Discovery
Health Medical Scheme

FOR OUR MEMBERS

INTEGRATED
REPORT 2017

INTEGRATED REPORT 2017

Discovery Health Medical Scheme's Integrated Report is designed to cater for various readers by grouping information in a logical way according to different levels and areas of interest. The chapters in the Report can be read as standalone pieces for this purpose.

06 FINANCIALS

STATEMENT OF RESPONSIBILITY BY THE BOARD OF TRUSTEES

for the year ended 31 December 2017

The Board of Trustees is responsible for ensuring that adequate accounting records are maintained and for the preparation, integrity and fair presentation of the Annual Financial Statements of Discovery Health Medical Scheme (the Scheme). The Annual Financial Statements comprise the Statement of Financial Position at 31 December 2017, and the Statements of Comprehensive Income, Changes in Funds and Reserves and Cash Flows for the year then ended, and the Notes, comprising a summary of significant accounting policies and other explanatory information. The Annual Financial Statements have been prepared in accordance with International Financial Reporting Standards and the Medical Schemes Act 131 of 1998, as amended, (the Act) and include amounts based on judgements and reasonable estimates.

The Trustees consider that in preparing the Annual Financial Statements they have used the most appropriate accounting policies, consistently applied and that all applicable International Financial Reporting Standards have been followed. The Trustees are satisfied that the information contained in the Annual Financial Statements fairly presents the results of operations for the year and the financial position of the Scheme at year end. The Trustees also reviewed the other information included in the Integrated Report and are responsible for both its accuracy and its consistency with the Annual Financial Statements.

The Trustees are responsible for the Scheme's systems of internal control and incorporate 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. Reliance is placed on Discovery Health (Pty) Ltd's system of internal controls.

Even an effective system of internal control, no matter how well designed, has inherent limitations, including the possibility of circumvention and the overriding of controls. An effective system of internal control therefore aims to provide reasonable assurance with respect to the reliability of financial information and, in particular, the presentation of Annual Financial Statements. To the best of their knowledge and belief, based on the above, the Trustees are satisfied that no material breakdown in the operation of the systems of internal control and procedures have occurred during the year under review.

The Board of Trustees has reviewed the Scheme's budget for the year ending 31 December 2018. On the basis of this review and in light of the current financial position and available cash resources, the Trustees have no reason to believe that the Scheme will not be a going concern for the foreseeable future. The going concern basis has therefore been adopted in preparing the Annual Financial Statements and these financial statements support the viability of the Scheme.

The Scheme's external auditors, PricewaterhouseCoopers Incorporated, have audited the Annual Financial Statements and their unqualified report is presented on pages 99 to 101. The Annual Financial Statements, which are presented on pages 95 to 169 were approved by the Board of Trustees on 12 April 2018 and are signed on its behalf by:

Neil Morrison

N MORRISON
CHAIRPERSON

Daisy Naidoo

D NAIDOO
TRUSTEE

Nozipho Sangweni

DR N SANGWENI
PRINCIPAL OFFICER

REPORT OF THE AUDIT COMMITTEE

for the year ended 31 December 2017

We are pleased to present our report for the financial year ended 31 December 2017. The Audit Committee (the Committee) is an independent statutory committee. Duties are delegated to the Committee by the Board of Trustees.

Audit Committee terms of reference and assessment

The Committee has adopted formal terms of reference that have been approved by the Board of Trustees and are reviewed at least annually. The Committee has conducted its affairs in compliance with its terms of reference and has discharged the responsibilities contained therein.

Members of the Committee collectively keep up to date with key developments affecting their required skill set.

The Committee conducts self-assessments to evaluate its effectiveness. The Committee was satisfied with the results of the assessments, and no significant matters of concern were identified.

Audit Committee members, meeting attendance and assessment

The membership and attendance of the members of the Committee has been set out on page 55.

Role and responsibilities

The Committee's role and responsibilities include statutory duties as per the Act and further responsibilities assigned to it by the Board. The Committee executed its duties in accordance with its terms of reference and applicable laws and regulations in force during the financial year.

External Auditor appointment and independence

The Committee considered the matters set out in Section 36 of the Act and nominated PricewaterhouseCoopers Inc. for appointment as external auditor of the Scheme. Corlia Volschenk was approved by the Council for Medical Schemes as the statutory auditor of the Scheme for the financial period 1 January 2017 to 31 December 2017 in accordance with section 36 (2) of the Act on 3 October 2017.

The Committee has satisfied itself that the External Auditor is independent of the Scheme as set out in Section 36 (3) of the Act. Requisite assurance was sought and provided by the Auditor that internal governance processes within the audit firm support and demonstrate its independence.

The Committee ensured that the appointment of the Auditor at the Annual General Meeting complied with the Act and Scheme Rules relating to the appointment of auditors.

The Committee, following consultation with the Scheme's Executive Officers, approved the engagement letter, audit plan, budgeted audit fees and representation letter for the year ended 31 December 2017. The Committee approved the actual audit fees for the year ended 31 December 2016.

There is a formal policy in respect of the provision of non-audit services by the External Auditors of the Scheme and a formal procedure governs the process whereby the Auditor is appointed to provide any non-audit services. The Chairperson of the Committee approves the nature and extent of any non-audit services that the External Auditor provides in terms of the agreed pre-approval policy and a schedule of approved non-audit services is reviewed annually by the Committee. Fees in respect of audit and non-audit services are reflected in Note 15 to the Annual Financial Statements.

During the year, the Committee met with the External Auditors without management being present.

Internal Auditors (IA)

The Committee is responsible for ensuring that IA is independent and has the necessary resources, standing and authority to enable it to discharge its duties. Furthermore, the Committee oversees cooperation between IA and the External Auditors, and serves as a link between the Board of Trustees and these functions.

The Committee considered and approved the IA Charter.

The IA annual audit plan was approved by the Committee. The results of the work carried out by IA in terms of the audit plan were reviewed and the effect of any action plans to mitigate risks of any matters reported were considered by the Committee.

IA has responsibility for reviewing and providing assurance on the adequacy of the internal control environment across all of the Scheme's operations. The Chief Audit Executive (CAE) is responsible for reporting the findings of the internal audit work, against the agreed IA plan to the Committee on a regular basis.

The CAE has direct access to the Committee, primarily through its Chairman.

The Committee has assessed and was satisfied with the performance of the CAE and the IA function.

During the year, the Committee met with the CAE without management being present.

Financial statements and accounting practices

The Committee has reviewed the accounting policies and the Scheme's Annual Financial Statements and is satisfied that they are appropriate and comply with International Financial Reporting

REPORT OF THE AUDIT COMMITTEE CONTINUED

for the year ended 31 December 2017

Standards, the Act and circulars issued by the Council for Medical Schemes.

Internal financial controls

The Committee is responsible for assessing the Scheme's system of internal financial and accounting control. In this regard the Committee has, among other things, evaluated the adequacy and effectiveness of the Scheme's systems of internal control and made appropriate recommendations to the Board of Trustees. This included a formal documented review by the Internal Audit function of the design, implementation and effectiveness of the Administrator's system of internal financial controls pertaining to the Scheme. Based on the results of this review, it is the view of the Committee that Reasonable Assurance* can be placed on the internal controls and risk management and High Assurance** can be placed on the adequacy and effectiveness of the Scheme's internal financial controls, relative to the fair presentation of the Annual Financial Statements.

* *Reasonable Assurance – The existing control framework provides reasonable assurance that material risks are identified and managed effectively.*

** *High Assurance – The existing control framework provides a high level of assurance that the Annual Financial Statements are fairly presented.*

Evaluation of the expertise and experience of the Chief Financial Officer and Finance function

The Committee is satisfied with the expertise and experience of the Scheme's Chief Financial Officer. The Committee further reviewed and satisfied itself of the appropriateness of the expertise, resources and experience of the Administrator's Finance function pertaining to the Scheme.

Whistle blowing

The Committee receives and deals with any concerns or complaints, whether from within or outside the Scheme, relating to the accounting practices and Internal Audit of the Scheme, the content or auditing of the Scheme's financial statements, the internal financial controls of the Scheme and related matters. The Administrator's forensic department assists the Committee in discharging this responsibility. No such concerns or complaints were received during the year.

Ethics and compliance

The Committee is responsible for reviewing any major breach of relevant legal and regulatory obligations. The Committee is satisfied that there has been no material non-compliance with laws and regulations, except for the matters of non-compliance with the Act as detailed in Note 33 to the Annual Financial Statements.

Risk management

The Committee monitors the risk management processes and systems of internal control of the Scheme through review of reports from and discussions with the Scheme's internal and external auditors and the risk management function.

Due to the Audit Committee's responsibility for ensuring that appropriate systems are in place for the monitoring of risk and compliance with laws, regulations and codes of conduct, the members of the Audit Committee also serve as members of the Risk Committee.

The Committee is satisfied that the system and the process of risk management is effective.

Going concern

The Committee has reviewed the Scheme's financial position as at 31 December 2017, as well as the budget for the year ending 31 December 2018. Total members' funds exceeded R16.6 billion with a solvency level of 27.44% as at 31 December 2017. Further, the Scheme had sufficient financial resources (cash and cash equivalents and financial assets at fair value through profit or loss) investments as at 31 December 2017 to cover monthly claims expenditure 5.78 times.

On the basis of this review and taking note of the current net surplus of R2.5 billion, the Committee considers that:

1. The Scheme's assets currently exceeds its liabilities; and
2. The Scheme will be able, in the ordinary course of the Scheme's business, to settle its liabilities as they arise for the foreseeable future.

The Committee agreed that based on the assessment conducted, the Board of Trustees could be advised that there is no reason to believe that the Scheme will not be a going concern in the foreseeable future.

MR B STOTT
CHAIRPERSON: AUDIT COMMITTEE

12 April 2018

INDEPENDENT AUDITOR'S REPORT

To the members of Discovery Health Medical Scheme

Report on the financial statements

Opinion

We have audited the financial statements of Discovery Health Medical Scheme (the Scheme), set out on pages 102 to 169, which comprise the statement of financial position as at 31 December 2017, and the statement of comprehensive income, the statement of changes in funds and reserves, and the statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Scheme as at 31 December 2017, and its financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards and the requirements of the Medical Schemes Act of South Africa.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report. We are independent of the Scheme in accordance with the Independent Regulatory Board for Auditors Code of Professional Conduct for Registered Auditors (IRBA Code) and other independence requirements applicable to performing audits of financial statements in South Africa. We have fulfilled our other ethical responsibilities in accordance with the IRBA Code and in accordance with other ethical requirements applicable to performing audits in South Africa. The IRBA Code is consistent with the International Ethics Standards Board for Accountants Code of Ethics for Professional Accountants (Parts A and B). We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key audit matter	How our audit addressed the key audit matter
Outstanding claims provision The outstanding claims provision (IBNR) of R1 240 billion at year-end as described in Note 6 to the financial statements, is a provision recognised for the estimated cost of healthcare benefits that have been incurred prior to year-end but that were only reported to the Scheme after year-end. The outstanding claims provision is calculated by the Scheme's actuaries, is reviewed by management and the Audit Committee, and recommended to the Board of Trustees for approval. The Scheme's actuaries use an actuarial model based on the Scheme's actual claim development patterns throughout the year to project the year-end provision. This model applies a combination of the Basic Chain Ladder (BCL) and Cost Per Event (CPE) methods. The claim treatment date, processing date and amount are used to derive claim development patterns. These historical patterns are then used to estimate the outstanding claims provision. We identified this as a matter of most significance to the audit because of the uncertainty in the projected claims pattern. A change in the projected claims pattern can cause a material change to the amount of the provision.	For a sample of actual claims received in the 2017 financial year, we tested the accuracy of the service and process dates and we identified no inconsistencies. We made use of various data analytics to substantively test the relevant claim rules against which the actual claims received by the Scheme are assessed for completeness and validity of actual claims data. The claims data that was included in the Scheme's actuarial model was agreed to the actual claims data that was tested above in the member administration system with no material differences noted. We obtained an understanding from the Scheme's actuaries regarding the process to calculate the outstanding claims provision. The actuarial model applied by the Scheme is generally applied within the medical scheme industry. To test the reasonableness of the Scheme's estimation process we compared actual claim results in the current year to the prior year provision and no material differences were noted. Our actuarial specialist independently calculated the Scheme's outstanding claims provision, taking into account the method applied by the Scheme and the claim data tested above. We compared our results with those of the Scheme and found the amounts to approximate each other.

INDEPENDENT AUDITOR'S REPORT CONTINUED

Other information

The Scheme's Trustees are responsible for the other information. The other information comprises the information included in the Discovery Health Medical Scheme Integrated Report as at 31 December 2017. This does not include the financial statements and our auditor's report thereon.

Our opinion on the financial statements does not cover the other information and we do not express an audit opinion or any form of assurance conclusion thereon.

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

Responsibilities of the Scheme's Trustees for the financial statements

The Scheme's Trustees are responsible for the preparation and fair presentation of the financial statements in accordance with International Financial Reporting Standards and the requirements of the Medical Schemes Act of South Africa, and for such internal control as the Scheme's Trustees determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Scheme Trustees are responsible for assessing the Scheme's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Scheme's Trustees either intend to liquidate the Scheme or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Scheme's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Scheme's Trustees.
- Conclude on the appropriateness of the Scheme's Trustees' use of the going concern basis of accounting and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Scheme's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Scheme to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with the Scheme's Trustees regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

From the matters communicated with the Scheme's Trustees, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Report on other legal and regulatory requirements

Non-compliance with the Medical Schemes Act of South Africa

As required by the Council for Medical Schemes, we report the following material instances of non-compliance with the requirements of the Medical Schemes Act of South Africa as amended that have come to our attention during the course of our audit:

- **Section 33 (2) (b) of the Medical Schemes Act of South Africa:** Certain benefit options were not self-supporting in terms of financial performance, as disclosed in Note 33 of the financial statements; and
- **Regulation 29 (2) of the Medical Schemes Act of South Africa:** The Scheme's accumulated funds expressed as a percentage of gross annual contributions was below the statutory solvency requirement of 25% at the end of January 2017. However, at 31 December 2017, the Scheme's accumulated funds expressed as a percentage of gross annual contributions was 27.44% which exceeded the statutory solvency requirement of 25%, as disclosed in Note 33 of the financial statements.

PricewaterhouseCoopers Inc.

PricewaterhouseCoopers Inc.
Director: C Volschenk
Registered Auditor
Johannesburg
12 April 2018

STATEMENT OF FINANCIAL POSITION

as at 31 December 2017

R'000	Notes	2017	2016
ASSETS			
Non-current assets		**4 417**	5 614
Long term employee benefit plan asset	25	**4 417**	5 614
Current assets		**25 728 677**	20 864 905
Financial assets at fair value through profit or loss	2	**14 005 644**	12 211 677
Derivative financial instruments	7	**85 857**	54 760
Trade and other receivables	3	**1 147 665**	2 058 008
Cash and cash equivalents			
– Personal Medical Savings Account trust assets	4	**4 609 149**	4 142 672
– Medical Scheme assets	5	**5 880 362**	2 397 788
Total assets		**25 733 094**	20 870 519
FUNDS AND LIABILITIES			
Members' funds		**16 684 435**	14 234 461
Accumulated funds		**16 684 435**	14 234 461
Current liabilities		**9 048 659**	6 636 058
Outstanding claims provision	6	**1 240 063**	1 121 394
Derivative financial instruments	7	**86 445**	4 376
Personal Medical Savings Account trust liabilities	8	**4 656 633**	4 204 043
Trade and other payables	9	**3 065 518**	1 306 245
Total funds and liabilities		**25 733 094**	20 870 519

STATEMENT OF COMPREHENSIVE INCOME

for the year ended 31 December 2017

R'000	Notes	2017	2016
Risk contribution income	10	**48 702 024**	43 626 398
Relevant healthcare expenditure		**(41 747 808)**	(38 035 898)
Net claims incurred	11	**(40 228 057)**	(36 613 210)
Claims incurred	11	**(40 371 417)**	(36 772 332)
Third party claim recoveries	11	**143 360**	159 122
Accredited managed healthcare services (no risk transfer)	12	**(1 534 311)**	(1 407 267)
Net profit/(loss) on risk transfer arrangements	13	**14 560**	(15 421)
Risk transfer arrangement fees		**(392 023)**	(366 344)
Recoveries from risk transfer arrangements		**406 583**	350 923
Gross healthcare result		**6 954 216**	5 590 500
Broker service fees	14	**(1 214 205)**	(1 101 648)
Expenses for administration	25	**(4 511 596)**	(4 150 194)
Other operating expenses	15	**(260 461)**	(236 206)
Net healthcare result		**967 954**	102 452
Other income		**1 893 686**	1 524 116
Investment income	21	**1 433 187**	1 257 479
Net gains on financial assets at fair value through profit or loss	22	**458 753**	264 278
Sundry income	23	**1 746**	2 359
Other expenditure		**(411 666)**	(321 118)
Expenses for asset management services rendered		**(44 428)**	(31 076)
Interest paid	24	**(367 238)**	(290 042)
Net surplus for the year		**2 449 974**	1 305 450
Other comprehensive income		**–**	–
Total comprehensive income for the year		**2 449 974**	1 305 450

STATEMENT OF CHANGES IN FUNDS AND RESERVES

for the year ended 31 December 2017

R'000	2017 Accumulated funds	2016 Accumulated funds
Balance at beginning of the year	**14 234 461**	12 929 011
Total comprehensive income for the year	**2 449 974**	1 305 450
Total member funds at end of the year	**16 684 435**	14 234 461

STATEMENT OF CASH FLOWS

for the year ended 31 December 2017

R'000	Notes	2017	2016
CASH FLOWS FROM OPERATING ACTIVITIES			
Cash flows generated from operations before working capital changes	27	**1 017 921**	151 902
Working capital changes:			
Decrease/(Increase) in trade and other receivables	27.1	**822 739**	(500 589)
Increase in outstanding claims provision		**118 669**	136 307
Increase in Personal Medical Savings Account trust liabilities		**452 590**	467 384
Increase in trade and other payables	27.2	**1 759 273**	123 640
Cash generated by operations		**4 171 192**	378 644
Purchases of financial instruments	27.3	**(2 953 775)**	(1 922 170)
Proceeds from sale of financial instruments	27.4	**1 669 533**	1 258 510
Increase in Long Term Employee Plan Asset		**(3 848)**	(7 544)
Interest received	21	**1 349 125**	1 206 486
Dividend income	21	**84 062**	50 993
Interest paid	24	**(367 238)**	(290 042)
Net cash flows from operating activities		**3 949 051**	674 877
NET INCREASE IN CASH AND CASH EQUIVALENTS		**3 949 051**	674 877
Cash and cash equivalents at beginning of year		**6 540 460**	5 865 583
CASH AND CASH EQUIVALENTS AT END OF YEAR		**10 489 511**	6 540 460
Cash and cash equivalents comprise			
Personal Medical Savings Account trust assets	4	**4 609 149**	4 142 672
Medical Scheme assets	5	**5 880 362**	2 397 788
		10 489 511	6 540 460

ACCOUNTING POLICIES

for the year ended 31 December 2017

General information

The Discovery Health Medical Scheme (the Scheme) offers the insurance of hospital, chronic illness and day-to-day benefits and is administered by Discovery Health (Pty) Ltd, a wholly owned subsidiary of Discovery Limited, listed in the insurance sector of the Johannesburg Stock Exchange (JSE).

