651**
Transfer to contingency reserve	(861)	(2,420)	648	**(1,772)**
Transfer to retained income	**2,741**	**8,341**	**1,538**	**9,879**

b. IAS39 (AC133) – Financial Instruments: Recognition and Measurement – Treatment of effective interest on available-for-sale debt securities

The effective interest method is a method of calculating the amortised cost of a financial asset and of allocating the interest income over the relevant period. The effective interest rate is the rate that discounts estimated future cash receipts through the expected life of the financial asset. The calculation includes all fees, transaction costs and premiums or discounts on the instrument.

Historically FEM recognised the difference between coupon and effective interest earned i.e. coupon interest plus amortisation of premium / discount on debt securities (bonds), directly to equity through the fair value adjustment, in terms of IAS39 (AC133), which was silent in this regard. Effective 01 January 2005, IAS39 (AC133) (revised) explicitly states that effective interest must be recognised through the income statement. FEM has therefore changed the accounting policy to be in line with the revised statement, and the prior year financial results have been restated to account for this. The new method of accounting for effective interest is the same basis on which the company reported interest and profit for tax purposes, and therefore, the change only impacts deferred tax and not the tax due to South African Revenue Services.

The following assets, liabilities and income statement items have been impacted by the change in accounting policy:

- Net deferred tax liability;
- Asset revaluation;
- Interest received on debt securities;
- Net gains / losses on realisation of debt securities; and
- Deferred tax charge.

The change in accounting policy has been applied retrospectively, and the comparative statements for 2004 have been restated. The impact and effect of the changes in the abovementioned balances in respect of 2004 and prior years is summarised below:

Balance sheet	2004 AFS*/ adjusted in Note 5a	2003 & prior years' adjustment	2004 prior year's adjustment	**2004 Restated**
Equity				
Retained income – restated 5a	288,434	1,108	310	**289,852**
Asset revaluation	77,713	(1,064)	(1,385)	**75,264**
Revaluation	105,931	(1,209)	(1,630)	**103,092**
Deferred tax	(28,218)	145	245	**(27,828)**
Liabilities				
Deferred tax liability – restated 5a	12,519	(44)	1,075	**13,550**
Deferred tax – temporary differences	(15,699)	101	1,320	**(14,278)**
Deferred tax – asset revaluation	28,218	(145)	(245)	**27,828**

*AFS - Annual Financial Statements

Income statement	2003 and prior years' impact	2004 as previously reported	2004 change in policy adjustment	**2004 Restated**
Interest earned on bonds		37,942	988	**38,930**
Net gains / losses on realisation of financial assets		36,085	642	**36,727**
Tax – restated 5a		6,071	(1,320)	**4,751**
Impact on net profit after tax	1,108		310	
PYA 5a – above	2,741		1,538	
Total impact of prior year adjustments on retained income	3,849		1,848	

c) *Reclassification of money market unit trusts as short term investments and investment bank settlement accounts as Cash & cash equivalents*

In 2005 management revised its accounting policy with regard to the treatment of "money market instruments", with specific reference to its investments in money market unit trusts and investment bank accounts. These balances were previously included in non-current assets, and have now been classified as current assets under "Short term investments" (money market unit trusts) and "Cash & cash equivalents" (investment bank accounts).

Management considers the new policy to be preferable as these money market instruments are current, rather than non-current in nature, and results in better presentation of the underlying instruments. The only impact on the annual financial statements is reclassification on the balance sheet as shown below:

Balance sheet	2004 AFS*	Reclassification	**2004 Restated**
Non-current assets			
Available-for-sale financial assets (2004: Investments at market value)	790,866	(132,974)	**657,892**
Current assets			
Short term investments	-	104,120	**104,120**
Cash & cash equivalents	29,756	28,854	**58,610**

*AFS - Annual Financial Statements

	Furniture & fittings R'000	Office equipment R'000	Computer equipment R'000	Motor vehicles R'000	Total R'000
6. FURNITURE, EQUIPMENT AND MOTOR VEHICLES					
Year ended 31 December 2004					
Opening cost	1,052	229	1,360	3,808	6,449
Opening accumulated depreciation	(417)	(123)	(827)	(1,381)	(2,748)
Opening net book amount	635	106	533	2,427	3,701
Additions	165	8	42	177	392
Disposals	-	-	(3)	(227)	(230)
Depreciation charge	(178)	(37)	(373)	(723)	(1,311)
Closing net book amount	622	77	199	1,654	2,552
At 31 December 2004					
Cost	1,217	237	1,363	3,488	6,305
Accumulated depreciation	(595)	(160)	(1,164)	(1,834)	(3,753)
Net book amount	622	77	199	1,654	2,552
Year ended 31 December 2005					
Opening net book amount	**622**	**77**	**199**	**1,654**	**2,552**
Additions	**89**	**136**	**654**	**1,090**	**1,969**
Disposals	**(14)**	**-**	**(4)**	**(128)**	**(146)**
Depreciation charge	**(186)**	**(47)**	**(216)**	**(779)**	**(1,226)**
Closing net book amount	**511**	**166**	**633**	**1,839**	**3,149**
At 31 December 2005					
Cost	**1,221**	**343**	**1,739**	**4,166**	**7,469**
Accumulated depreciation	**(710)**	**(177)**	**(1,106)**	**(2,327)**	**(4,320)**
Net book amount	**511**	**166**	**633**	**1,839**	**3,149**

Depreciation expenses of R1,23 million (2004: R1,31 million) have been charged to administration expenses (Note 22).