The Scheme is an open medical scheme registered in terms of the Medical Schemes Act 131 of 1998, as amended (the Act) and is domiciled in South Africa.

These Annual Financial Statements were authorised for issue by the Board of Trustees on 12 April 2018.

1 Basis of preparation

The Annual Financial Statements have been prepared in accordance with International Financial Reporting Standards (IFRS), which are set by the International Accounting Standards Board (IASB). The Annual Financial Statements are also prepared in accordance with the Act, which requires additional disclosures for registered medical schemes.

The accounting policies applied in the preparation of these Annual Financial Statements are set out below. These policies have been consistently applied to all years presented, except for changes required by the mandatory adoption of new and revised IFRS, discussed in the table below.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Scheme's accounting policies. The areas involving a higher degree of judgement, or areas where estimates are significant to the Annual Financial Statements, are disclosed in Note 32.

The Annual Financial Statements are prepared in accordance with the going concern principle using the historical cost basis except for certain financial assets and liabilities, which include:

- Financial instruments at fair value through profit or loss; and
- Derivative financial instruments carried at fair value through profit or loss.

All monetary information and figures presented in these financial statements are stated in thousands of rand (R'000), unless otherwise indicated.

ACCOUNTING POLICIES CONTINUED

for the year ended 31 December 2017

1 Basis of preparation *continued*

New standards, amendments and interpretations not yet effective and relevant to the Scheme:

The following new standards, amendments and interpretations to the existing standards have been published and are not yet effective for the current financial year. The Scheme has not early adopted them and it is not expected that they will have any material impact on the Scheme's assets, liabilities and results but may result in additional disclosure in the financial statements.

Standard	Scope	Effective date
IFRS 4 (Amendment): Insurance contracts	These two amendments address the interaction between IFRS 9: Financial Instruments and IFRS 4. A temporary exemption from IFRS 9 has been granted to insurers that meet the specified criteria and an optional accounting policy choice has been introduced to allow an insurer to apply the overlay approach to designated financial assets when it first applied IFRS 9. The Scheme will not apply the temporary exemption or the overlay approach.	01 January 2018.
IFRS 9 (Amendment): Financial instruments	The final version of IFRS 9 replaces IAS 39 Financial Instruments: Recognition and Measurement and comprises guidance on Classification, Measurement, Impairment Hedge Accounting and Derecognition. IFRS 9 introduces a new approach to the classification of financial assets, which is driven by the business model in which the asset is held and its cash flow characteristics. A new business model was introduced which allows certain financial assets to be categorised as "fair value through other comprehensive income" in certain circumstances. The requirements for financial liabilities are mostly carried forward from IAS 39. Some changes were made to the fair value option for financial liabilities to address the issue of own credit risk allowing the recognition of these changes in other comprehensive income for liabilities designated as fair value through profit or loss. The standard changes the impairment model from an incurred loss model and introduces a single "expected credit loss" impairment model for the measurement of financial assets. The standard contains a new model for hedge accounting that aligns the accounting treatment with the entity's risk management activities. Enhanced disclosures will provide better information about risk management and the effect of hedge accounting on the financial statements. Potential impact: The Scheme classifies financial assets at "fair value through profit or loss" or "amortised cost". The changes introduced by this standard will have no material impact on the Scheme. The introduction of the expected credit loss model and the requirement for the loss allowance to be measured at an amount equal to the lifetime expected credit losses has been assessed and not expected to have a material impact on the Scheme's results. The Scheme does not have any financial liabilities at fair value.	01 January 2018.

1 Basis of preparation *continued*

New standards, amendments and interpretations not yet effective and relevant to the Scheme:

Standard	Scope	Effective date
IFRS 16: Leases	The standard introduces a single lessee accounting model and requires a lessee to recognise assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. A lessee is required to recognise a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. A lessee measures right-of-use assets similarly to other non-financial assets (such as property, plant and equipment) and lease liabilities similarly to other financial liabilities. As a consequence, a lessee recognises depreciation on the right-of-use asset and interest on the lease liability, and also classifies cash repayments of the lease liability into a principal and interest portion and presents them in the statement of cash flows. The Scheme does not have any agreements with a term of more than 12 months.	01 January 2019.
IFRS 17: Insurance contracts	The standard was issued in May 2017 and supersedes IFRS 4 Insurance Contracts. The standard creates one accounting model for all insurance contracts and establishes principles for the recognition, measurement, presentation and disclosure of insurance contracts issued. The standard requires insurance contracts to be measured using updated estimates and assumptions that reflect the timing of cash flows and take into account any uncertainty relating to insurance contracts. The standard provides for a simplified approach (premium allocation approach) for the measurement of a group of insurance contracts only if at the inception of the group, the entity reasonably expects that the simplification will produce measurement of the liability for remaining coverage that would not differ materially from that produced using the general measurement model and if the coverage period is one year or less. Potential impact: The coverage period for the Scheme's contracts is one year or less allowing for the premium allocation approach to be applied, resulting in similar treatment to the current accounting treatment with the most notable exception being the treatment of onerous contracts.	01 January 2021.

ACCOUNTING POLICIES CONTINUED

for the year ended 31 December 2017

2 Classification, recognition, presentation and derecognition of financial instruments

The Scheme recognises a financial instrument when, and only when, it becomes a party to the contractual provisions of the instrument. The Scheme classifies its financial instruments into the following categories: financial assets or financial liabilities at fair value through profit or loss, and loans and receivables. Loans and receivables are receivables other than those arising from insurance contracts and include balances due by related parties, sundry accounts receivable and interest receivable. Loans and receivables are disclosed under Trade and other receivables.

The classification depends on the purpose for which the financial instruments are acquired. Management determines the classification of financial instruments at initial recognition. All purchases and sales of financial instruments are recognised on the trade date, which is the date on which the Scheme commits to purchase the financial asset or assume financial liability.

Offsetting financial instruments

This applies where a legally enforceable right to set off exists for recognised financial assets and financial liabilities, and there is an intention to realise the asset and settle the liability simultaneously or to settle on a net basis.

The Scheme will disclose the net asset or liability in the Statement of Financial Position or accompanying notes if the above conditions are met.

Derecognition of financial assets and liabilities

The Scheme derecognises a financial asset or part of a financial asset when:

- The contractual right to the cash flows from the asset expires.
- The Scheme retains the contractual right to receive cash flows of the asset, but assumes the obligation to pay one or more third parties the cash flow without material delay.
- The Scheme transfers the asset, while transferring substantially all the risks and rewards of ownership.
- The Scheme neither transfers the financial asset nor retains significant risk and reward of ownership, but has transferred control of the financial asset.

The Scheme derecognises a financial liability when the obligation under the liability is discharged, cancelled or expires.

3 Financial assets

Financial assets at fair value through profit or loss

The Scheme recognises a financial asset at fair value through profit or loss when any of the following conditions are met:

- The asset is acquired principally for the purpose of selling in the near term.
- The portfolio of assets are traded for short-term profit.
- A derivative that is not designated as an effective hedge.
- Upon initial recognition the Scheme designated the asset as fair value through profit or loss.

A group of financial assets is designated as at fair value through profit or loss if it is managed and its performance is evaluated on a fair value basis, in accordance with the Scheme's documented risk management strategy, and information about the group of assets is provided internally on that basis to the Scheme's key management personnel.

Financial assets at fair value through profit or loss are initially recognised at fair value and the transaction costs are expensed in the profit or loss section of the Statement of Comprehensive Income.

The fair value of the financial instruments traded in an active market is determined by using quoted market prices or dealer quotes. The fair value of financial instruments not traded in an active market is determined by using valuation techniques that maximise the use of observable market data and rely as little as possible on entity specific estimates.

Gains or losses arising from subsequent changes in fair value are recognised under Other Income in the Statement of Comprehensive Income within the period in which they arise.

Trade and other receivables

Receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than those the Scheme intends to sell in the short term.

Receivables are initially recognised at fair value plus transaction costs and subsequently measured at amortised cost using the effective interest rate method, less provision for impairment.

4 Foreign currency translation

Functional and presentation currency

Items included in the Annual Financial Statements are measured using the currency of the primary economic environment in which the entity operates (functional currency).

The functional and presentation currency of the Scheme is the South African Rand (R).

Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets denominated in foreign currencies are recognised in the Statement of Comprehensive Income.

5 Scheme amalgamations

Scheme amalgamations are accounted for by applying the acquisition method.

The cost of an amalgamation is measured as the fair value of the assets transferred and liabilities incurred or assumed at the date of exchange.

When an entity is amalgamated into the Scheme, all identifiable assets, liabilities and members' funds are accounted for at their fair values at the acquisition date. No consideration is paid for these transactions and they are recognised as from the transaction date.

The Scheme recognises the net assets from amalgamated schemes as a direct addition to reserves in its Statement of Financial Position.

Section 63 (14) of the Act prescribes that relevant assets and liabilities of the party effecting the transfer shall vest in and become binding upon the party to which transfer is effected.

No goodwill is recognised on the amalgamation of schemes.

6 Cash and cash equivalents

Cash and cash equivalents are short-term, highly liquid instruments that are readily convertible to known amounts of cash and are subject to an insignificant risk of changes in value.

In the Statement of Cash Flows, cash and cash equivalents comprise:

- Coins and bank notes.
- Money on call and short notice.
- Balances with banks.

Cash and cash equivalents only include items held for the purpose of meeting short-term cash commitments rather than for investing or other purposes and are carried at cost, which, due to their short-term nature, approximates fair value.

7 Impairment of financial assets

The Scheme assesses at each reporting date whether there is objective evidence that a financial asset is impaired. A financial asset or group of financial assets is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a "loss event") and that loss event (or events) has an adverse impact on the estimated future cash flows of the financial asset that can be reliably estimated.

Objective evidence that a financial asset or group of financial assets is impaired includes observable data that comes to the attention of the Scheme regarding the following loss events:

- Significant financial difficulty of service provider or member debtors.
- Breach of contract, such as non-payment of member contributions when due and if these remain unpaid for extended periods.
- Default or delinquency in payments due by service providers and other debtors.
- Observable data indicating that there is a measurable decrease in the estimated future cash flows from other Scheme assets since the initial recognition of those assets, although the decrease cannot yet be attributed to the individual financial assets in the Scheme.
- Adverse changes in the payment status of members of the Scheme.
- National or local economic conditions that correlate with non-payment of debtor contributions.

The Scheme first assesses whether objective evidence of impairment exists, individually for financial assets that are individually significant, such as service provider debtors. In the case of assets which are not individually significant, such as contribution debtors, financial assets are grouped on the basis of similar credit characteristics, such as asset type and past due status. These characteristics are used in the estimation of future recoverable cash flows.

If there is objective evidence that an impairment loss on a financial asset has been incurred, the amount of the loss is measured as the difference between the assets' carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced and the amount of the loss is recognised in the Statement of Comprehensive Income.

When a receivable is uncollectable, it is written off against the related provision for impairment. Such receivables are written off after all the necessary collection procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off decrease the amount of the provision for impairment in the Statement of Comprehensive Income.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognised in the Statement of Comprehensive Income.

ACCOUNTING POLICIES CONTINUED

for the year ended 31 December 2017

8 Members' funds

The funds represent the accumulated funds of the Scheme. The funds are mainly held as statutory reserves in lieu of the solvency requirement as required by the Act.

9 Financial liabilities

Financial liabilities are initially recognised at fair value net of transaction costs incurred. After initial recognition the financial liabilities are measured at amortised cost, using the effective interest rate method. In addition, the Scheme is not permitted to borrow, in terms of Section 35 (6) (c) of the Act. The Scheme therefore has no long-term financial liabilities.

Derivative liabilities include liabilities that exist at year end as a result of marked-to-market losses accrued on derivative instruments.

Trade payables

Trade payables are obligations to pay for goods or services that have been acquired in the ordinary course of business from suppliers. Trade payables are classified as current liabilities if payment is due within one year or less. If not, they are presented as non-current liabilities.

Trade payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest rate method.

Personal Medical Savings Account trust liabilities

Members' Personal Medical Savings Accounts, which are managed by the Scheme on behalf of its members, represent savings contributions (which are a deposit component of the insurance contracts), and accrued interest thereon, net of any savings claims paid on behalf of members in terms of the Scheme's registered rules. The deposit component has been unbundled since the Scheme can measure the deposit component separately and the Scheme's accounting policies do not otherwise require recognition of all obligations and rights arising from the deposit component.

The savings accounts contain a demand feature and are initially measured at fair value plus transaction costs, which is the amount payable to a member on demand, discounted from the first date that the amount could be required to be paid. Subsequent to initial measurement, the liability is measured at amortised cost using the effective interest rate method.

Unspent savings at year end are carried forward to meet future expenses for which the members are responsible. In terms of the Act, balances standing to the credit of members are refundable only in terms of Regulation 10 of the Act.

Advances on savings contributions are funded from the Scheme's funds and the risk of impairment is carried by the Scheme.

Interest payable on members' Personal Medical Savings Accounts is expensed when incurred.

10 Provisions

The Scheme recognises a provision once the following conditions are met:

- It 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.
- A reliable estimate of the amount of the obligation can be made.

Provisions are measured as the present value of management's best estimate of the expenditure required to settle the obligation at the reporting date. Where the effect of discounting to present value is material, provisions are adjusted to reflect the time value of money.

Outstanding claims provision

Claims outstanding comprise provisions for the Scheme's best estimate of the ultimate cost of settling all claims incurred but not yet reported at the reporting date. Claims outstanding are determined as accurately as possible based on a number of factors. These include previous experience in claims patterns, claims settlement patterns, trends in claims frequency, changes in the claims processing cycle, and variations in the nature and average cost incurred per claim.

Claims handling expenses are not separately accounted for as this service is provided by the Administrator and a fixed fee is paid for the full administration service including claims handling. No provision for claims handling expenses is required as the Scheme has no further liability to the Administrator at year end.

Estimated co-payments and payments from members' Personal Medical Savings Accounts are deducted in calculating the outstanding claims provision. The Scheme does not discount its provision for outstanding claims since the effect of the time value of money is not considered material.

11 Contingent liability

The Scheme will disclose a contingent liability if one of the following conditions are met:

- A possible obligation arising from past events, the existence of which will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Scheme.
- A present obligation that arises from past events but not recognised because:
  - It is not probable that an outflow of resources will be required to settle an obligation.
  - The amount of the obligation cannot be measured with sufficient reliability.

12 Member insurance contracts

Contracts under which the Scheme accepts significant insurance risk from another party (the member) by agreeing to compensate the member or other beneficiary if a specified uncertain future event (the insured event) adversely affects the member or other beneficiary are classified as insurance contracts.

The contracts issued compensate the Scheme's members for healthcare expenses incurred and are detailed in Note 30.

13 Contribution income

Gross contributions comprise risk contributions and Personal Medical Savings Account contributions.

Contributions on member insurance contracts are accounted for monthly when their collection in terms of the insurance contract is reasonably assured. Risk contributions represent gross contributions after the deduction of Personal Medical Savings Account contributions. Risk contributions are earned from the date of attachment of risk, over the indemnity period on a straight-line basis. The earned portion of risk contributions received is recognised as revenue.

Risk contributions are shown before the deduction of broker service fees.

14 Relevant healthcare expenditure

Relevant healthcare expenditure consists of net claims incurred, accredited managed healthcare services (no risk transfer) and net income or expense from risk transfer arrangements.

14.1 Claims incurred

Gross claims incurred comprises of the total estimated cost of all claims arising from healthcare events that have occurred in the year and for which the Scheme is responsible, whether or not reported by the end of the year.

Risk claims incurred comprise:

- Claims submitted and accrued for services rendered during the year.
- Payments under provider contracts for services rendered to members.
- Over or under provisions relating to prior year claims estimates.
- Claims incurred but not yet reported.
- Claims settled in terms of risk transfer arrangements.

Net of:

- Claims from members' Personal Medical Savings Accounts.
- Recoveries from members for co-payments.
- Recoveries from third parties.
- Discount received from service providers.

Anticipated recoveries under risk transfer arrangements are disclosed separately as assets and are assessed in a manner similar to the assessment of the outstanding claims provision and claims reported not yet paid.

14.2 Risk transfer arrangements

Risk transfer arrangements are contractual arrangements entered into by the Scheme with a third party which undertakes to indemnify the Scheme against all or part of the loss that the Scheme may incur as a result of carrying on the business of a medical scheme. Risk transfer arrangements do not reduce the Scheme's primary obligations to its members and their dependants, but the arrangements only decrease the loss the Scheme may incur as a result of carrying on the business of a medical scheme.

Risk transfer arrangement fees (including Managed care: healthcare services) are recognised as an expense over the indemnity period on a straight-line basis.

The claims incurred under member insurance contracts and the equivalent claims recoveries are presented in the Statement of Comprehensive Income on a gross basis. Amounts recoverable under such contracts are therefore recognised in the same year as related claims. The claims incurred liability under risk transfer arrangements and the equivalent receivable are also presented in the Statement of Financial Position on a gross basis.

Assets relating to risk transfer arrangements include balances due under risk transfer arrangements for outstanding claims provisions and claims reported not yet paid. Amounts recoverable under risk transfer arrangements are estimated in a manner consistent with the outstanding claims provision, claims reported not yet paid and settled claims associated with the risk transfer arrangement.

Amounts recoverable under risk transfer arrangements are assessed for impairment at each reporting date. These assets are deemed impaired if there is objective evidence, as a result of an event that occurred after its initial recognition, that the Scheme may not recover all amounts due and that the event has a reliably measurable impact on the amounts that the Scheme will receive under the risk transfer arrangement. The Scheme gathers the objective evidence that a risk transfer arrangement asset is impaired using the same process adopted for financial assets held at amortised cost. The impairment loss is also calculated following the same method used for these financial assets. These processes are described in Accounting Policy Note 7.

ACCOUNTING POLICIES CONTINUED

for the year ended 31 December 2017

14 Relevant healthcare expenditure *continued*

14.3 Accredited managed healthcare services (no risk transfer)

Accredited managed healthcare services (no risk transfer) fees comprise amounts paid or payable to a third party for managing the utilisation, costs and quality of healthcare services to the members of the Scheme and are expensed as incurred.

Accredited managed healthcare services are part of healthcare expenditure as they directly impact on the delivery of cost-effective and appropriate healthcare benefits to beneficiaries of the Scheme.

15 Liability adequacy test

Liability adequacy tests are performed to ensure the adequacy of the member insurance contract liabilities as at the reporting date. In performing these tests, current estimates of future cash flows under the Scheme's insurance contracts are used. Any deficiency is immediately recognised in the Scheme's surplus or deficit for the year.

16 Broker service fees

Broker service fees are fees paid as acquisition costs for the introduction and provision of ongoing services to members and are expensed as incurred.

17 Expenses for administration and other operating expenses

Fees paid to the Scheme Administrator are included in Expenses for administration and are expensed as incurred. Other operating expenses include expenses other than administration fees and are expensed as incurred.

18 Investment income

Investment income comprises dividends and interest received and accrued on investments at fair value through profit or loss and interest on cash and cash equivalents.

Interest income is recognised using the effective interest method, taking into account the principal amount outstanding and the effective interest rate over the period to maturity, when it is determined that such income will accrue to the Scheme.

Dividend income from investments is recognised when the right to receive payment is established – this is on the "last day to trade" for listed shares and on the "date of declaration" for unlisted shares.

19 Reimbursements from the road accident fund

The Scheme grants assistance to its members in defraying expenditure incurred in connection with the rendering of any relevant health service. Such expenditure may be in connection with a claim that is also made against the Road Accident Fund, administered in terms of the Road Accident Fund Act No 56 of 1996. If the member is reimbursed by the Road Accident Fund, they are obliged contractually to cede that payment to the Scheme to the extent that they have already been compensated.

Due to the uncertainty around the confirmation and measurability of the Road Accident Fund amounts, the Scheme accounts for these amounts on a cash basis and recognises them as a reduction of net claims incurred.

20 Unallocated funds

Unallocated funds arise on the receipt of unidentified deposits in favour of the Scheme.

Unallocated funds that have legally prescribed, that is funds older than three years, are written back and are included under Sundry income on the face of the Statement of Comprehensive Income.

A liability for unallocated funds that have not legally prescribed is recognised and disclosed under Trade and other payables. The liability is measured at amortised cost using the effective interest rate method.

21 Employee benefits

Pension obligations

All employees of the Scheme are members of defined contribution plans. Defined contribution plans are plans under which the Scheme pays fixed contributions to separate legal entities.

The Scheme has no legal or constructive obligation to pay further contributions if the funds do not hold sufficient assets to pay all employees the benefits relating to employee service in the current and prior periods. The Scheme has no further payment obligations once the contributions have been paid. Contributions to the defined contribution funds are recognised in the net surplus or deficit for the year in which they are incurred.

Other post-employment obligations

The Scheme has no liability for the post-retirement medical benefits of employees.

Other long term employee benefits

The long term employee benefit plan refers to awards made to qualifying employees.

The amount recognised in the Statement of Financial Position in respect of the defined benefit plan is the present value of the defined benefit obligation at the end of the reporting period less the fair value of plan assets out of which the obligations are to be settled directly. The defined benefit obligation is calculated using the Projected Unit Credit Method.

Leave pay accrual

The Scheme recognises in full employees' rights to annual leave entitlement in respect of past service.

Bonuses

Management and staff bonuses are recognised as an expense in staff costs as incurred.

22 Income tax

In terms of Section 10 (1) (d) of the Income Tax Act 58 of 1962, as amended, receipts and accruals of a benefit fund are exempt from normal tax. A medical scheme is included in the definition of a benefit fund and consequently the Scheme is exempt from income tax.

23 Allocation of income and expenditure to benefit plans

The following items are directly allocated to benefit plans:

- Contribution income.
- Claims incurred.
- Risk transfer arrangement fees.
- Accredited managed healthcare service fees.
- Expenses for administration.
- Broker service fees.
- Interest paid on Personal Medical Savings Accounts.

The remaining items are allocated as detailed below:

- For contributions that are not directly allocated to benefit plans, these amounts are apportioned based on a percentage of net contribution income per plan.
- For claims that are not directly allocated to benefit plans, these amounts are apportioned based on a percentage of net claims incurred per plan.
- The following items are apportioned based on the number of members per benefit plan:
  - Other operating expenditure;
  - Investment income, excluding interest income on Personal Medical Savings Accounts;
  - Net fair value gains/(losses) on financial assets at fair value through profit or loss;
  - Other income;
  - Expenses for asset management services rendered; and
  - Interest paid, excluding Personal Medical Savings Accounts.

24 Structured entities

A structured entity is an entity that has been designed so that voting or similar rights are not the dominant factor in deciding who controls the entity, such as when any voting rights relate to administrative tasks only, and the relevant activities are directed by means of contractual agreements. A structured entity often has some or all of the following features or attributes:

- Restricted activities.
- A narrow and well-defined objective, such as to provide investment opportunities for investors by passing on risks and rewards associated with the assets of the structured entity to investors.
- Insufficient equity to permit the structured entity to finance its activities without subordinated financial support.
- Financing in the form of multiple contractually linked instruments to investors that create concentrations of credit or other risks (tranches).

The Scheme has determined that some of its investments in pooled funds and in collective investments (funds) are investments in unconsolidated structured entities. Disclosure of these investments has been made in Note 31 to the Annual Financial Statements. The objectives include achieving medium to long-term capital growth and the investment strategy does not include the use of leverage.

These funds are managed by independent asset managers who apply various investment strategies to accomplish their respective investment objectives.

The change in fair value of each fund is included in the Statement of Comprehensive Income in 'Net fair value gains/(losses) on financial assets at fair value through profit or loss'.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS

for the year ended 31 December 2017

R'000	2017	2016
1 Accounting policies		
The accounting policies of the Scheme are set out on pages 105 to 113.		
2 Financial assets at fair value through profit or loss		
The Scheme's financial assets at fair value through profit or loss are summarised by measurement classes as follows:		
Current assets	**14 005 644**	12 211 677
– Offshore bonds	**1 463 064**	1 245 709
– Equities	**3 378 331**	2 049 834
– Yield-enhanced bonds	**3 721 190**	3 413 740
– Inflation-linked bonds	**792 666**	610 476
– Money market instruments	**4 268 369**	4 891 918
– Listed property investments	**382 024**	–
	14 005 644	12 211 677
Reconciliation of the balance at the beginning of the year to the balance at the end of the year:		
At the beginning of the year	**12 211 677**	11 399 332
Acquisitions	**2 953 775**	1 922 170
Disposals	**(1 571 646)**	(1 127 159)
Net gains on revaluation of financial assets at fair value through profit or loss (Note 22)	**411 838**	17 334
At the end of the year	**14 005 644**	12 211 677
A register of investments is available for inspection at the registered office of the Scheme.		
3 Trade and other receivables		
Insurance receivables		
Contribution receivables	**751 192**	1 629 627
Contributions outstanding	**762 685**	1 639 386
Less: Provision for impairment	**(11 493)**	(9 759)
Member and service provider claims receivables	**94 025**	84 190
Amount due	**361 566**	341 473
Less: Provision for impairment	**(267 541)**	(257 283)
Other risk transfer arrangements	**11 796**	24 426
Recoveries due from other risk transfer arrangements	**3 660**	6 718
Share of outstanding claims provision (Note 6)	**8 136**	17 708
Broker fee receivables	**743**	1 084
Amounts due from brokers	**1 690**	1 948
Less: Provision for impairment	**(947)**	(864)
Other insurance receivables	**52 045**	138 781
Total receivables arising from insurance contracts	**909 801**	1 878 108

R'000	2017	2016

3 Trade and other receivables *continued*

Loans and receivables		
Balance due by related party	**18 616**	20 540
Discovery Third Party Recovery Services (Pty) Ltd (Note 25)	**18 616**	20 540
Sundry accounts receivable	**215 234**	157 670
Interest receivable	**4 014**	1 690
Total receivables arising from loans and receivables	**237 864**	179 900
	1 147 665	2 058 008

At 31 December 2017 the carrying amounts of Trade and other receivables approximate their fair values due to the short term maturities of these assets. Interest is not charged on overdue balances. The estimated future cash flow receipts have not been discounted as the effect would be immaterial.

4 Cash and cash equivalents – Personal Medical Savings Account trust assets

(Monies managed by the Scheme on behalf of members)

PERSONAL MEDICAL SAVINGS ACCOUNT TRUST PORTFOLIO		
(Managed by Aluwani Capital Partners (Pty) Ltd)		
Balance at beginning of the year	**2 071 391**	1 832 987
Net additional Investments	**55 608**	84 040
Interest Income	**177 819**	154 364
Balance at the end of the year	**2 304 818**	2 071 391
PERSONAL MEDICAL SAVINGS ACCOUNT TRUST PORTFOLIO		
(Managed by Taquanta Asset Managers (Pty) Ltd)		
Balance at beginning of the year	**2 071 281**	1 834 469
Net additional Investments	**61 143**	86 660
Interest Income	**171 907**	150 152
Balance at the end of the year	**2 304 331**	2 071 281
Total Personal Medical Savings Account trust assets	**4 609 149**	4 142 672

These funds represent members' Personal Medical Savings Account assets managed by the Scheme on behalf of its members. As required by Circular 38 of 2011 and Circular 5 of 2012 issued by the Council for Medical Schemes, these assets have been invested separately from the Scheme's assets. The difference between total Personal Medical Savings Account assets and Personal Medical Savings Account liabilities (Note 8) is reconciled monthly and arises from timing of cash flows to and from the portfolios. For the year under review the average rate earned on the Personal Medical Savings Account Trust assets was 8.33% (2016: 7.64%).

NOTES TO THE ANNUAL FINANCIAL STATEMENTS CONTINUED

for the year ended 31 December 2017

R'000	2017	2016
5 Cash and cash equivalents – medical scheme assets		
Current accounts	**3 891 038**	940 981
Money market instruments	**1 989 324**	1 456 807
	5 880 362	2 397 788
At 31 December 2017 cash and cash equivalents are carried at amortised cost, which approximates fair value.		
6 Outstanding claims provision		
Outstanding claims provision – not covered by risk transfer arrangements	**1 231 927**	1 103 686
Outstanding claims provision – covered by risk transfer arrangements (Note 3)	**8 136**	17 708
	1 240 063	1 121 394
Analysis of movement in outstanding claims		
Balance at beginning of the year	**1 121 394**	985 087
Payments in respect of prior year	**(1 117 213)**	(951 858)
Over provision in prior year (Note 11)	**4 181**	33 229
Outstanding claims provision raised in current year	**1 235 882**	1 088 165
Not covered by risk transfer arrangements	**1 227 746**	1 070 457
Covered by risk transfer arrangements (Note 3)	**8 136**	17 708
Balance at end of the year	**1 240 063**	1 121 394
Analysis of outstanding claims provision		
Estimated gross claims	**1 323 263**	1 192 494
Less:		
Estimated recoveries from savings plan accounts (Note 8)	**(83 200)**	(71 100)
Balance at end of the year	**1 240 063**	1 121 394

R'000	2017	2016
7 Derivative financial instruments		
Financial assets held at fair value through profit or loss		
Current assets		
– Derivative financial instruments	**85 857**	54 760
Financial liabilities held at fair value through profit or loss		
Current liabilities		
– Derivative financial instruments	**(86 445)**	(4 376)
Derivative financial (liability)/asset at the end of the year	**(588)**	50 384
Reconciliation of the balance at beginning of the year to the balance at the end of the year:		
Derivative financial asset/(liability) at the beginning of the year	**50 384**	(65 210)
Net realised gain on derivative financial instruments (Note 27.4)	**(89 802)**	(131 351)
Realised gains on derivative financial instruments	**(91 869)**	(136 710)
– Equity portfolio derivatives	**–**	(693)
– Zero-cost currency collars	**(91 869)**	(136 017)
Realised losses on derivative financial instruments	**2 067**	5 359
– Bond portfolio derivatives	**2 067**	3 719
– Zero-cost currency collars	**–**	1 640
Net fair value gain on derivative financial instruments (Note 22)	**38 830**	246 944
Gains on revaluation of derivative financial instruments to fair value	**179 148**	255 039
– Equity portfolio derivatives	**–**	9 138
– Zero-cost equity collars	**–**	91 072
– Zero-cost currency collars	**174 851**	154 829
– Bond portfolio derivatives	**4 297**	–
Losses on revaluation of derivative financial instruments to fair value	**(140 318)**	(8 095)
– Zero-cost equity collars	**(138 330)**	–
– Bond portfolio derivatives	**(1 988)**	(8 095)
Derivative financial (liability)/asset at the end of the year	**(588)**	50 384

Derivative Instruments

The Trustees approved a strategy to protect the value of the Scheme's investments by entering into zero-cost equity collars which protects the Scheme's equity portfolios against a fall in equity markets and zero-cost currency collars to protect the Scheme's offshore Dollar denominated bond portfolios against Rand appreciation.

The Scheme's equity managers entered into All Shareholder Index (ALSI) and SWIX 40 futures contracts to generate an equity-related return on cash held in the equity portfolios.

The Scheme's bond managers entered into bond futures to hedge the bond portfolios and provide protection against market risk.

Details of the Scheme's derivatives and the impact of these instruments on investment return are set out in the Financial Risk Management Report (Note 31).