	2005 R'000	2004 R'000
7. AVAILABLE-FOR-SALE FINANCIAL ASSETS		
Available-for-sale financial assets		
Equity securities		
- listed	**389,379**	291,462
Debt securities		
- listed: fixed interest rate	**417,987**	299,198
- listed: floating interest rate	**84,730**	67,232
Total	**892,096**	657,892
Available-for-sale financial assets		
At the beginning of year	**666,844**	615,452
Additions	**453,495**	312,298
Disposals	**(335,090)**	(359,625)
Fair value net gains	**117,803**	98,719
At end of year	**903,052**	666,844
Market value	**892,096**	657,892
Accrued income	**10,956**	8,952
	903,052	666,844

A requirement of the company's licence is to hold assets which comply with the requirements of Regulation 34 of the regulations made under section 76 of the Insurance Act 1943, (as amended and substituted from time to time), regulating the composition of the assets to be held in respect of insurance business, to cover specified insurance liabilities of the company's minimum required assets. This minimum requirement is R579,2 million (2004: R464,03 million) and qualifying assets totalled R860,5 million (2004: R688,40 million).

	2005 R'000	2004 R'000
8. REINSURANCE ASSETS		
Reinsurers' share of insurance liabilities	**8,303**	5,938

Amounts due from reinsurers in respect of claims already paid by the company are included in other receivables.

	2005 R'000	2004 R'000
9. INSURANCE ASSETS		
Pipeline premium provision	**14,583**	11,973
Due from policyholders	**2,793**	3,740
Less provision for impairment of amounts due from policyholders	**(1,093)**	(1,042)
	16,283	14,671

There is little concentration of credit risk with respect to the amounts due from policyholders, as the company has a number of nationally dispersed debtors.

The company has recognised a loss of R540k (2004: R623k) for the impairment of amounts due from policyholders, which has been set off against estimated premium income (Note 18).

	2005 R'000	2004 R'000
10. OTHER RECEIVABLES		
Accrued investment income - financial assets	**12,206**	11,835
Accrued investment income - SARS	**818**	275
Reinsurance receivables	**1,414**	845
Prepayments	**132**	117
Other	**183**	149
	14,753	13,221

There is no concentration of credit risk with respect to the other receivables, as the amounts due are from various sources (Government, private sector, four reinsurers).

11. SHORT TERM INVESTMENTS		
Money market unit trusts	**67,704**	104,120

Money market unit trusts were previously disclosed as "Investments", but have been classified as current assets as short term investments (see note 5c).

The effective interest rate received on money market unit trusts was 7.23% (2004: 8.03%).

12. SHARE CAPITAL		
Authorised and issued		
500,000 ordinary shares of 2 cents each	**10**	10

There has been no movement in the authorised and issued share capital of the company for the year.

13. OTHER RESERVES		
Total other reserves	**124,756**	125,564
Total other reserves comprise the following balances (Notes 13.1 - 13.4)		
13.1 Statutory contingency reserve		
Opening balance (restated)	**12,943**	11,171
Movement	**3,810**	1,772
Closing balance	**16,753**	12,943

In terms of the reserving requirements of the Short-term Insurance Act of 1998, FEM is required to hold 10% of gross premiums received less approved reinsurance as a statutory contingency reserve.

13.2 Special pensions reserve		
Opening balance	**17,357**	57,814
Movement	**(17,357)**	(40,457)
Closing balance	**-**	17,357

This reserve was available for any future special increases which the Compensation Commissioner may have awarded to pensioners. These increases were granted in 2005 (See note 15.2 page 43 "Experience adjustments"), and the balance of the reserve has been released back to retained income in the current year.

	2005 R'000	2004 R'000
13. OTHER RESERVES (continued)		
13.3 AIDS / claims / rehabilitation reserve		
Opening balance	**20,000**	20,000
Movement	**(20,000)**	-
Closing balance	**-**	20,000

This reserve was raised to account for the uncertain, potential impact of AIDS on claims costs and / or the pensions liability (CVP). No obvious impact has been identified and therefore the reserve has been released back to retained income in the current year.