NOTES TO THE ANNUAL FINANCIAL STATEMENTS CONTINUED

for the year ended 31 December 2017

R'000	2017	2016
8 Personal Medical Savings Account trust liabilities		
(Personal Medical Savings Account trust monies managed by the Scheme on behalf of its members)		
Balance on Personal Medical Savings Accounts at the beginning of the year	**4 204 043**	3 736 659
Add:		
Personal Medical Savings Accounts contributions received or receivable	**11 008 711**	10 429 814
For the current year (Note 10)	**11 008 711**	10 429 814
Interest on Personal Medical Savings Accounts (Note 24)	**367 238**	287 923
Transfers received from other medical schemes	**31 784**	13 691
Less:		
Claims paid to or on behalf of members (Note 11)	**(10 602 298)**	(9 942 225)
Refunds on death or resignation	**(352 845)**	(321 819)
Balance due to members on Personal Medical Savings Accounts held in trust at the end of the year	**4 656 633**	4 204 043

It is estimated that claims to be paid out of members' Personal Medical Savings Accounts in respect of claims incurred in 2017 but not reported will amount to approximately R83 200 000 (2016: R71 100 056) (Note 6).

As at 31 December 2017 the carrying amount of the members' Personal Medical Savings Accounts were deemed to be equal to their fair values, which is the amount payable on demand. The amounts were not discounted, due to the demand feature.

Interest is allocated on these Personal Medical Savings Account balances monthly in accordance with Circular 38 of 2011 and Circular 5 of 2012 issued by the Council for Medical Schemes. The Scheme does not charge interest on negative (overdrawn) Personal Medical Savings Account balances.

R'000	2017	2016
9 Trade and other payables		
Insurance payables		
Contributions received in advance	**1 851 573**	137 260
Contribution refunds due to employers	**1 110**	1 804
Reported claims not yet paid	**562 086**	548 257
Balance at the beginning of the year	**548 257**	506 752
Net movement for the year	**13 829**	41 505
Broker fee creditors	**111 819**	97 234
Accredited brokers	**111 819**	97 234
Total liabilities arising from insurance contracts	**2 526 588**	784 555
Financial liabilities		
Balance due to related parties	**513 571**	469 924
Discovery Health (Pty) Ltd (Note 25)	**513 571**	469 924
Unallocated funds	**8 943**	2 438
Total accruals	**16 416**	49 328
General accruals	**16 317**	49 268
Leave pay provision	**99**	60
Total arising from financial liabilities	**538 930**	521 690
	3 065 518	1 306 245

At 31 December 2017 the carrying amounts of insurance and other payables approximate their fair values due to the short term maturities of these liabilities.

R'000	2017	2016

10 Risk contribution income

Gross contributions per registered Scheme rules	**59 710 735**	54 056 212
Less:		
Personal Medical Savings Account contributions (Note 8)	**(11 008 711)**	(10 429 814)
	48 702 024	43 626 398

11 Net claims incurred

Current year claims per registered Scheme rules	**50 855 045**	46 578 250
Claims not covered by risk transfer arrangements	**50 448 462**	46 227 327
Claims covered by risk transfer arrangements (Note 13)	**406 583**	350 923
Movement in outstanding claims provision	**118 670**	136 307
Over provision in prior year (Note 6)	**(4 181)**	(33 229)
Adjustment for current year	**122 851**	169 536
	50 973 715	46 714 557
Less:		
Claims charged to members' Personal Medical Savings Accounts (Note 8)	**(10 602 298)**	(9 942 225)
Claims incurred	**40 371 417**	36 772 332
Third party claim recoveries	**(143 360)**	(159 122)
	40 228 057	36 613 210

Risk transfer arrangements

During 2017 the Scheme had six (2016: six) risk transfer arrangements in place. The methodologies used to determine the claims covered by these arrangements are set out below.

- **Risk transfer arrangement covering in-hospital and out-of-hospital benefits for certain members on the KeyCare Plus and KeyCare Access plans.**

  The claims experience for members on the KeyCare Plus and KeyCare Access plans for the 2017 benefit year that were not part of this risk transfer agreement was used as the basis for determining the claims under this arrangement. These claim amounts are adjusted to include a provision for outstanding claims and then converted to a per life per month (PLPM) rate using the membership on the KeyCare Plus and KeyCare Access plans.

  In order to determine the value of claims under this arrangement, the average 2017 PLPM rate is multiplied by the lives exposure for this arrangement's membership.

- **Risk transfer arrangement providing optometry services to members on the KeyCare Plus and KeyCare Access plans.**

  An analysis as to the expected costs of optometry benefits using the experience from other Scheme plans was conducted. These claim amounts are adjusted to include a provision for outstanding claims and converted to a PLPM rate. Generally the claims experience on KeyCare Plus and KeyCare Access is different to that of other Scheme plans as KeyCare Plus and KeyCare Access is aimed at a specific target market and the benefits are restricted. To allow for this, the overall PLPM is adjusted by the ratio of KeyCare Plus and KeyCare Access claims experience to the other plans offered by the Scheme. The value of claims under this arrangement is determined by multiplying the PLPM rate by the lives exposure for KeyCare Plus and KeyCare Access.

- **Risk transfer arrangement providing dentistry services to members on the KeyCare Plus and KeyCare Access plans.**

  The cost of the group of dental procedure codes was isolated. Using claims data linked to this group, the overall PLPM cost of dental services on all plans excluding KeyCare Plus and KeyCare Access was estimated. These claim amounts are adjusted to include a provision for outstanding claims. Generally, the claims experience on KeyCare Plus and KeyCare Access is different to that of other Scheme plans as KeyCare Plus and KeyCare Access is aimed at a specific target market and the benefits are restricted. To allow for this, the overall PLPM is adjusted by the ratio of KeyCare Plus and KeyCare Access claims experience to the other benefit plans offered by the Scheme. The value of claims under this arrangement is determined by multiplying the PLPM rate by the lives exposure for KeyCare Plus and KeyCare Access.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS CONTINUED

for the year ended 31 December 2017

11 Net claims incurred *continued*

- **Risk transfer arrangement covering treatment for Executive and Comprehensive Plan members diagnosed with diabetes (type I and II).**

  For their diabetes-related treatment, members have a choice of using the managed care organisation under this risk transfer arrangement or not. As the risk profile of the two groups of members are similar, the claims experience of the Executive and Comprehensive Plan members who have not elected to use this provider was used to estimate the members' fee-for-service cost for those who have elected to use this provider.

  As no underlying fee-for-service data is available, the cost of providing the capitated services was estimated as follows:

  - PLPM estimates were calculated for consultations, procedures, medication and hospital admissions to the extent that these services were covered under this risk transfer arrangement for the Executive and Comprehensive Plan members who have not elected this provider.
  - The expected fee-for-service cost was calculated by multiplying the calculated PLPM costs by the number of members exposed for the period on this programme.

- **Risk transfer arrangement providing acute medication dispensing services to members on the Smart plan.**

  The Scheme contracted with two providers as Designated Service Providers (DSPs) to provide acute medication dispensing services for Smart plan members. The Scheme remunerates the DSPs at the contracted monthly capitation fee.

  The estimated claims incurred under this arrangement is determined using the acute medicine claims experience for members not on the Smart plan and calculating a PLPM rate. The value of claims under this arrangement is determined by multiplying the PLPM rate by the lives exposure for Smart Plan members.

R'000	2017	2016

12 Accredited managed healthcare services (no risk transfer)

The accredited managed healthcare services (no risk transfer) have been grouped into the following categories of services.

	2017	2016
Discovery Health (Pty) Ltd		
Active Disease Risk Management Services and Disease Risk Management Support Services	**494 155**	453 235
Hospital Benefit Management Services	**458 289**	420 400
Managed Care Network Management Services and Risk Management Services	**426 180**	390 788
Pharmacy Benefit Management Services	**155 687**	142 844
	1 534 311	1 407 267

13 Net profit/(loss) on risk transfer arrangements

The Scheme operated the following risk transfer arrangements during the year:

	2017	2016
Risk transfer arrangement fees	**(392 023)**	(366 344)
Recoveries under risk transfer arrangements (Note 11)	**406 583**	350 923
	14 560	(15 421)

R'000	2017	2016

14 Broker service fees

R'000	2017	2016
Brokers' fees	**1 214 205**	1 101 648
	1 214 205	1 101 648

15 Other operating expenses

R'000	2017	2016
Association fees	**1 359**	1 616
Audit fees	**9 066**	11 594
Audit services for the year ended 2017	**1 759**	–
Audit services for the year ended 2016	**3 084**	1 661
Audit services for the year ended 2015	**–**	2 462
Other services	**4 223**	7 471
Audit Committee and Risk Committee fees (Note 16)	**2 001**	1 755
Audit Committee	**1 458**	1 167
Risk Committee	**543**	588
Bank charges	**9 817**	10 681
Clinical Governance Committee fees	**662**	375
Council for Medical Schemes	**44 103**	40 631
Debt collecting fees	**2 789**	3 850
Dispute Committee fees	**636**	871
Fidelity Guarantee Insurance	**285**	226
General meeting costs	**9 989**	8 986
Investment Committee fees	**701**	323
Investment reporting fees	**3 669**	3 416
Legal fees	**476**	816
Net impairment losses (Note 17)	**87 604**	75 167
Non-Healthcare Expenses Committee Fees	**131**	–
Nomination Committee fees (Note 18)	**285**	571
Other expenses	**25 951**	25 499
Principal Officer fees – Remuneration	**5 128**	5 706
Principal Officer fees – Unvested long term employee benefit	**1 803**	1 438
Printing, postage and stationery	**839**	735
Product Committee fees	**73**	–
Professional fees	**10 517**	9 548
Remuneration Committee fees	**106**	109
Scheme Office costs	**5 658**	6 314
Staff costs (Note 19)	**28 723**	20 127
Sundry amounts written off	**100**	293
Stakeholder Relations and Ethics Committee* fees	**156**	129
Trustees' remuneration and consideration expenses (Note 20)	**7 834**	5 430
	260 461	236 206

* *Previously Stakeholder Relations Committee.*

NOTES TO THE ANNUAL FINANCIAL STATEMENTS CONTINUED

for the year ended 31 December 2017

R'000	2017	2016
16 Audit Committee and Risk Committee fees		
Audit Committee fees	**1 458**	1 167
B Stott – Independent member (Chairperson)	**818**	603
S Green – Independent member	**213**	158
D King – Independent member	**–**	64
S Ludolph – Independent member	**225**	163
P Maphumulo – Independent member	**202**	179
Risk Committee fees	**543**	588
B Stott – Independent member (Chairperson)	**156**	161
S Green – Independent member	**125**	128
D King – Independent member	**–**	57
S Ludolph – Independent member	**137**	113
P Maphumulo – Independent member	**125**	129
	2 001	1 755

These are payments to independent members of the Audit and Risk Committees. These members are not Trustees of the Scheme. Amounts paid to Trustee members of these Committees are disclosed in Note 20.

R'000	2017	2016
17 Net impairment losses		
Insurance and other receivables		
Contributions that are not collectable	1 734	126
Movement in provision	1 734	126
Members' and service providers' portions that are not recoverable	85 688	76 422
Movement in provision	85 688	76 422
Amounts due by brokers that are not recoverable	82	81
Movement in provision	82	81
Payables/receivables written off	111	(1 462)
Less:		
Previously written off receivables recovered	(11)	–
	87 604	75 167
18 Other Committee fees		
Nomination Committee fees		
P Goss – Independent member (Chairperson)	89	201
T Wixley – Independent member	89	184
R Shough – Independent member	107	186
	285	571
19 Staff costs		
Salaries and bonuses	23 099	16 466
Pension costs – defined contribution plans	1 497	1 160
Medical and other benefits	846	699
Long term employee benefits service cost	3 242	1 563
Increase in leave pay accrual	39	239
	28 723	20 127
Number of employees at 31 December	12	11

NOTES TO THE ANNUAL FINANCIAL STATEMENTS CONTINUED

for the year ended 31 December 2017

20 Trustees' remuneration and consideration expenses

The following table records the remuneration and consideration paid to Trustees during the year:

		Committee fees					Committee fees				
31 December 2017	**Services as Trustee R'000**	**Audit Committee R'000**	**Risk Committee R'000**	**Investment Committee R'000**	**Clinical Governance Committee R'000**	**Product Committee R'000**	**Non-healthcare Expenditure Committee R'000**	**Remuneration Committee R'000**	**Stakeholder Relations and Ethics[1] Committee R'000**	**Trustee travel R'000**	**Total R'000**
N Morrison (Chairperson)	**625**	**90**	**51**	**222**	**–**	**11**	**136**	**38**	**51**	**–**	**1 224**
M van der Nest SC	**573**	**–**	**–**	**–**	**–**	**–**	**–**	**49**	**66**	**1**	**689**
G Waugh	**180**	**67**	**45**	**–**	**–**	**56**	**92**	**–**	**–**	**7**	**447**
D Moodley	**486**	**–**	**–**	**222**	**241**	**114**	**–**	**–**	**114**	**18**	**1 195**
D King	**488**	**–**	**–**	**–**	**–**	**–**	**136**	**76**	**114**	**90**	**904**
D Naidoo	**521**	**210**	**139**	**247**	**–**	**113**	**155**	**–**	**–**	**–**	**1 385**
J Adams SC	**231**	**115**	**84**	**–**	**115**	**–**	**–**	**–**	**–**	**–**	**545**
J Butler SC	**248**	**–**	**–**	**–**	**–**	**–**	**54**	**43**	**85**	**36**	**466**
J Human	**202**	**78**	**63**	**104**	**–**	**69**	**–**	**–**	**–**	**53**	**569**
S Brynard	**202**	**–**	**–**	**–**	**–**	**63**	**–**	**38**	**63**	**44**	**410**
Total	**3 756**	**560**	**382**	**795**	**356**	**426**	**573**	**244**	**493**	**249**	**7 834**

		Committee fees					Committee fees				
31 December 2016	Services as Trustee R'000	Audit Committee R'000	Risk Committee R'000	Investment Committee R'000	Clinical Governance Committee R'000	Product Committee R'000	Non-healthcare Expenditure Committee R'000	Remuneration Committee R'000	Stakeholder Relations Committee R'000	Trustee travel R'000	Total R'000
M van der Nest SC (Chairperson)	813	–	–	–	–	–	–	66	104	22	1 005
P Maserumule	206	–	–	95	–	–	–	–	35	–	336
N Graves SC	247	–	–	46	–	35	64	33	–	13	438
Z van der Spuy	260	–	–	–	71	45	–	–	–	69	445
G Waugh	441	129	132	–	–	121	102	–	–	–	925
D Moodley	207	5	–	56	86	52	–	–	–	24	430
N Morrison	220	66	71	56	–	5	32	–	–	2	452
D King	206	–	–	–	–	–	41	33	45	59	384
D Naidoo	469	127	133	132	–	52	91	–	–	11	1 015
Total	**3 069**	**327**	**336**	**385**	**157**	**310**	**330**	**132**	**184**	**200**	**5 430**

1 *At the end of 2017, the Committee adopted an expanded social and ethics governance mandate and new name of Stakeholder Relations and Ethics Committee (previously Stakeholder Relations Committee).*

NOTES TO THE ANNUAL FINANCIAL STATEMENTS CONTINUED

for the year ended 31 December 2017

R'000	2017	2016
21 Investment income		
Financial assets at fair value through profit or loss:	**1 383 773**	1 200 503
Dividend income	**84 062**	50 993
Interest income	**1 299 711**	1 149 510
Cash and cash equivalents interest income	**49 414**	56 976
Investment income per Statement of Comprehensive Income	**1 433 187**	1 257 479
The Scheme's total interest income is summarised below.		
Financial assets not at fair value through profit or loss:		
Cash and cash equivalents interest income	**49 414**	56 976
Financial assets at fair value through profit or loss:		
Interest income	**1 299 711**	1 149 510
Total interest income	**1 349 125**	1 206 486
22 Net gains on financial assets at fair value through profit or loss		
Net fair value gains on financial assets at fair value through profit or loss (Note 2):	**411 838**	17 334
Fair value gains on financial assets at fair value through profit or loss:	**529 340**	180 725
– Equities	**435 490**	126 213
– Money market instruments	**27 814**	598
– Inflation-linked bonds	**–**	5 574
– Listed property investments	**29 476**	–
– Yield-enhanced bonds	**36 560**	48 340
Fair value losses on financial assets at fair value through profit or loss:	**(117 502)**	(163 391)
– Equities	**–**	(64 229)
– Money market instruments	**–**	(2 759)
– Offshore bonds	**(96 851)**	(88 161)
– Inflation-linked bonds	**(14 592)**	(7 845)
– Yield-enhanced bonds	**(6 059)**	(397)
Net fair value gains on derivative financial instruments (Note 7):	**38 830**	246 944
Fair value gains on derivative financial instruments:	**179 148**	255 039
Fair value losses on derivative financial instruments:	**(140 318)**	(8 095)
Net fair value gains on cash and cash equivalents	**8 085**	–
	458 753	264 278

R'000	2017	2016
23 Sundry income		
Prescribed amounts written back	**24 951**	2 433
(Reversal of stale cheques written back)/Stale cheques written back	**(23 205)**	(74)
	1 746	2 359
24 Interest paid		
Financial assets not at fair value through profit or loss:		
Interest on Personal Medical Savings Accounts (Note 8)	**367 238**	287 923
Interest paid to Administrator (Note 25)	**–**	2 119
	367 238	290 042

25 Related party transactions

The Scheme is governed by the Board of Trustees who are elected by the members of the Scheme.

Key management personnel and their close family members

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Scheme. Key management personnel include the non-executive Board of Trustees and the Executive Officers of the Scheme. The disclosure deals with full-time Executive Officers who are compensated on a salary basis, and non-executive Board of Trustees who are compensated on a fee basis.

Close family members include close family members of the Board of Trustees and Executive Officers of the Scheme.

Parties with significant influence over the Scheme

Administrator

Discovery Health (Pty) Ltd has significant influence over the Scheme, as Discovery Health (Pty) Ltd participates in the Scheme's financial and operating policy decisions, but does not control the Scheme. Discovery Health (Pty) Ltd provides administration, managed care services, broker services and wellness programmes.

Third party collection services are provided through Discovery Third Party Recovery Services (Pty) Ltd, specialist pharmaceutical services through Southern RX Distributors (Pty) Ltd and home-based care through Grove Nursing Services (Pty) Ltd, all wholly-owned subsidiaries of Discovery Health (Pty) Ltd.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS CONTINUED

for the year ended 31 December 2017

25 Related party transactions *continued*

Transactions with related parties

The following provides the total amount in respect of transactions, which have been entered into with related parties for the relevant financial year.

Transactions with key management personnel and their close family members which includes Trustees and Executive Officers:

R'000	2017	2016
Statement of Comprehensive Income transactions		
Compensation		
Short term employee benefits	**(35 683)**	(26 381)
Unvested long term employee benefit	**(5 045)**	(3 000)
Contributions and claims		
Gross contributions received	**761**	724
Claims paid from the Scheme	**(454)**	(281)
Claims paid from the Personal Medical Savings Account	**(182)**	(163)
Interest paid on Personal Medical Savings Accounts	**(1)**	(1)
Statement of Financial Position transactions		
Long term employee benefit plan asset	**4 417**	5 614
Plan asset	**8 981**	9 738
Plan liability	**(4 564)**	(4 124)
Contribution debtors	**57**	35
Personal Medical Savings Account balances	**(12)**	(28)

The terms and conditions of the related party transactions were as follows:

Transactions	Nature of transactions and their terms and conditions
Compensation	This constitutes remuneration and consideration paid to Trustees and Executive Officers, short term employee benefits and unvested long term employee benefits.
Contributions received	This constitutes the contributions paid by the related party as a member of the Scheme, in their individual capacity. All contributions were on the same terms as applicable to other members.
Claims incurred	This constitutes amounts claimed by the related parties, in their individual capacity as members of the Scheme. All claims were paid out in terms of the rules of the Scheme, as applicable to other members.
Contribution debtors	This constitutes outstanding contributions receivable. The amounts are due immediately. No impairment provisions have been raised on these amounts.
Personal Medical Savings Account balances	The amounts owing to the related parties relate to Personal Medical Savings Account balances to which the parties have a right. In line with the terms applied to other members, the balances earn monthly interest on an accrual basis, at interest rates aligned to the rates earned within the Personal Medical Savings Account Trust Portfolios. The amounts are all current and would need to be payable on demand as applicable to other members.

R'000	2017	2016
25 Related party transactions *continued*		
Transactions with entities that have significant influence over the Scheme		
Discovery Health (Pty) Ltd – Administrator		
Statement of Comprehensive Income transactions		
Administration fees paid	**(4 511 596)**	(4 150 194)
Interest paid on monthly balances (Note 24)	**–**	(2 119)
Statement of Financial Position transactions		
Balance due to Discovery Health (Pty) Ltd (Note 9)*	**(384 681)**	(351 510)
Discovery Health (Pty) Ltd – Managed care organisation		
Statement of Comprehensive Income transactions		
Accredited managed healthcare services (no risk transfer) (Note 12)	**(1 534 311)**	(1 407 267)
Statement of Financial Position transactions		
Balance due to Discovery Health (Pty) Ltd at year end (Note 9)*	**(128 890)**	(118 414)
Discovery Health (Pty) Ltd – Brokers		
Statement of Comprehensive Income transactions		
Broker fees paid	**–**	(14 135)
Discovery Third Party Recovery Services (Pty) Ltd		
Statement of Comprehensive Income transactions		
Third party collection fees	**(21 827)**	(22 030)
Statement of Financial Position transactions		
Balance due to the Scheme at year end (Note 3)	**18 616**	20 540
Southern RX Distributors (Pty) Ltd		
Statement of Comprehensive Income transactions		
Claims paid from the Scheme	**(205 254)**	(145 325)
Statement of Financial Position transactions		
Claims due to provider	**(1 916)**	(1 837)
Discovery Health (Pty) Ltd – Wellness experiences		
Statement of Comprehensive Income transactions		
Claims paid from the Scheme	**(16 489)**	(9 541)
Statement of Financial Position transactions		
Claims due to provider	**(2)**	(93)
Grove Nursing Services (Pty) Ltd		
Statement of Comprehensive Income transactions		
Claims paid from the Scheme	**(7 862)**	(9 677)
Statement of Financial Position transactions		
Claims (due to)/ from provider	**(153)**	(35)

** Total amount due to Discovery Health (Pty) Ltd for the current financial year is R514 million (2016: R 470 million), disclosed in Note 9.*

NOTES TO THE ANNUAL FINANCIAL STATEMENTS CONTINUED

for the year ended 31 December 2017

25 Related party transactions *continued*

Transactions with entities that have significant influence over the Scheme *continued*

The terms and conditions of the transactions with entities with significant influence over the Scheme were as follows:

Administration agreement

The administration agreement is in terms of the Rules of the Scheme and in accordance with instructions given by the Board of Trustees. The agreement was effective from January 2015 for a three year period which ended on 31 December 2017. A new agreement for a five year period has been entered into effective from 1 January 2018. The Scheme and the Administrator shall be entitled to terminate the agreement by giving the other party at least 12 calendar months' written notice. Effective from January 2017, the parties agreed that no interest would be levied on amounts owing.

The administration fees are an all-inclusive fee, calculated on a per member per month basis. The total expense for administration cost changes in line with membership growth and inflation.

The main categories of service provided can be broken down as follows:

- Member and provider servicing;
- Marketing and advertising;
- Financial and actuarial services; and
- Governance, risk, compliance and internal audit.

Managed healthcare agreement

Managed healthcare means clinical and financial risk assessment and management of healthcare, with a view to facilitating appropriateness and cost-effectiveness of relevant health services within the constraints of what is affordable, through the use of rules-based and clinical management-based programmes.

The Scheme has contracted with the Administrator to provide accredited managed healthcare services (no risk transfer). These services include bill review, specialist and hospital referrals, case management, disease management (where healthcare benefits are not included in the contract), peer review, claims audits and statistical analysis.

This agreement is in accordance with instructions given by the Board of Trustees. The agreement was effective from January 2015 for a three year period which ended on 31 December 2017. A new agreement for a five year period has been entered into effective from 1 January 2018. The Scheme and Discovery Health (Pty) Ltd shall be entitled to terminate the agreement by giving the other party at least 12 calendar months' written notice. Effective from January 2017, the parties agreed that no interest would be levied on amounts owing.

The accredited services provided by the managed care organisation include:

- Active disease risk management services and disease risk management support services;
- Hospital benefit management services;
- Managed care network management services and risk managed services; and
- Pharmacy benefit management services.

25 Related party transactions *continued*

Third party collection services

The Scheme has contracted with Discovery Third Party Recovery Services (Pty) Ltd, a wholly owned subsidiary of Discovery Health (Pty) Ltd, to manage the identification and collection of third party recoveries from the Road Accident Fund and the Compensation for Occupational Injuries and Diseases. The Scheme has sold all Road Accident Fund claims incurred by the Scheme during the period 1 January 2017 to 31 December 2017 to Discovery Third Party Recovery Services (Pty) Ltd for the amount of R15 million (2016: R14 million).

Specialist Pharmaceutical Services

The Scheme is contracted with Southern RX Pharmacy, a wholly owned subsidiary of Discovery Health (Pty) Ltd to provide specialist pharmaceutical services to members of the Scheme.

Wellness experiences

Discovery Health (Pty) Ltd provides wellness experiences through lifestyle and health assessments to Scheme members with the use of information technology and on-site medical evaluations of key health indicators.

Home-based nursing services

The Scheme is contracted with Grove Nursing services also known as Discovery HomeCare services, a wholly owned subsidiary of Discovery Health (Pty) Ltd, to provide home-based care to members of the Scheme in the comfort of their home.

Broker service fees

The Scheme contracted with Discovery Health (Pty) Ltd to provide broker services directly to the consumer. The amounts were determined and paid based on the terms and conditions applicable to other brokers. This agreement was terminated during 2016 and no amounts were paid to Discovery Health (Pty) Ltd during the year under review.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS CONTINUED

for the year ended 31 December 2017

26 Surplus/(deficit) from operations per benefit plan

2017	Executive R'000	Classic Comp. R'000	Classic Comp. Zero MSA R'000	Classic Core R'000	Classic Saver R'000	Classic Priority R'000	Essential Comp. R'000	Essential Saver R'000	Essential Core R'000
Risk contribution income	**925 588**	**10 127 603**	**60 524**	**1 999 904**	**10 690 234**	**4 470 174**	**1 008 291**	**3 495 369**	**1 193 011**
Net claims incurred	(1 193 107)	(10 161 581)	(57 558)	(1 457 631)	(7 977 065)	(3 565 076)	(861 544)	(2 156 717)	(784 339)
Claims incurred	(1 194 229)	(10 177 005)	(57 652)	(1 463 164)	(8 008 290)	(3 575 217)	(863 324)	(2 169 553)	(788 666)
Third party claim recoveries	1 122	15 424	94	5 533	31 225	10 141	1 780	12 836	4 327
Net income/(expense) on risk transfer arrangements	(572)	(12 956)	(199)	–	–	–	(1 995)	–	–
Risk transfer arrangement fees	(10 080)	(138 895)	(1 169)	–	–	–	(14 420)	–	–
Recoveries from risk transfer arrangements	9 508	125 939	970	–	–	–	12 425	–	–
Accredited managed healthcare services (no risk transfer)	(12 446)	(171 435)	(1 038)	(59 452)	(335 991)	(111 187)	(19 830)	(133 479)	(44 975)
Relevant healthcare expenditure	**(1 206 125)**	**(10 345 972)**	**(58 795)**	**(1 517 083)**	**(8 313 056)**	**(3 676 263)**	**(883 369)**	**(2 290 196)**	**(829 314)**
Gross healthcare result	**(280 537)**	**(218 369)**	**1 729**	**482 821**	**2 377 178**	**793 911**	**124 922**	**1 205 173**	**363 697**
Broker service fees	(11 547)	(161 712)	(960)	(46 371)	(299 770)	(105 070)	(18 837)	(105 091)	(32 258)
Expenses for administration	(40 220)	(554 028)	(3 356)	(192 226)	(1 085 766)	(359 412)	(64 086)	(431 333)	(145 337)
Other operating expenses	(2 114)	(29 123)	(176)	(10 092)	(57 056)	(18 884)	(3 369)	(22 649)	(7 631)
Net healthcare result	**(334 418)**	**(963 232)**	**(2 763)**	**234 132**	**934 586**	**310 545**	**38 630**	**646 100**	**178 471**
Investment income	11 628	160 198	971	55 540	313 841	103 886	18 534	124 636	41 999
Net fair value gains on financial assets at fair value through profit or loss	3 669	50 511	309	17 733	100 334	32 929	5 840	40 376	13 594
Sundry income	11	153	–	66	375	108	20	180	61
Other income	**15 308**	**210 862**	**1 280**	**73 339**	**414 550**	**136 923**	**24 394**	**165 192**	**55 654**
Expenses for asset management services rendered	(359)	(4 961)	(31)	(1 723)	(9 729)	(3 219)	(572)	(3 864)	(1 303)
Interest paid	(4 536)	(62 479)	–	–	(122 291)	(40 501)	(7 228)	(48 529)	–
Other expenditure	**(4 895)**	**(67 440)**	**(31)**	**(1 723)**	**(132 020)**	**(43 720)**	**(7 800)**	**(52 393)**	**(1 303)**
Net surplus/(deficit) for the year	**(324 005)**	**(819 810)**	**(1 514)**	**305 748**	**1 217 116**	**403 748**	**55 224**	**758 899**	**232 822**

26 Surplus/(deficit) from operations per benefit plan *continued*

2017	Essential Priority R'000	Coastal Saver R'000	Coastal Core R'000	KeyCare Plus R'000	KeyCare Core R'000	KeyCare Access R'000	Classic Smart R'000	Essential Smart R'000	Total R'000
Risk contribution income	**296 693**	**6 144 961**	**2 711 384**	**4 620 954**	**239 426**	**61 615**	**528 258**	**128 035**	**48 702 024**
Net claims incurred	(187 054)	(4 849 658)	(2 191 449)	(4 267 578)	(150 219)	(25 603)	(297 584)	(44 294)	(40 228 057)
Claims incurred	(187 801)	(4 869 552)	(2 200 521)	(4 293 000)	(151 800)	(26 132)	(299 905)	(45 606)	(40 371 417)
Third party claim recoveries	747	19 894	9 072	25 422	1 581	529	2 321	1 312	143 360
Net income/(expense) on risk transfer arrangements	–	–	–	32 924	–	(267)	(2 375)	–	14 560
Risk transfer arrangement fees	–	–	–	(215 369)	–	(2 954)	(9 136)	–	(392 023)
Recoveries from risk transfer arrangements	–	–	–	248 293	–	2 687	6 761	–	406 583
Accredited managed healthcare services (no risk transfer)	(8 146)	(216 145)	(98 103)	(268 094)	(16 434)	(5 511)	(22 359)	(9 686)	(1 534 311)
Relevant healthcare expenditure	**(195 200)**	**(5 065 803)**	**(2 289 552)**	**(4 502 748)**	**(166 653)**	**(31 381)**	**(322 318)**	**(53 980)**	**(41 747 808)**
Gross healthcare result	**101 493**	**1 079 158**	**421 832**	**118 206**	**72 773**	**30 234**	**205 940**	**74 055**	**6 954 216**
Broker service fees	(7 252)	(184 488)	(72 897)	(139 717)	(7 303)	(1 937)	(14 980)	(4 015)	(1 214 205)
Expenses for administration	(26 325)	(698 495)	(317 029)	(468 790)	(15 445)	(6 213)	(72 250)	(31 285)	(4 511 596)
Other operating expenses	(1 384)	(36 705)	(16 655)	(45 484)	(2 784)	(933)	(3 789)	(1 633)	(260 461)
Net healthcare result	**66 532**	**159 470**	**15 251**	**(535 785)**	**47 241**	**21 151**	**114 921**	**37 122**	**967 954**
Investment income	7 612	201 923	91 649	250 408	15 350	5 147	20 864	9 001	1 433 187
Net fair value gains on financial assets at fair value through profit or loss	2 418	64 268	29 191	80 559	4 957	1 669	6 969	3 427	458 753
Sundry income	8	225	103	324	22	7	42	41	1 746
Other income	**10 038**	**266 416**	**120 943**	**331 291**	**20 329**	**6 823**	**27 875**	**12 469**	**1 893 686**
Expenses for asset management services rendered	(237)	(6 260)	(2 842)	(7 760)	(476)	(159)	(650)	(283)	(44 428)
Interest paid	(2 967)	(78 707)	–	–	–	–	–	–	(367 238)
Other expenditure	**(3 204)**	**(84 967)**	**(2 842)**	**(7 760)**	**(476)**	**(159)**	**(650)**	**(283)**	**(411 666)**
Net surplus/(deficit) for the year	**73 366**	**340 919**	**133 352**	**(212 254)**	**67 094**	**27 815**	**142 146**	**49 308**	**2 449 974**