	2005 R'000	2004 R'000
13.4 Asset revaluation reserve		
Opening balance - revaluation	**103,092**	39,912
Movement	**43,153**	63,180
Closing balance - revaluation	**146,245**	103,092
Opening balance - deferred tax on revaluation	**(27,828)**	(4,148)
Movement	**(11,376)**	(23,680)
Movement - change in rate	**962**	-
Closing balance - deferred tax on revaluation	**(38,242)**	(27,828)
Opening balance - net	**75,264**	35,764
Movement	**32,739**	39,500
Closing balance - net	**108,003**	75,264

The asset revaluation reserve takes account of the market value movements in available-for-sale financial assets, net of the impact of tax.

	2005 R'000	2004 R'000
14. TAX		
14.1 Deferred tax		
The deferred tax assets and liabilities are attributable to the following items:		
Deferred income tax assets:		
- Provisions	**14,117**	9,365
- Limitation of technical reserves	**-**	6,840
- Sundry	**-**	33
	14,117	16,238
Deferred income tax liabilities:		
- Asset revaluation	**(38,242)**	(27,828)
- Pipeline premium provisions	**(2,082)**	(1,925)
- Sundry	**-**	(35)
	(40,324)	(29,788)
Total	**(26,207)**	(13,550)

Deferred income taxes are calculated on all temporary differences under the liability method using the statutory tax rate of 29% (2004: 30%).

	Notes	2005 R'000	2004 R'000
14.1 Deferred tax (continued)			
The movement on the deferred income tax liability account is as follows:			
At beginning of year		**(13,550)**	5,564
Income statement (charge) / release	14.2	**(2,243)**	4,566
Asset revaluation	13.4	**(10,414)**	(23,680)
At end of year		**(26,207)**	(13,550)
14.2 Normal and deferred tax			
South African normal tax at 29% (2004: 30%)			
Current tax			
- current year		**7,259**	-
- prior years under / (over) provision		**2,359**	(185)
		9,618	(185)
Deferred tax			
- current year		**1,474**	(3,476)
- change in rate		**476**	-
- prior years under / (over) provision		**293**	(1,090)
		2,243	(4,566)
Total tax charge / (credit)		**11,861**	(4,751)

The company's profit before tax differs from the theoretical amount that would arise using the basic tax rate of South Africa as follows:

	2005 R'000	2004 R'000
Profit before tax	**43,287**	7,210
Tax calculated at 29% (2004: 30%)	**12,553**	2,163
Income not subject to tax	**(4,519)**	(6,131)
Prior years under / (over) provision - deferred tax	**293**	(1,090)
Capital gains tax	**563**	700
Prior years under / (over) provision - current tax	**2,359**	(185)
Other	**-**	(374)
Expenses not deductible for tax purposes	**136**	166
Change in rate	**476**	-
Tax charge / (credit)	**11,861**	(4,751)
Effective rate of tax	**27%**	-

	Notes	2005 R'000	2004 R'000
15. INSURANCE LIABILITIES AND REINSURANCE ASSETS			
Gross			
Outstanding claims	15.1	**104,331**	74,506
Capitalised value of pensions	15.2	**311,001**	273,222
Provision for unearned premiums	15.3	**28,439**	22,180
Provision for rebates - non-current	15.4	**43,511**	27,292
Provision for rebates - current	15.4	**35,637**	23,424
Total insurance liabilities - gross		**522,919**	420,624
Recoverable from reinsurers			
Outstanding claims recoveries	8	**8,303**	5,938
Total reinsurer's share of insurance liabilities		**8,303**	5,938
Net			
Outstanding claims		**96,028**	68,568
Capitalised value of pensions		**311,001**	273,222
Provision for unearned premiums		**28,439**	22,180
Provision for rebates - non-current		**43,511**	27,292
Provision for rebates - current		**35,637**	23,424
Total insurance liabilities - net		**514,616**	414,686
15.1 Outstanding and unintimated claims			
Outstanding claims - reported claims		**89,555**	63,754
Incurred but not reported ("IBNR")		**14,776**	10,752
		104,331	74,506

The risks associated with the number of accidents registered and the future claims to be paid are difficult to predict and the liability therefore contains an element of uncertainty. The outstanding claims estimate is based on the average cost of a claim for each underwriting year, less claims paid and pension awards made to date. The average cost per claim is recalculated at each year end to ensure that the estimate is updated and correctly reflects the future anticipated costs. The IBNR liability is based on historical trends which best reflect the future claims to be registered in respect of past underwriting periods.