NOTES TO THE ANNUAL FINANCIAL STATEMENTS CONTINUED

for the year ended 31 December 2017

26 Surplus/(deficit) from operations per benefit plan *continued*

2016	Executive R'000	Classic Comp. R'000	Classic Comp. Zero MSA R'000	Classic Core R'000	Classic Saver R'000	Classic Priority R'000	Essential Comp. R'000	Essential Saver R'000	Essential Core R'000
Risk contribution income	**875 516**	**9 802 065**	**51 050**	**1 857 849**	**9 115 477**	**4 202 272**	**1 014 102**	**2 885 453**	**1 013 633**
Net claims incurred	(1 157 978)	(9 709 842)	(47 899)	(1 340 447)	(6 784 281)	(3 384 976)	(833 849)	(1 805 622)	(660 685)
Claims incurred	(1 159 318)	(9 728 653)	(48 001)	(1 346 843)	(6 817 367)	(3 396 783)	(836 103)	(1 818 786)	(665 369)
Third party claim recoveries	1 340	18 811	102	6 396	33 086	11 807	2 254	13 164	4 684
Net income/(expense) on risk transfer arrangements	(2 425)	(35 647)	(320)	–	–	–	(4 161)	–	–
Risk transfer arrangement fees	(9 914)	(131 482)	(938)	–	–	–	(13 673)	–	–
Recoveries from risk transfer arrangements	7 489	95 835	618	–	–	–	9 512	–	–
Accredited managed healthcare services (no risk transfer)	(12 280)	(172 806)	(915)	(57 064)	(294 412)	(107 268)	(20 650)	(112 847)	(39 701)
Relevant healthcare expenditure	**(1 172 683)**	**(9 918 295)**	**(49 134)**	**(1 397 511)**	**(7 078 693)**	**(3 492 244)**	**(858 660)**	**(1 918 469)**	**(700 386)**
Gross healthcare result	**(297 167)**	**(116 230)**	**1 916**	**460 338**	**2 036 784**	**710 028**	**155 442**	**966 984**	**313 247**
Broker service fees	(11 360)	(165 057)	(828)	(42 828)	(259 350)	(102 255)	(20 642)	(86 194)	(26 669)
Expenses for administration	(39 938)	(562 224)	(2 975)	(185 567)	(957 550)	(348 811)	(67 157)	(366 937)	(129 091)
Other operating expenses	(2 063)	(28 989)	(153)	(9 580)	(49 421)	(18 009)	(3 469)	(18 938)	(6 662)
Net healthcare result	**(350 528)**	**(872 500)**	**(2 040)**	**222 363**	**770 463**	**240 953**	**64 174**	**494 915**	**150 825**
Investment income	10 968	154 294	818	50 982	263 050	95 799	18 438	100 903	35 499
Net fair value gains on financial assets at fair value through profit or loss	2 370	33 385	174	10 798	55 540	20 560	3 986	20 697	7 236
Sundry income	20	308	(1)	95	498	184	33	184	65
Other income	**13 358**	**187 987**	**991**	**61 875**	**319 088**	**116 543**	**22 457**	**121 784**	**42 800**
Expenses for asset management services rendered	(272)	(3 820)	(23)	(1 259)	(6 505)	(2 369)	(453)	(2 490)	(874)
Interest paid	(3 806)	(53 555)	–	(83)	(91 299)	(33 251)	(6 402)	(35 016)	(57)
Other expenditure	(4 078)	(57 375)	(23)	(1 342)	(97 804)	(35 620)	(6 855)	(37 506)	(931)
Net surplus/(deficit) for the year	**(341 248)**	**(741 888)**	**(1 072)**	**282 896**	**991 747**	**321 876**	**79 776**	**579 193**	**192 694**

26 Surplus/(deficit) from operations per benefit plan *continued*

2016	Essential Priority R'000	Coastal Saver R'000	Coastal Core R'000	KeyCare Plus R'000	KeyCare Core R'000	KeyCare Access R'000	KeyCare Smart R'000	Total R'000
Risk contribution income	**297 133**	**5 385 228**	**2 413 696**	**4 207 970**	**220 866**	**57 055**	**227 033**	**43 626 398**
Net claims incurred	(205 856)	(4 491 692)	(1 962 720)	(3 964 639)	(127 085)	(22 924)	(112 715)	(36 613 210)
Claims incurred	(206 777)	(4 514 656)	(1 973 413)	(3 993 633)	(128 916)	(23 551)	(114 163)	(36 772 332)
Third party claim recoveries	921	22 964	10 693	28 994	1 831	627	1 448	159 122
Net income/(expense) on risk transfer arrangements	–	–	–	31 190	–	(2 923)	(1 135)	(15 421)
Risk transfer arrangement fees	–	–	–	(204 582)	–	(2 923)	(2 832)	(366 344)
Recoveries from risk transfer arrangements	–	–	–	235 772	–	–	1 697	350 923
Accredited managed healthcare services (no risk transfer)	(8 360)	(204 472)	(94 660)	(250 933)	(15 471)	(5 423)	(10 005)	(1 407 267)
Relevant healthcare expenditure	**(214 216)**	**(4 696 164)**	**(2 057 380)**	**(4 184 382)**	**(142 556)**	**(31 270)**	**(123 855)**	**(38 035 898)**
Gross healthcare result	**82 917**	**689 064**	**356 316**	**23 588**	**78 310**	**25 785**	**103 178**	**5 590 500**
Broker service fees	(7 510)	(174 400)	(65 440)	(124 596)	(6 517)	(1 794)	(6 208)	(1 101 648)
Expenses for administration	(27 182)	(664 984)	(307 902)	(436 502)	(14 540)	(6 115)	(32 719)	(4 150 194)
Other operating expenses	(1 404)	(34 320)	(15 889)	(42 119)	(2 598)	(908)	(1 684)	(236 206)
Net healthcare result	**46 821**	**(184 640)**	**(32 915)**	**(579 629)**	**54 655**	**16 968**	**62 567**	**102 452**
Investment income	7 465	182 695	84 590	224 314	13 832	4 846	8 986	1 257 479
Net fair value losses on financial assets at fair value through profit or loss	1 604	38 516	17 766	46 306	2 820	1 013	1 507	264 278
Sundry income	13	343	158	411	25	10	13	2 359
Other income	**9 082**	**221 554**	**102 514**	**271 031**	**16 677**	**5 869**	**10 506**	**1 524 116**
Expenses for asset management services rendered	(184)	(4 516)	(2 090)	(5 540)	(342)	(119)	(220)	(31 076)
Interest paid	(2 591)	(63 409)	(143)	(380)	(23)	(11)	(16)	(290 042)
Other expenditure	**(2 775)**	**(67 925)**	**(2 233)**	**(5 920)**	**(365)**	**(130)**	**(236)**	**(321 118)**
Net surplus/(deficit) for the year	**53 128**	**(31 011)**	**67 366**	**(314 518)**	**70 967**	**22 707**	**72 837**	**1 305 450**

NOTES TO THE ANNUAL FINANCIAL STATEMENTS CONTINUED

for the year ended 31 December 2017

R'000	2017	2016
27 Cash flows from operations before working capital changes		
Net surplus for the year	**2 449 974**	1 305 450
Adjustments for:		
Impairment losses (Note 17)	**87 604**	75 167
Interest received (Note 21)	**(1 349 125)**	(1 206 486)
Dividend income (Note 21)	**(84 062)**	(50 993)
Interest paid (Note 24)	**367 238**	290 042
Unvested long term employee benefit	**5 045**	3 000
Net gains on financial assets at fair value through profit or loss (Note 22)	**(458 753)**	(264 278)
	1 017 921	151 902
Reconciliation of movements in the cash flow statement		
27.1 Increase/(decrease) in trade and other receivables	**822 739**	(500 589)
Opening balance	**2 058 008**	1 632 586
Closing balance (Note 3)	**(1 147 665)**	(2 058 008)
Impairment losses	**(87 604)**	(75 167)
27.2 Increase in trade and other payables	**1 759 273**	123 640
Opening balance	**(1 306 245)**	(1 182 605)
Closing balance (Note 9)	**3 065 518**	1 306 245
27.3 Purchases of financial instruments	**(2 953 775)**	(1 922 170)
Financial assets at Fair value (Note 2)	**(2 953 775)**	(1 922 170)
27.4 Proceeds from sale of financial instruments	**1 669 533**	1 258 510
Financial assets at Fair value (Note 2)	**1 571 646**	1 127 159
Money market instruments (Note 22)	**8 085**	–
Derivative financial instruments (Note 7)	**89 802**	131 351

28 Events after the reporting period

No significant events occurred between the reporting date and the date the financial statements were authorised for issue. During the year under review an amalgamation was confirmed with the University of the Witwatersrand, Johannesburg Staff Medical Aid Fund with an effective date of 1 January 2018. The detail of the amalgamation is set out in Note 29.

29 Amalgamations

University of the Witwatersrand, Johannesburg Staff Medical Aid Fund

An amalgamation between the Scheme and University of the Witwatersrand, Johannesburg Staff Medical Aid Fund (WitsMed) was confirmed and effective from 1 January 2018. The disclosures provided below have no effect on the current reporting period but have been provided to enable users to evaluate the nature and financial effect of the amalgamation that occurs after the end of the current reporting period.

WitsMed is a not-for-profit restricted medical scheme registered in terms of the Act. Membership of the Scheme is open to all current and retired employees of the University of the Witwatersrand, its subsidiaries and associates. Retired employees of subsidiaries and associates, which have been disposed of, may continue their membership if they so elect.

In terms of the Act, medical schemes do not have equity therefore the Scheme did not acquire any voting equity interest.

The members of the Scheme and WitsMed voted that the amalgamation of WitsMed with the Scheme would be in the best interest of the WitsMed members.

The Scheme obtained control of WitsMed by means of the exposition requirements as set out in Section 63 of the Act.

On the date of the amalgamation 2 604 principal members and 4 920 beneficiaries joined the Scheme.

No goodwill will be recognised as a result of this transaction.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS CONTINUED

for the year ended 31 December 2017

29 Amalgamations *continued*

The acquisition date fair value of the total consideration to be transferred and the acquisition date fair value of each major class of assets and liabilities is:

R'000	2017	2016
University of the Witwatersrand, Johannesburg Staff Medical Aid Fund		
Reserves effectively transferred:		
(Acquisition date fair value of WitsMed members' interest)	**149 210**	–
Net recognised values of WitsMed identifiable assets and liabilities:	**149 210**	–
Non-current assets	**1 762**	–
Available for sale investments	**1 762**	–
Current assets	**155 227**	–
Cash and cash equivalents	**151 584**	–
Member and service provider claims receivables	**1 370**	–
Provision for impairment	**(1 158)**	
Interest receivable	**767**	–
Other accounts receivable	**2 664**	–
Current liabilities	**(7 779)**	–
Outstanding claims provision	**(4 600)**	–
Reported claims not yet paid	**(2 188)**	–
Contribution in advance	**(159)**	–
Unallocated funds	**(40)**	–
Discovery Health (Pty) Ltd	**(468)**	–
General accruals	**(324)**	–
Closing balance	**149 210**	–

Movements subsequent to the amalgamation date generally relate to contributions, claims and operating expenses adjustments.

As a result of the amalgamation, the Scheme acquired the following receivables information of which is set out below.

R'000	2017	2016
Fair value of receivables acquired:	**3 463**	–
Insurance receivables	**2 876**	–
Members claim debtors	**211**	–
Service provider claim debtors	**1 159**	–
Other accounts receivable	**2 664**	–
Provision for impairment	**(1 158)**	–
Loans and receivables	**767**	–
Interest receivable	**767**	–
Gross contractual amounts receivable:	**4 801**	
Insurance receivables	**4 034**	–
Member claim debtors	**211**	–
Service provider claim debtors	**1 159**	–
Other accounts receivable	**2 664**	–
Loans and receivables	**767**	–
Interest receivable	**767**	–

29 Amalgamations *continued*

R'000	2017	2016
Best estimate at the acquisition date of the contractual cash flows not expected to be collected are:		
Insurance receivables	(1 158)	–
Member claim debtors	(178)	–
Service provider claim debtors	(980)	–
The amounts recognised as of the acquisition date for each major class of assets acquired and liabilities assumed.		
Non-current assets	1 762	–
Available for sale investments	1 762	–
Current assets	155 227	–
Cash and cash equivalents	151 584	–
Member claim debtors	33	–
Service provider claim debtors	179	–
Interest receivable	767	–
Other accounts receivable	2 664	–
Current liabilities	(7 779)	–
Outstanding claims provision	(4 600)	–
Reported claims not yet paid	(2 188)	–
Contribution in advance	(159)	
Unallocated funds	(40)	–
Discovery Health (Pty) Ltd	(468)	–
General accruals	(324)	–
	149 210	–

NOTES TO THE ANNUAL FINANCIAL STATEMENTS CONTINUED

for the year ended 31 December 2017

30 Insurance risk management report

Nature and extent of risks arising from insurance contracts

The Scheme issues contracts that transfer insurance risk. The primary insurance activity carried out by the Scheme indemnifies covered members and their dependants against the risk of loss arising as a result of the occurrence of a health event, in accordance with the Scheme Rules and the requirements of legislation.

This section summarises these risks and the way in which they are managed.

Insurance risk

The risk under any insurance contract can be expressed as the probability that an insured event occurs multiplied by the expected amount of the resulting claim. Insurance events are random and therefore the actual number and size of events during any year are unknown and vary from those estimated. The principal risk that the Scheme faces under its insurance contracts is that the actual claim payments exceed the projected amount of the insurance liabilities. This could occur because the frequency and severity of claims are greater than estimated.

A larger number of members will result in smaller variability of the actual claims experience relative to expected levels. This is because an adverse experience is diluted by a larger group of members whose claims are stable and thus predictable.

Factors that aggravate insurance risk include unanticipated demographic movements, adverse experience due to an unexpected epidemic, changes in members' disease profiles, unexpected price increases, prevalence of fraud, supplier induced demand and the cost of new technologies or drugs.

The risks that the Scheme faces can be discussed for the different benefits offered. The three main types of benefits offered by the Scheme in return for monthly contributions are indicated below:

Hospital benefits

The hospital benefit covers medical expenses incurred arising from admission to hospital. This includes accommodation, theatre, professional, medication, equipment and consumables.

Day-to-day benefits

Day-to-day benefits cover the cost of out-of-hospital healthcare services, such as visits to general practitioners and dentists as well as prescribed non-chronic medicines. The day-to-day benefits include both the Personal Medical Savings Account (PMSA) and an insurance risk element. This includes the Insured Network Benefit and Above Threshold Benefit (ATB). The Scheme does not carry risk for PMSA benefits.

Chronic benefits

The Chronic Illness Benefit (CIB) covers approved medication and treatment for up to 61 listed conditions, including the 27 Prescribed Minimum Benefit chronic conditions. These include conditions such as HIV/AIDS, high blood pressure, cholesterol and asthma.

The risks associated to the Scheme with the types of benefits offered to members are addressed below:

30 Insurance risk management report *continued*

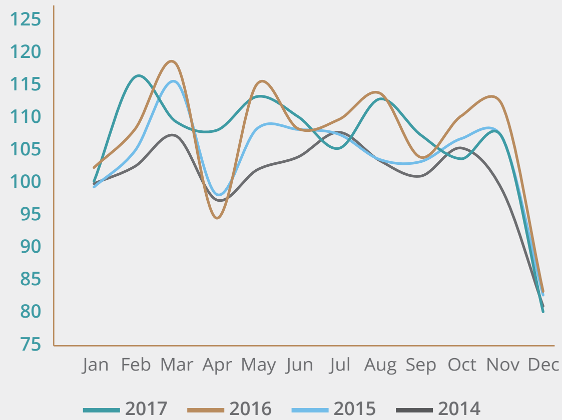
Hospital benefit risk

The main factors impacting the frequency and severity of hospital claims are the number of admissions and the cost per event. An increase in the frequency and severity of claims result in an increase in the cost of claims.

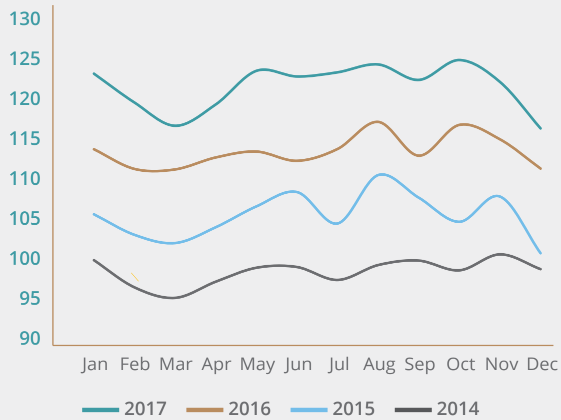
An increase in the admission rate is often linked to increases in the number of beneficiaries at older ages or with chronic conditions. The increase in cost per event is driven by annual tariff and other cost increases. An increased cost per event can also be caused by an increased case-mix, severity of admissions and the introduction of new hospital-based technologies.

The following graphs indicate the change in the admission rate over the past four years as well as the impact on the cost per event. These graphs are indexed to a value of 100 as at January 2014.