Movement in outstanding claims and IBNR

2005	**Notes**	**Gross**	**Reinsurance**	**Net**
Claims and benefits				
Notified claims		63,754	(5,938)	57,816
Incurred but not reported		10,752	-	10,752
Total at beginning of year		74,506	(5,938)	68,568
Cash paid for settled claims	21	(63,418)	4,423	(58,995)
Pensions awarded		(17,532)	-	(17,532)
Increase in liabilities		110,775	(6,788)	103,987
- arising from current year claims		101,486	(3,422)	98,064
- arising from prior year claims		9,289	(3,366)	5,923
Total at end of year		**104,331**	**(8,303)**	**96,028**
Notified claims		89,555	(8,303)	81,252
Incurred but not reported		14,776	-	14,776
Total at end of year		**104,331**	**(8,303)**	**96,028**
Movement for the year	21	**29,825**	**(2,365)**	**27,460**

Movement in outstanding claims and IBNR (continued)

2004	**Notes**	**Gross**	**Reinsurance**	**Net**
Claims and benefits				
Notified claims		59,569	(7,594)	51,975
Incurred but not reported		9,461	-	9,461
Total at beginning of year		69,030	(7,594)	61,436
Cash paid for settled claims	21	(51,398)	10,497	(40,901)
Pensions awarded		(28,558)	-	(28,558)
Increase in liabilities		85,432	(8,841)	76,591
- arising from current year claims		76,181	(1,355)	74,826
- arising from prior year claims		9,251	(7,486)	1,765
Total at end of year		**74,506**	**(5,938)**	**68,568**
Notified claims		63,754	(5,938)	57,816
Incurred but not reported		10,752	-	10,752
Total at end of year		**74,506**	**(5,938)**	**68,568**
Movement for the year	21	**5,476**	**1,656**	**7,132**

Claims development (Outstanding claims, accidents registered and average claims costs)

The development of gross outstanding claims for the last five years is shown below:

Accident / underwriting year	*2001*	*2002*	*2003*	*2004*	*2005*
Estimate of ultimate claims costs (including IBNR)					
- at end of underwriting year	53,311	58,700	68,365	76,838	102,486
- one year later	52,464	55,856	76,927	78,102	-
- two years later	54,284	55,112	78,196	-	-
- three years later	54,732	56,056	-	-	-
- four years later	58,702	-	-	-	-
Current estimate of cumulative claims	58,702	56,056	78,196	78,102	102,486
Cumulative payments & pension awards to date	(53,515)	(51,463)	(66,540)	(60,343)	(37,350)
Liability recognised in balance sheet	5,187	4,593	11,656	17,759	65,136
Total liability recognised in the balance sheet					**104,331**

The development of accidents registered for the last five years is shown below:

Accident / underwriting year	*2001*	*2002*	*2003*	*2004*	*2005*
- at end of underwriting year	5,711	5,939	6,472	7,186	7,745
- one year later	6,457	6,814	7,296	8,077	-
- two years later	6,498	6,867	7,352	-	-
- three years later	6,513	6,882	-	-	-
- four years later	6,520	-	-	-	-

The development of average cost of claims for the last five years is shown below:

Accident / underwriting year	*2001*	*2002*	*2003*	*2004*	*2005*
	R's	R's	R's	R's	R's
- at end of underwriting year	7,920	8,400	9,000	9,125	11,400
- one year later	7,920	8,000	10,340	9,350	-
- two years later	8,200	7,880	10,500	-	-
- three years later	8,250	8,000	-	-	-
- four years later	8,850	-	-	-	-

(including costs of claims registered before 2001)

	Notes	2005 R'000	2004 R'000
15.2 Capitalised value of pensions			
Opening balance		**273,222**	204,556
Transfer from income statement	21	**37,779**	68,666
Closing balance		**311,001**	273,222

Independent actuarial valuations of the capitalised value of pensions liability were carried out every three years and from 2004, will be carried out annually.

The principal actuarial assumptions utilised in the calculation of the liability are as follows:

	2005	2004
Pensions liability assumptions		
Investment return	**7.5%**	8.0%
Annual pensions increases	**4.5%**	4.0%
Real discount rate	**3.0%**	4.0%
Expense assumptions		
Administration cost per pensioner	**R 1,025**	R 950
Investment return	**7.5%**	8.0%
Inflation	**5.5%**	5.0%
Real discount rate	**2.0%**	3.0%

Assumptions used

Mortality & morbidity

As with 2004, the non-AIDS mortality assumptions are based on the SA8590 Heavy standard table, with adjustments based on duration and severity of disablement.

Economic assumptions

The discount factors in respect of investment income, future pension increases and management expense inflation have all been revised in line with the change in the economic environment, and are explained individually below:

Investment income:

Investment income returns have been reduced from 8% in 2004 to 7.5% in 2005, with reference to the yields at valuation date on the South African Government R189 and R197 CPI bonds and the R157 bond.

Pension increases:

Future pension increases granted by the Compensation Commissioner are expected to be in line with CPI, and the company has therefore assumed an increase of 4.5%, being the midpoint of the Reserve Bank's target inflation.

Expense increases:

Expense inflation for 2006 onwards is assumed to be 5.5% per annum, which maintains the 1% margin above the general inflation assumption.

	2005 R'000	2004 R'000

Impact of HIV / AIDS

The actuaries have explicitly modelled HIV infection and AIDS mortality using their internal HIV & AIDS demographic and financial model, qAIDS. The rates of new HIV infection on which modelling is based are drawn from models provided by the Actuarial Society of South Africa ("ASSA"), which recently updated its estimates with the release of ASSA2003, replacing ASSA2002.

The HIV & AIDS risk of FEM pensioners has been based on 70% of the South African national rates of HIV infection by age and sex from the ASSA 2003 AIDS & Demographic model, with some allowance for access to antiretroviral therapy.

Experience adjustments in respect of external valuation

	2005 R'000	2004 R'000
Opening balance	**273,222**	204,556
Increase in CVP before special increases (new membership, cancellations, new valuation date, normal pension increases)	**11,573**	39,147
Special increases to be awarded	**-**	9,799
Increase due to discount rate reduction of 1% (2004: 0.5%)	**25,727**	12,704
Increase in expense reserve	**3,980**	8,818
Adjustment for HIV & AIDS table ASSA2003 (2004: ASSA2002)	**(3,501)**	(15,565)
Adjustment in respect of mortality basis	**-**	13,763
Closing balance	**311,001**	273,222

Experience adjustments in respect of the last independent external actuarial valuation (Performed as at 31 December 2005, 2004 and 2001)

	2005 R'000	2004 R'000
Opening balance (Valuation 2004 & 2001)	**273,222**	170,375
Change the AIDS basis to ASSA2003 (2004: ASSA2002) and qAIDS model	**269,721**	173,857
Increase in CVP before special increases (new membership, cancellations, new valuation date, normal pension increases)	**285,274**	256,155
Apply special additional increases to pensions payment	**-**	256,910
Change the mortality basis	**-**	259,213
Change the discount rate and economic assumptions	**311,001**	273,222
Closing balance (Valuation 2005 & 2004)	**311,001**	273,222

Sensitivity analysis

There are two critical assumptions made in the valuation of the pensions liability, namely the net discount factor and the impact of HIV / AIDS. A sensitivity analysis of this is summarised below:

Net discount factor

A 0.5% increase or decrease in the net discount factor would impact the pension liability as follows:

	R'000	%
Current liability	**311,001**	
0.5% increase in net discount rate	**295,451**	
Impact on the liability	**(15,550)**	*-5.0%*
0.5% decrease in net discount rate	**328,140**	
Impact on the liability	**17,139**	*5.5%*

	2005 R'000	2004 R'000

15.2 Capitalised value of pensions (continued)

Impact of HIV / AIDS

The liability with greater or lower AIDS risk (incidence and access to antiretroviral treatment ("ART") would impact the pension liability as follows:

	R'000	%
Current liability	311,001	
Higher incidence (100% of ASSA2003 incidence & 25% access to ART)	304,015	
Impact on the liability	(6,986)	-2.2%
Lower incidence (50% of ASSA2003 incidence & 75% access to ART)	322,201	
Impact on the liability	11,200	3.6%

Liquidity

Claims and benefits are currently funded by operational cash i.e. premium receipts plus investment income, less expenses paid. The company is not exposed to a high level of liquidity risk as it very rarely pays lump sum benefits to individuals (Commutations need to be approved by the Compensation Commissioner), and only incurs monthly pension payments and normal short-term claims. The cash & cash equivalents and short term investments are adequate to cover all short-term claims at year end.

All insurance liabilities (Note 15), excluding the rebates provision, and the contingency reserve, are covered by bonds (see note 7). Every 6-12 months the duration and future cashflows of the bonds are compared to the duration and future cashflows of the existing pensioners. The last comparison was performed in December 2005 as part of the year-end valuation and, prior to that, in August 2005. No material mis-matches were highlighted.

15.3 Unearned premium provision

	2005 R'000	2004 R'000
At beginning of year	22,180	16,650
Prior year adjustment	-	1,552
Opening balance restated	22,180	18,202
Movement during the period (see note 18 Premium income)	6,259	3,978
- Increase in the period	28,439	22,180
- Release during the period	(22,180)	(18,202)
Total at end of year	**28,439**	22,180

As the reinsurance contract runs from 01 January to 31 December, there is no unearned premium asset in respect of reinsurance.