Hospital admission rate
(Indexed to Jan 2014 = 100)



Total cost per event
(Indexed to Jan 2014 = 100)

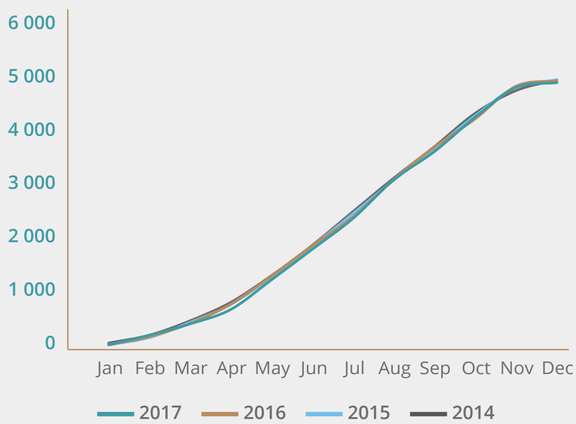


Day-to-day benefits risk

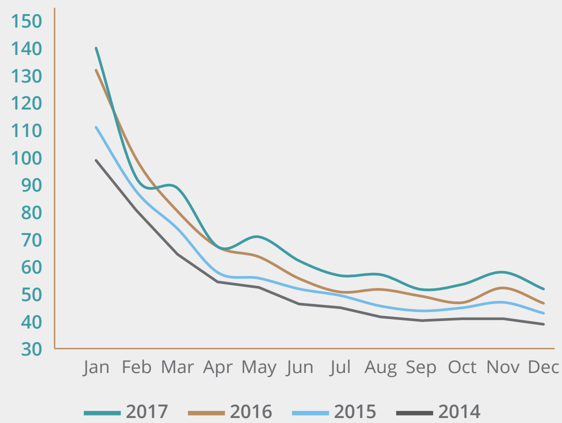
For the Above Threshold Benefit component, the frequency and severity of claims are driven by the number and disease burden of claimants. The mix of members between the different benefit options will also have an impact on the claims.

The frequency of these claims increases throughout the year as an increased number of members run out of their medical savings.

Claimants per 1000 beneficiaries from Above Threshold Benefits
(Indexed to Jan 2014 = 100)



Cost per ATB claimant
(Indexed to Jan 2014 = 100)



NOTES TO THE ANNUAL FINANCIAL STATEMENTS CONTINUED

for the year ended 31 December 2017

30 Insurance risk management report *continued*

Chronic benefits risk

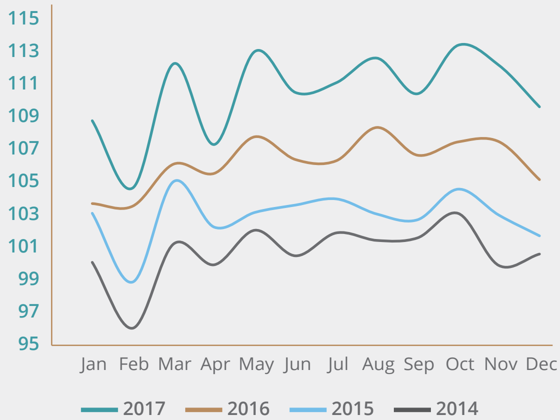
The main factors impacting the frequency and severity of chronic claims are the number of claimants and the cost per claimant respectively.

The cost per claimant increases during the year because Single Exit Price increases usually occur during the first quarter (as opposed to other price increases which happen on 1 January). Each manufacturer also has discretion as to exactly when they will implement this increase following the publication of the increase by the Department of Health.

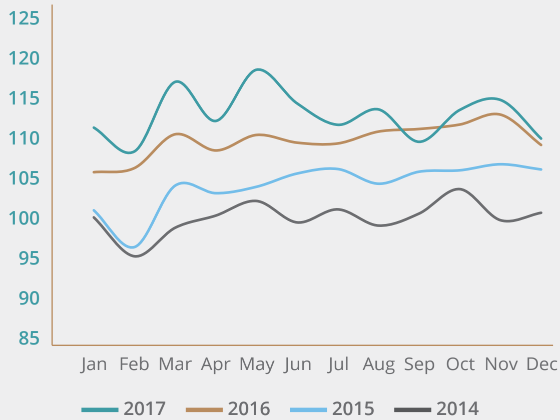
Higher increases in chronic claimants are linked to increases in the number of beneficiaries at older ages. In addition, changes relating to the eligibility for chronic benefits will also impact costs. An increase in the number of items per claimant will drive up the costs of chronic claims per claimant. Increases in the regulated prices for chronic medication, the Single Exit Price, and increases in dispensing fees will also result in an increase in costs per claim. The mix between the various chronic conditions will also have an impact on the frequency and severity of claims.

The following graphs indicate the change in the number of claimants over the past four years as well as the impact on the cost per claimant. These graphs are indexed to a value of 100 as at January 2014.

Chronic claimants per 1000 beneficiaries
(Indexed to Jan 2014 = 100)



Chronic cost per claimant
(Indexed to Jan 2014 = 100)



Risk management

The Scheme has various initiatives that are used to manage the risk associated with claims experience. These include:

- Members have to be referred by a doctor prior to an elective admission.
- All hospital admissions have to be pre-authorised.
- Case managers monitor members with hospital stays that are longer than expected to ensure that members are discharged at appropriate times.
- On-site case managers deployed at high risk establishments.
- The work of the Clinical Policy Unit, which evaluates the effectiveness of new technologies and recommends whether and to what extent the Scheme should cover these.
- The development of protocols around various high cost conditions, such as lower back surgery.
- The Drug Risk Management Unit is responsible for the development and maintenance of risk management strategies, including formulary development and maintenance.
- Designated Service Provider (DSP) Networks, including hospitals, GPs, specialists, retail pharmacies, etc.
- The management and mitigation of the risks associated with chronic illness benefits through an extensive managed care programme, involving detailed drug policy interventions, medicine protocols and benefit rules, all of which comply with the Regulations on Prescribed Minimum Benefits. In addition, the Clinical Policy Unit is involved in evaluating the effectiveness of new drugs and recommends whether the Scheme should cover these drugs or not.
- The establishment of a unit to focus on reducing surgical consumables and devices spend.
- The profiling of statistically significant outlier doctors on admission rate and generated costs as well as peer reviewing them.
- The establishment of the Coordinated Care Programme (CCP). This is a dedicated unit to ensure direct coordination of care from medical providers to high risk beneficiaries that are exposed to conditions that would generate multiple admissions if not managed.
- The establishment of an Advanced Illness Benefit Programme dedicated to managing care during the end of life stage for patients that are terminally ill.
- The establishment of a disease management unit dedicated to managing high risk beneficiaries with complex diseases.
- Alternative reimbursement contracts exist with hospitals to mitigate the risk of additional utilisation above that which is expected for the demographics of the Scheme and severity of admissions.
- Value-based contracting with selected healthcare provides, including establishment of centres of excellence.

30 Insurance risk management report *continued*

Concentration of insurance risk

As the largest open medical scheme by membership in South Africa, the Scheme is not subject to a significant degree of concentration risk. The Scheme also offers a wide range of benefit plans which meet a variety of members' needs. This results in the Scheme being representative of the medical scheme market and, as such, it experiences limited variability of the outcome.

An annual actuarial valuation is performed, which specifies the contribution to be charged in return for the benefits to be provided given the expected demographic profile of each benefit option.

Risk transfer arrangements

The Scheme has six (2016: six) risk transfer agreements in which suppliers are paid to provide certain minimum benefits to Scheme members, as and when required by the members. These arrangements fix the cost to the Scheme of providing these benefits.

The first risk transfer arrangement covers in-hospital and out-of-hospital benefits for certain members on the KeyCare Plus and KeyCare Access plans. There are two arrangements providing optometry and dentistry services to members on the KeyCare Plus and KeyCare Access plans. The fourth arrangement covers the treatment for Executive and Comprehensive plan members diagnosed with diabetes (type I and II). The fifth and sixth arrangements cover Smart plan members for acute medication prescribed by their network doctors.

Risk in terms of risk transfer arrangements

The Scheme does, however, remain liable to its members to provide the benefits. If any supplier fails to meet the obligations of the risk transfer arrangement, the Scheme will cover the cost of the benefit.

When selecting a supplier, the Scheme assesses their ability to provide the relevant service. This is to mitigate the reputational and operational risks that the Scheme faces should a supplier not meet its obligations. The Scheme also monitors the performance of the suppliers, checks the quality of care provided and has access to data on the underlying fee-for-service claims which are included in the arrangement.

Claims development

Detailed claims development tables are not presented as the uncertainty regarding the amount and timing of claim payments are typically resolved within one year and in the majority of cases within three months. At year end, a provision is made for those claims outstanding that are not yet reported at that date.

The methodology followed in setting the outstanding claims provision is the generally accepted actuarial methodology of chain ladder estimation. This methodology is the most objective, but the accuracy of the estimate is sensitive to changes in the average time from treatment to payment of claims. For hospital claims in the latest service month, a blend of the chainladder method and another method using the estimated cost per event and pre-authorised admissions is also followed.

The estimation of the December 2017 outstanding claims provision was made in accordance with Advisory Practice Note 304 of the Actuarial Society. In accordance with this guidance note, the following factors are considered to determine whether they would have any impact on the outstanding claims provision estimate:

- The homogeneity of claims data.
- The credibility of claims data.
- Changes in emergence and settlement patterns.
- The impact of seasonality.
- The impact of re-opened or adjusted claims.
- The impact of benefit limits and changes.
- External influences.
- The demographic profile of the Scheme.

Based on the processing patterns and claims development up to the end of December 2017 in respect of treatment dates during 2017, the recommended provision for outstanding claims as at December 2017 is R1 240 million (2016: R1 121 million).

R'000	2017	2016
The total claims incurred (including the provision for outstanding claims) for the most significant claims categories are as follows:		
Total estimate of incurred claims		
In-hospital claims incurred	**29 475 556**	26 807 352
Chronic claims incurred	**2 474 427**	2 271 897
Out-of-hospital risk claims incurred	**8 240 285**	7 745 832

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for the year ended 31 December 2017

30 Insurance risk management report *continued*

Concentration of insurance risk *continued*

The table below outlines the sensitivity of insured liability estimates to slower claims processing. If processing is slower than expected, a larger claims provision for unprocessed claims will be required. It should be noted that this is a deterministic approach with no correlations between the key variables

	Change in variable %	Impact on outstanding claims provision 2017 R'000	Impact on outstanding claims provision 2016 R'000
In-hospital claims incurred	1% slower claims processing	**326 614**	318 755
Chronic claims incurred	1% slower claims processing	**10 364**	7 682
Out-of-hospital risk claims incurred	1% slower claims processing	**89 670**	78 728

Liquidity risk

The main component of the Scheme's insurance liabilities is the outstanding claims provision. These are generally settled in a short period of time. Approximately 98% of this provision is settled within three months after the claim was incurred and the balance is settled within six months. The remaining insurance liabilities are generally settled within 30 days.

Liquidity risk can also arise when the Scheme's investment mix does not match the nature of the liabilities. However, investments are managed by professional asset managers and finance professionals whose mandates ensure that investments are always sufficiently liquid to meet current liabilities while excess reserves are invested to maximise investment return within the scope of Regulations to the Medical Schemes Act.

Assumption risk

The Scheme's reserves and therefore solvency are most sensitive to changes in claims development patterns. Another relevant assumption is medical inflation. Other assumptions that are considered include utilisation trends, the impact of new technology and the expected demographic profile of the Scheme membership.

31 Financial risk management report

Overview

The Scheme is exposed to financial risk through its financial assets, insurance assets, financial liabilities and insurance liabilities. In particular, the financial risk is that the proceeds, for any reason, from its financial assets are not sufficient to fund the obligations arising from its insurance contracts. The most important components of financial risk include market risk, interest rate risk, credit risk and liquidity risk.

The Scheme's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Scheme's statutory solvency requirement.

The Board of Trustees has overall responsibility for the establishment and oversight of the Scheme's risk management framework.

The Scheme manages these risks through various risk management processes. These processes have been developed to ensure that the long-term investment return on assets supporting the insurance liabilities is sufficient to contribute towards funding members' reasonable benefit expectations.

The Scheme manages the financial risks as follows:

- The Investment Committee, a Committee of the Board of Trustees, recommends the Scheme's investment policy to the Board of Trustees for approval. The Investment Committee meets at least quarterly and reports back to the Board of Trustees on the matters included in its terms of reference.
- The Scheme has appointed reputable external asset managers to manage its investments and their performance is monitored regularly.
- An external asset consulting company has been appointed to assist in formulating the investment strategy and to provide ongoing reporting and monitoring of the asset managers. During the year under review, the Scheme conducted a formal tender process for the asset consultant. The incumbent consultant was reappointed following this process.
- Asset management agreements and mandates are concluded and reviewed by the Scheme's in-house legal counsel.
- An independent valuation of the Scheme's investments is performed by a third party.

31 Financial risk management report *continued*

Personal Medical Savings Account trust assets

These portfolios have been established to manage members' Personal Medical Savings Account balances in portfolios which are distinct and separate from the Scheme.

The Scheme appointed two asset managers, Aluwani Capital Partners (Pty) Ltd and Taquanta Asset Managers, to manage the assets underlying the members' Personal Medical Savings Account balances. These portfolios are managed in accordance with Circular 38 of 2011 and Circular 5 of 2012 issued by the Council for Medical Schemes.

Changes in the interest rates have no bearing on the Scheme's surplus or deficit as the investment income earned, net of fees, is allocated to the members' Personal Medical Savings Account balance. Consequently, no further analysis is presented.

Market risk

Market risk is the risk that changes in market variables, such as foreign exchange rates, interest rates and equity prices will affect the Scheme's income or the value of its holdings in financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk.

The table below summarises the primary risks affecting the Scheme's financial assets at fair value through profit or loss exposure to market risk.

R'000	Total	Currency risk	Price risk	Interest rate risk
31 December 2017				
Investments	**14 005 644**			
Offshore bonds	**1 463 064**	✓		✓
Equities	**3 378 331**		✓	
Yield enhanced bonds	**3 721 190**			✓
Inflation linked bonds	**792 666**			✓
Money market instruments	**4 268 369**			✓
Listed property investments	**382 024**		✓	
31 December 2016				
Investments	12 211 677			
Offshore bonds	1 245 709	✓		✓
Equities	2 049 834		✓	
Yield enhanced bonds	3 413 740			✓
Inflation linked bonds	610 476			✓
Money market instruments	4 891 918			✓

The Scheme's insurance liabilities are settled within one year and the Scheme does not discount insurance liabilities. Consequently changes in market interest rates would not affect the Scheme's surplus or deficit arising from changes in the insurance liability.

Currency risk

The majority of the Scheme's benefits are Rand-denominated and therefore the Scheme does not have significant net currency risk relating to benefits.

For the purpose of seeking investment diversification, the Scheme continued to invest in offshore bond portfolios (reference currency is the US dollar). Derivative financial instruments are utilised by bond managers within these portfolios for risk mitigation and efficient portfolio construction. At 31 December 2017 R1.46 billion (2016: R1.25 billion) (Note 2) was invested in these portfolios.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS CONTINUED

for the year ended 31 December 2017

31 Financial risk management report *continued*

Currency risk *continued*

- ***Currency derivatives financial instrument (zero-cost currency collars)***

The Scheme enters into zero-cost currency collar arrangements with South African banks to hedge exposure to changes in the Rand/US dollar exchange rate with respect to its offshore bond portfolios. The following table provides detail of the three (2016: one) open contracts at year end expiring during 2018.

Contract	Nominal USD value $'000	2017 USD put ("floor")	2017 USD call ("cap")	2017 % above floor
1	$11 250	**R12.70**	**R14.83**	**16.73%**
2	$11 250	**R12.85**	**R14.91**	**16.01%**
3	$98 000	**R13.27**	**R15.30**	**15.30%**

The zero-cost currency collars are not designated as hedge instruments and hedge accounting is thus not applicable. The zero-cost currency collars are categorised as at fair value through profit or loss.

At the time of expiry the following transactions could occur depending on the spot rate at which the Rand is trading against the US Dollar:

- If the spot rate is higher than the cap, the Scheme would be required to pay the difference between the cap and the spot rate to the counterparty.
- If the spot rate is trading lower than the cap but higher than the floor, no action would take place.
- If the spot rate is trading lower than the floor, the counterparty would be required to pay the difference between the floor and the spot rate to the Scheme.

The fair value of these contracts have been included in financial assets. Gains and losses on these arrangements are included in the Net surplus (Note 7).

- ***Currency risk sensitivity analysis***

The sensitivity of the Rand appreciating and depreciating against the US Dollar is presented below. This impact would be recognised in the Net Surplus. The potential outcomes of the sensitivity is based on the assumption that the Rand has strengthened or weakened against the US Dollar by 5% (increase or decrease of R0.62) or 15% (increase or decrease of R1.85) from a spot level of R12.32 to the US Dollar, with all other variables held constant. The analysis is presented including and excluding the impact of the zero-cost currency collars, valued at year-end, based on the underlying valuation variables. The actual outcome of the impact of the zero-cost currency collars would be based on the spot rate at the date of expiry of the respective contracts.

R'000	15% Rand appreciation	5% Rand appreciation	5% Rand depreciation	15% Rand depreciation
(Loss)/gain arising from Rand appreciation/depreciation before zero cost currency collars	(219 460)	(73 153)	73 153	219 460
(Loss)/gain arising from Rand appreciation/depreciation after zero cost currency collars	50 041	69 502	108 303	171 938

Price risk

The Scheme is exposed to equity securities price risk due to equity investments held by the Scheme that are classified as at fair value through profit or loss. The value of the Scheme's equity investments amounted to R3.4 billion (2016: R2 billion) (Note 2).