15.4 Provision for rebates

	2005 R'000	2004 R'000
Opening balance - non-current	27,292	24,577
Transfer to current	(27,292)	(24,577)
Charge to income statement	43,511	27,292
Closing balance - non-current	**43,511**	27,292
Opening balance - current	23,424	16,759
Charge to income statement	5,451	2,191
Utilised during the year	(28,875)	(18,950)
Transfer from non-current	27,292	24,577
Charge to income statement 25% (2004: 20%)	8,345	(1,153)
Closing balance - current	**35,637**	23,424

	Notes	2005 R'000	2004 R'000
15.4 Provision for rebates (continued)			
Charge to income statement		**57,307**	28,330
Special rebates paid		**9,216**	-
Total income statement charge for rebates paid & provided		**66,523**	28,330
15.5 Reinsurance liabilities			
Minimum deposit premium		**3,481**	2,571
Pipeline premium		**1,403**	1,226
Reinsurance premiums liability		**4,884**	3,797
16. ACCOUNTS PAYABLE			
Investec Asset Managers (Asset management fee)		**312**	5,286
Staff incentives		**2,019**	2,083
Accident fund administration		**1,774**	1,415
SARS (PAYE)		**289**	4,957
Outstanding cheques		**640**	1,031
Outstanding trade settlements		**-**	22
Other		**1,033**	813
		6,067	15,607
17. PROVISIONS			
Provision for leave pay and post retirement medical aid ("PRMA")			
Opening balance		**854**	1,990
PRMA utilised during the year (Note 28 - CE Saville)		**-**	(1,131)
Leave pay utilised during the year		**(148)**	(262)
Charge to income statement - leave pay		**212**	257
Closing balance		**918**	854
18. NET PREMIUM REVENUE			
Premium income	2.6	**180,026**	145,391
Estimated premium, net of allowances and write offs		**158,873**	125,405
Pipeline premium - current year		**14,583**	11,973
Adjustment to estimates - prior year		**6,570**	8,013
Movement in unearned premium provision	2.6	**(6,259)**	(3,978)
Estimated premium		**(5,837)**	(3,595)
Pipeline premium		**(422)**	(383)
Premium revenue		**173,767**	141,413
Estimated premium ceded		**(18,520)**	(15,721)
Pipeline premium ceded		**(177)**	(243)
Premium income ceded	2.6	**(18,697)**	(15,964)
Net premium revenue		**155,070**	125,449

The reinsurance cover for 2005 and 2004 was purchased with an inception date of 1 January, and there is therefore no unearned reinsurance asset at year-end.

	Notes	2005 R'000	2004 R'000
19. INVESTMENT INCOME			
Available-for-sale financial assets			
- interest income		**37,157**	38,930
- dividend income		**11,805**	8,457
Short term investment & Cash and cash equivalents			
- money market unit trusts		**4,918**	6,224
- investment bank account		**1,794**	1,258
- operational bank account		**645**	993
Sundry income		**545**	275
Investment income		**56,864**	56,137
20. NET REALISED GAINS ON FINANCIAL ASSETS			
Realised gains on financial assets			
- equity securities		**77,757**	37,861
- debt securities		**3,883**	6,927
Realised losses on financial assets			
- equity securities		**(1,750)**	(8,046)
- sundry		**-**	(15)
Net realised gains on financial assets		**79,890**	36,727
21. INSURANCE CLAIMS & BENEFITS			
Gross claims		**93,243**	56,874
Claims paid	15.1	**63,418**	51,398
Movement in claims liabilities	15.1	**29,825**	5,476
Gross pensions		**60,986**	90,658
Pensions paid		**23,207**	21,992
Movement in pensions liability	15.2	**37,779**	68,666
Reinsurance		**(7,357)**	(6,474)
Claims paid recovered from reinsurers	15.1	**(4,423)**	(10,497)
Movement in reinsurance assets	15.1	**(2,365)**	1,656
Movement in reinsurance receivables		**(569)**	2,367
Net claims and benefits		**146,872**	141,058

2005	**Gross R'000**	**Reinsurance R'000**	**Net R'000**
Current year claims paid	33,689	-	33,689
Prior year claims paid	29,729	(4,423)	25,306
Total	63,418	(4,423)	58,995
Current year pensions awarded	3,661	-	3,661
Prior year pensions awarded	13,870	-	13,870
Total	17,531	-	17,531

21. INSURANCE CLAIMS & BENEFITS (continued)

2004	Gross R'000	Reinsurance R'000	Net R'000
Current year claims paid	26,383	-	26,383
Prior year claims paid	25,015	(10,497)	14,518
Total	51,398	(10,497)	40,901
Current year pensions awarded	5,645	-	5,645
Prior year pensions awarded	22,913	-	22,913
Total	28,558	-	28,558

22. ADMINISTRATION EXPENSES	**Notes**	**2005 R'000**	2004 R'000
Depreciation	6	**1,226**	1,311
Staff costs	22.1	**16,564**	16,073
Post retirement medical aid	22.2	**-**	1,384
Directors' fees	28	**1,947**	1,905
Auditors' remuneration	22.3	**556**	418
Operating lease rentals		**2,395**	2,192
(Profit) / Loss on furniture, equipment and motor vehicle disposals		**(14)**	214
Refund in respect of financial services levy		**(2,746)**	-
Other expenses		**6,023**	5,737
		25,951	29,234

22.1 Staff costs

Basic salaries	**11,779**	11,225
Pensions	**1,080**	908
Medical aid	**908**	991
Training & recruitment	**156**	299
Motor vehicles	**904**	757
Incentives	**1,653**	1,816
Temporary staff	**84**	77
	16,564	16,073
Average number of employees	**75**	74

22.2 Commutation of post-retirement medical aid

Charged to income	**-**	1,384
Utilised from provision	**-**	8,656
	-	10,040

22.3 Auditors' remuneration

Audit fees (current year)	**492**	395
Audit fees (prior year)	**31**	23
Other services	**33**	-
	556	418

	2005 R'000	2004 R'000
23. NOTES TO THE CASH FLOW STATEMENT		
23.1 Cash (used in) / generated from operations		
Profit for the year	**31,426**	11,961
Adjustments for		
- tax expense (Note 14.2)	**11,861**	(4,751)
- depreciation (Note 6)	**1,226**	1,311
- profit on disposal of furniture, equipment and motor vehicles (Note 22)	**(14)**	214
- profit on disposal of financial assets: equities	**(73,764)**	(29,816)
- movement in revaluation of available-for-sale financial assets: bonds	**7,851**	3,501
Impairment losses		
- insurance assets (Note 9)	**51**	(1,545)
Changes in operating assets and liabilities		
Net increase / (decrease) in insurance liabilities	**103,382**	87,819
Net (increase) / decrease in reinsurance assets	**(2,365)**	1,656
Net (increase) / decrease in insurance assets	**(1,663)**	(3,525)
Net (increase) / decrease in loans & receivables	**(1,557)**	2,408
Net (increase) / decrease in debt securities	**(136,287)**	27,482
Net decrease / (increase) in short term investments	**36,416**	(60,988)
Net (decrease) / increase in other payables	**(9,574)**	7,665
Net increase / (decrease) in provisions	**64**	(11,045)
	(32,947)	32,347
23.2 Tax paid		
Opening balance	**12,888**	4,436
Income statement charge	**(11,861)**	4,751
Deferred tax	**2,243**	(4,566)
Closing balance	**(11,451)**	(12,888)
Tax paid	**(8,181)**	(8,267)

24. RETIREMENT BENEFITS

Pension fund

The retirement benefit fund, Amalgam Investment Choice Pension Fund, is a defined contribution fund administered by Liberty Corporate Benefits and is governed by the Pensions Fund Act of 1956. The fund covers all qualifying employees.

Post-retirement medical aid benefits

In 2003 the company provided for post-retirement medical aid benefits to qualifying employees, based on an independent actuarial valuation performed at 31 December 2003. In 2004 this liability was bought out by the company by paying all qualifying employees their entitlement, thereby revoking all rights to post retirement medical aid benefits.

	2005	2004
Opening balance	**-**	11,040
Utilised during the year	**-**	(12,643)
Charge to income statement (Notes 22.2 & 28)	**-**	1,603
Present value of total obligation	**-**	-

	2005 R'000	2004 R'000

25. OPERATING LEASE COMMITMENTS

The company leases all four regional offices under non-cancellable operating lease agreements. The leases have varying terms, escalation clauses and renewal rights.

The company also leases various computer and other equipment under cancellable lease agreements. The company is generally required to give between 3 and 6 months notice for the termination of these agreements.

The lease expenditure charged to the income statement during the year is disclosed in note 22.

The future aggregate minimum lease payments under non-cancellable operating leases are as follows:

	2005 R'000	2004 R'000
Not later than 1 year	**980**	2,805
Later than 1 year and not later than 5 years	**807**	1,580
	1,787	4,385

26. RELATED PARTIES

26.1 Associated parties

The Federated Employers' Trust Limited ("FET")
The Federated Employers' Trust Limited ("FET") owns 37.4% (2004: 36.1%) of the issued share capital of FEM. FET was created to facilitate the movement in shares issued or redeemed in respect of new and cancelled policyholders respectively.

The Federated Employers' Trust ("The Trust")
The Trust, an inter-vivos trust, owns 100% of FET, and was created to house the share capital of FET. The beneficiaries of The Trust are the policyholders of FEM. In terms of the Trust Deeds, all reasonable expenditure incurred by the trust must be paid by FEM.

Associated party transactions

The Federated Employers' Trust Limited ("FET")
In 2005 FET charged FEM an administration fee of R115k (2004: R60k) for services rendered and in 2004, FET refunded FEM R61k in respect of Value Added Tax ("VAT") incorrectly charged in prior financial periods.

The net amount due by FET at 31 December 2005 is R25k (2004: R34k due to FET).

The Federated Employers' Trust ("The Trust")
In 2005 the amount paid to The Trust in respect of administration costs amounted to R67k, which is included in administration expenses (Note 22).

26.2 Related party transactions

Operating lease rentals
FEM leases its Houghton offices from Barrow Construction (Pty) Ltd., which is a related party (See note 28). Operating lease costs paid for the year were R1,78 million (2004: R1,61 million). There were no amounts due to the related party at year end.

		2005 R'000	2004 R'000

Insurance on motor vehicles and office equipment

Insurance cover for motor vehicles, office equipment and computer equipment, is placed with Alexander Forbes Insurance. Mr H Walker is a director of Alexander Forbes Financial Services, Africa, which controls Alexander Forbes Insurance. Insurance premiums paid for the year were R270 k (2004: R249 k). There were no amounts due to the related party at year end.

Consulting fees

Mr CE Saville, an independent non-executive director, provided consulting services to the company for which he was paid R22k (2004: Rnil) and he was paid an incentive of R83k in respect of 2004.

Premium income

Certain non-executive directors have insurance policies with the company in respect of their construction companies. The premium charged is at arms length, being at the same rates as would be applicable to all other policyholders. No amounts were due to the company at year end. The following is a list of premium income received in respect of these related parties:

Director	**Company name**	2005 R'000	2004 R'000
Messrs JA Barrow and JR Barrow	Barrow Group	**541**	262
Mr GD Irons	GD Irons Construction (Pty)Ltd	**241**	143
Mr CS Jiyane	Rainbow Construction (Pty)Ltd	**397**	388
Mr NF Maas	Gauteng and Free State Piling (Pty)Ltd	**120**	67
Total premium income		**1,299**	860

27. EXECUTIVE COMMITTEE COMPENSATION

	2005 R'000	2004 R'000
Total cost of employment, excluding vehicle expenses	**2,434**	2,280
Vehicle expenses	**464**	464
Incentives	**502**	531
Total earnings (Included in staff costs - note 22.1)	**3,400**	3,275

28. DIRECTORS' REMUNERATION

Executive Directors

	2005 R'000	2004 R'000
Mrs TT Pugh (2004: 01 June - 31 December)		
Basic salary	**769**	396
Pensions	**41**	32
Medical aid	**33**	16
Leave encashment	**-**	31
Vehicle costs	**114**	114
Incentive	**362**	399
Total earnings	**1,319**	988
Mr CE Saville (01 January - 31 May 2004)		
Basic salary	**-**	284
Pensions	**-**	23
Medical aid	**-**	11
Leave encashment	**-**	148
Total earnings	**-**	466
Total executive directors' earnings	**1,319**	1,454

	2005 R'000	2004 R'000
Non Executive Directors' fees		
Mr JA Barrow (Chairman)	**92**	92
Mr DG Barrow *	**46**	51
Mr RG Hurry *	**-**	39
Mr GD Irons ^	**26**	-
Dr APH Jammine	**50**	50
Mr CS Jiyane ^	**42**	10
Mr NF Maas ^	**42**	10
Mr DH Mitchell *	**-**	20
Dr H Ngakane	**42**	39
Mr CE Saville ^	**42**	20
Mr H Walker	**68**	64
Mr PL Wilmot	**73**	56
Total non-executive directors' fees	**523**	451
* resigned during the year		
^ appointed during the year		
Non Executive Directors' fees for other services		
Mr CE Saville		
- incentive	**83**	-
- consulting fees	**22**	-
Total non-executive directors' other	**105**	-
Total non-executive directors' earnings	**628**	451
Total	**1,947**	1,905
Commutation of post retirement medical aid		
Mrs TT Pugh	**-**	1,453
Charged to income	**-**	200
Utilised from provision	**-**	1,253
Mr CE Saville	**-**	1,150
Charged to income	**-**	19
Utilised from provision (Note 17)	**-**	1,131
Total	**-**	2,603

Regional offices

Head Office

1st Floor, Building no. 2,
101 Central Street
Houghton, 2198
Private Bag 87109, Houghton, 2041

Managing Director:	Mrs T T Pugh
Telephone:	(011) 359-4300
Facsimile:	(011) 359-4302

Cape Town

8th Floor, 80 Strand Street
Cape Town
8001
P O Box 2555, Cape Town, 8000

Chief Underwriting Officer:	Mr. R A Saunders
Telephone:	(021) 418-3210
Facsimile:	(021) 425-1544

Johannesburg

Ground Floor, Building no. 2,
101 Central Street
Houghton, 2198
Private Bag 87109, Houghton, 2041

Area Manager (Inland):	Mr. R Spreadbury
Claims Manager:	Ms K Naidoo
Telephone:	(011) 359-4300
Facsimile:	(011) 359-4336

Durban

16th Floor, Mercury House,
320 Smith Street
Durban, 4001
P O Box 429, Durban, 4000

Branch Manager:	Mr. M J Vernon
Assistant Branch & Claims Manager:	Mr. W A Bell
Telephone:	(031) 304-8958
Facsimile:	(031) 304-3158

Pretoria

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Branch Manager:	Mr. C A van Biljon
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FEM

THE FEDERATED EMPLOYERS' MUTUAL ASSURANCE COMPANY LIMITED