The Scheme manages the price risk arising from investments in equity securities, through the diversification of its investment portfolios. Diversification of the portfolios is performed by asset managers in accordance with the mandate set by the Scheme. During the year, an additional strategy was implemented to manage price risk, with the decision taken to limit exposure to any constituent of the benchmark to a maximum weight of 15%.

The Scheme purchased derivative financial instruments to protect the solvency of the Scheme as a result of fluctuations in the equity market. The derivative strategy was also adjusted to take into consideration the decision to limit the maximum exposure to 15% of any constituent of the benchmark.

31 Financial risk management report *continued*

Price risk *continued*

- ***Equity derivative financial instrument (zero-cost equity collars)***

The Scheme entered into zero-cost equity collar arrangements to hedge approximately 100% of the exposure to changes in market prices for investments in the equity portfolios. The contracts provide downside protection of up to 15% after a reduction in equity prices of 5% (Scheme is at risk for the first 5% drop in equity prices but protected for the next 15%). To achieve this, the Scheme agreed to forego upside benefit from an increase in equity prices above the pre-determined level (the cap). The cap for these contracts range between 13% and 15% above the pre-determined level. These contracts expire during 2018.

	2017				
Contract	Nominal value R'000	Reference level at trade date	Short put level	Put level	Call level ("cap')
1	**R830 000**	**47 313**[1]	**80.00%**	**95.00%**	**114.00%**
2	**R720 000**	**48 176**[1]	**80.00%**	**95.00%**	**113.07%**
3	**R185 000**	**49 618**[1]	**80.00%**	**95.00%**	**112.88%**
4	**R734 000**	**49 730**[1]	**80.00%**	**95.00%**	**113.16%**
5	**R600 000**	**11 500**[2]	**80.00%**	**95.00%**	**115.63%**
6	**R90 000**	**3 525**[3]	**N/A**	**100.80%**	**115.60%**

1 *Reference level: FTSE/JSE TOP40.*

2 *Reference level: FTSE/JSE SWIX TOP40.*

3 *Reference level: Naspers (Bloomberg: NPN SJ Equity).*

The zero-cost equity collars are not designated as hedge instruments and hedge accounting is thus not applicable. The zero-cost equity collars are categorised as at fair value through profit or loss.

At the time of expiry the following transactions could occur depending on the level at which the equity index trades:
- If the index level is higher than the cap, the Scheme would be required to pay the difference between the cap and the index level to the counterparty.
- If the index level is trading lower than the cap but higher than the floor, no action would take place.
- If the index level is trading lower than the floor but above the short put level, the counterparty would be required to pay the difference between the floor and the index level to the Scheme.
- If the index level is trading lower than the short put level, the counterparty would be required to pay the difference between floor and the short put level to the Scheme.

The fair value of these contracts have been included in financial assets and financial liabilities. Gains and losses on these arrangements are included in the Net surplus (Note 7).

NOTES TO THE ANNUAL FINANCIAL STATEMENTS CONTINUED

for the year ended 31 December 2017

31 Financial risk management report *continued*

Price risk *continued*

- ***Equity price risk sensitivity analysis***

The analysis reflecting the impact of increases or decreases in equity prices has been presented below. This impact would be recognised in the Net Surplus. The potential outcomes of the sensitivity is based on the assumption that equity prices had increased or decreased by 5% or 15%, spot reference levels of 52,533; 11,973 or 3,525 respectively, with all other variables held constant. The analysis is presented excluding and including the impact of the zero-cost equity collars, valued at year-end, based on the underlying valuation variables. The actual outcome of the impact of the zero-cost equity collars would be based on the reference level at the date of expiry of the respective contracts.

The following table indicates the 5% or 15% change in the respective index.

Index	5% increase or decrease	15% increase or decrease
FTSE/JSE TOP40	**2 627**	**7 880**
FTSE/JSE SWIX TOP40	**599**	**1 796**
Naspers (Bloomberg: NPN SJ Equity)	**176**	**529**

R'000	15% price decrease	5% price decrease	5% price increase	15% price increase
(Loss)/gain arising from price decrease/increase before zero-cost equity collars	**(518 695)**	**(172 898)**	**172 898**	**518 695**
(Loss)/gain arising from price decrease/increase after zero-cost equity collars	**(420 860)**	**(168 558)**	**49 726**	**212 665**

The analysis reflecting the impact of increases or decreases in prices of the listed property portfolio has been presented below. This impact would be recognised in the Net Surplus. The potential outcomes of the sensitivity is based on the assumption that prices had increased or decreased by 5% or 15%, with all other variables held constant. This portfolio was only implemented during the course of the year under review and therefore no comparatives are presented. The Scheme has not hedged this portfolio.

R'000	15% price decrease	5% price decrease	5% price increase	15% price increase
(Loss)/gain arising from price decrease/increase	**(60 041)**	**(20 014)**	**20 014**	**60 041**

31 Financial risk management report *continued*

Interest rate risk

The Scheme is exposed to interest rate risk as it places funds in short dated investments, money market accounts and bonds. The risk is managed by maintaining an appropriate mix between fixed and floating rate investments within the Scheme's money market investment portfolio as well as additional fixed and call deposit investments. The bond managers have made use of bond futures and other derivative instruments within these portfolios to manage duration risk.

The table summarises the Scheme's exposure to interest rate risks. Included in the table are the Scheme's investments at carrying amounts, categorised by the earlier of contractual repricing or maturity dates.

As at 31 December 2017 R'000	**0 – 3 Months**	**3 – 12 Months**	**> 12 Months**	**Total**
Cash and cash equivalents	**5 880 362**	**–**	**–**	**5 880 362**
Money market instruments carried at fair value through profit or loss	**–**	**4 268 369**	**–**	**4 268 369**
Yield enhanced bonds carried at fair value through profit or loss	**–**	**3 721 190**	**–**	**3 721 190**
Inflation linked bonds carried at fair value through profit or loss	**–**	**792 666**	**–**	**792 666**
Offshore bonds carried at fair value through profit or loss	**–**	**1 463 064**	**–**	**1 463 064**

As at 31 December 2016 R'000	0 – 3 Months	3 – 12 Months	> 12 Months	Total
Cash and cash equivalents	2 397 788	–	–	2 397 788
Money market instruments carried at fair value through profit or loss	–	4 891 918	–	4 891 918
Yield enhanced bonds carried at fair value through profit or loss	–	3 413 740	–	3 413 740
Inflation linked bonds carried at fair value through profit or loss	–	610 476	–	610 476
Offshore bonds carried at fair value through profit or loss	–	1 245 709	–	1 245 709

- ***Interest rate risk sensitivity analysis***

  A sensitivity analysis indicating results of increases in interest rates has been presented below. This impact would be recognised in the Net Surplus. The sensitivity is based on the assumption that local or foreign interest rates had increased or decreased by 1% or 2%, with all other variables held constant.

Gains/(losses) arising from changes in: R'000	**2% interest rate decrease**	**1% interest rate decrease**	**1% interest rate increase**	**2% interest rate increase**
Local portfolios	**73 934**	**38 996**	**(40 491)**	**(75 576)**
Foreign portfolios	**105 103**	**52 552**	**(52 552)**	**(105 103)**

The majority of the Scheme's assets are invested in variable interest rate instruments with a significant portion of the fixed rate instruments maturing in the short term. As a result, interest rate changes are not expected to have a material impact on the valuation of Scheme assets due to the short duration thereof.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS CONTINUED

for the year ended 31 December 2017

31 Financial risk management report *continued*

Legal risk

Legal risk is the risk that the Scheme will be exposed to contractual obligations which have not been provided for. At 31 December 2017 the Scheme did not consider there to be any significant concentration of legal risk that had not been provided for.

Investment risk

Investment risk is the risk that the investment returns on accumulated assets will not be sufficient to cover future liabilities.

The Scheme's Investment Committee oversees that the funds are invested in line with the Act.

The investment philosophy is to hold a diversified pool of assets. The assets are selected as being most appropriate given the liquidity and solvency requirements of the Scheme. In contemplating solvency, the return goals of the Scheme, as well as the risk associated with all assets and asset classes are considered. Diversification is across asset classes, geographic regions as well as managers within asset classes where practical. The Scheme diversifies its investment portfolio by investing in short-term deposits, money market, bond, listed property and equity portfolios managed by reputable asset managers.

The Scheme's investment objective statement is:

- Maximise targeted investment returns, which is dependent on contribution increases implemented over the next year and the evaluation of the solvency level above the statutory minimum requirement from time to time.
- The return target will be reviewed at the end of every year taking into account the actual returns achieved, projected operating surplus and finalised contribution increases.
- To track medical inflation.

The Investment Committee monitors the performance of the Scheme's asset managers to ensure performance in accordance with the agreed mandates.

Breakdown of investments

The investments are split between the following in the Annual Financial Statements:

- Investments carried at fair value through profit and loss; and
- Cash and cash equivalents.

R'000	Segregated Funds	Collective Investment Schemes	Policy of Insurance	Total
31 December 2017				
Investments	**12 542 580**	**901 589**	**561 475**	**14 005 644**
Offshore bonds	**–**	**901 589**	**561 475**	**1 463 064**
Equities	**3 378 331**	**–**	**–**	**3 378 331**
Yield enhanced bonds	**3 721 190**	**–**	**–**	**3 721 190**
Inflation linked bonds	**792 666**	**–**	**–**	**792 666**
Listed property investments	**382 024**	**–**	**–**	**382 024**
Money market instruments	**4 268 369**	**–**	**–**	**4 268 369**
Cash and cash equivalents:	**3 891 038**	**1 989 324**	**–**	**5 880 362**
	16 433 618	**2 890 913**	**561 475**	**19 886 006**
31 December 2016				
Investments	10 965 968	672 885	572 824	12 211 677
Offshore bonds	–	672 885	572 824	1 245 709
Equities	2 049 834	–	–	2 049 834
Yield enhanced bonds	3 413 740	–	–	3 413 740
Inflation linked bonds	610 476	–	–	610 476
Money market instruments	4 891 918	–	–	4 891 918
Cash and cash equivalents:	940 981	1 456 807	–	2 397 788
	11 906 949	2 129 692	572 824	14 609 465

31 Financial risk management report *continued*

Breakdown of investments *continued*

Money market portfolios:

Local portfolios:

The two local money market portfolios are each managed by an independent asset manager. The investment mandate is for an actively managed portfolio of financial instruments aimed at maximising return on the investments, on a long-term basis, with due regard to the relevant risks and the constraints imposed by the mandates.

For the first portfolio, the mandate stipulates liquidity requirements that 5% of the assets must be available within 24 hours and 15% within five working days. The weighted modified duration of the portfolio may not exceed 180 days. The weighted term to maturity of the portfolio shall not exceed two years. The term of each individual instrument is also limited. The average weighted credit rating of this portfolio will not be less than A+.

The liquidity requirements of the second portfolio also stipulate that 5% of the assets must be available on 24 hours notice and an additional 15% within five working days. The average portfolio duration is limited to 180 days. There are a number of additional liquidity requirements included in the mandate such as requiring that all investments with a maturity longer than 18 months must be of a negotiable nature. The key feature of being of a negotiable nature is that the instrument can be sold by the holder of that instrument to another party without requiring explicit consent from the issuer of the instrument.

The performance benchmark for these portfolios has been changed during the year from measuring against the Short Term Fixed Income (STeFI) Composite Index to being measured against the STeFI + 130 basis points per annum over rolling one year periods.

The local money market portfolios comprise approximately 30% (2016: 40%) of the Scheme's financial assets at fair value through profit or loss.

Bond portfolios:

Local portfolios:

The Scheme has two bond portfolios, each managed by an independent asset manager.

One of the portfolios uses a specialist fixed income strategy with South African exposure and invests in a broad spectrum of listed and unlisted fixed income instruments. The instruments are typically investment grade and include but are not limited to asset types such as, listed bonds, credit-linked notes, floating rate notes, interest rate swaps and bond futures. During the year, the benchmark for this portfolio was changed from the 3-month Johannesburg Interbank Agreed Rate (JIBAR) to STeFI 3 month index + 150 basis points per annum.

The other portfolio is a specialist low interest rate yield-enhanced bond portfolio with moderate risk limits that seeks diversity, reasonable yield enhancement, moderate liquidity and relatively low volatility due to constrained interest rate positions. This is achieved by investing in a broad spectrum of fixed interest and yield-enhanced debt instruments. The benchmark for this portfolio is STeFI.

The mandates set specific exposure limits depending on the credit rating of the individual counterparty and set exposure limits to unrated investments. These portfolios comprise approximately 27% (2016: 28%) of the Scheme's financial assets at fair value through profit or loss.

Offshore portfolios:

The Scheme has two offshore portfolios each managed by independent asset managers.

The primary objective of the first portfolio is to provide income and to protect and maximise the real asset value of its investments in terms of their international purchasing power by means of the management and diversification of currency exposure and investment in fixed interest bearing securities of varying maturities. The majority of these assets are denominated in major currencies and exposure to minor currencies is managed on a cautious basis. The fund is benchmarked against 3 month USD LIBOR.

The primary objective of the second portfolio is the long-term growth of capital and income and is a policy of insurance referencing participatory interests in a foreign collective investment scheme portfolio investing in fixed income instruments. The benchmark for this portfolio is the Barclays Capital Global Aggregate.

These portfolios comprise approximately 10% (2016: 10%) of the Scheme's financial assets at fair value through profit or loss.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS CONTINUED

for the year ended 31 December 2017

31 Financial risk management report *continued*

Breakdown of investments *continued*

Inflation linked bonds:

The Scheme has two inflation-linked bond portfolios, each managed by an independent asset manager.

The primary mandate of the first portfolio is aimed at generating inflation-linked bond returns on initial capital invested. The benchmark is the JSE Composite Inflation-Linked Index (CILI).

The second portfolio is a fully discretionary, actively managed portfolio of inflation-linked and fixed income instruments. The portfolio only invests funds in domestic instruments. The benchmark for this portfolio is the JSE Bond Exchange and Actuarial Society of South Africa (JSE BEASSA IGOV Index).

These portfolios comprise approximately 6% (2016: 5%) of the Scheme's financial assets at fair value through profit or loss.

Equity portfolios:

The primary goal is to maximise long-term investment performance with due regard to the relevant risks, including volatility of returns, risk of capital loss and liquidity. These risks are mitigated by blending investment mandates across different manager styles and sectors.

The Scheme has further diversified its equity exposure by adding a long only general equity portfolio, managed by a boutique manager and a passive equity portfolio. The number of portfolios has increased from three to five. Each portfolio is managed by an independent asset manager.

The portfolios may only be invested in South African equities and are to be as fully invested as can practically be achieved at all times. One portfolio has a maximum cash allocation of 2% and the remaining portfolios a maximum allocation of 5%. The portfolios must comply with the Act and are prohibited from investing in Discovery Limited. The Scheme has mitigated exposure to any single benchmark constituent by limiting investment in any single benchmark constituent to a maximum of 15%.

The Scheme considers responsible investing in all its investments. Managers are required to exclude tobacco manufacturers and related exposures by utilising negative screening. This includes all direct investments and indirect investments greater than 5%.

The performance of the actively managed portfolios is measured against the benchmark, which is the FTSE/JSE Shareholder weighted index (SWIX) adjusted to exclude tobacco (as per the Scheme's responsible investment policy) and capping the exposure of any benchmark constituent to 15%. The performance of the passive portfolio is measured against the FTSE/JSE SWIX 40 (J400) adjusted to exclude tobacco (as per the Scheme's responsible investment policy) and capping the exposure of any benchmark constituent to 15%.

These portfolios comprise approximately 24% (2016: 17%) of the Scheme's financial assets at fair value through profit or loss.

Listed property:

During the year, the Scheme allocated a portion of its investments to listed property and appointed an independent asset manager to manage the portfolio.

The primary objective of this mandate is to deliver consistent and incremental out-performance of the benchmark over a long-term period. The benchmark is the SA Listed Property Index (J253).

The mandate does not permit investment in foreign listed shares or direct property investments and requires that there will always be more than six holdings in the portfolio.

This portfolio comprises approximately 3% of the Scheme's financial assets at fair value through profit or loss.

The following table compares the fair value and carrying amounts of assets and liabilities per class of assets and liabilities.

31 Financial risk management report *continued*

Breakdown of investments *continued*

R'000	**Financial assets and liabilities at fair value through profit and loss** – **Designated upon initial recognition**	**Classified as held for trading**	**Loans and receivables**	**Insurance receivables and (payables)**	**Financial liabilities at amortised cost**	**Total carrying amount**	**Fair value amount**
31 December 2017							
Investments							
– Offshore bond portfolio	**1 463 064**	**–**	**–**	**–**	**–**	**1 463 064**	**1 463 064**
– Listed equities	**3 378 331**	**–**	**–**	**–**	**–**	**3 378 331**	**3 378 331**
– Yield-enhanced bond portfolio	**3 721 190**	**–**	**–**	**–**	**–**	**3 721 190**	**3 721 190**
– Inflation-linked bond portfolio	**792 666**	**–**	**–**	**–**	**–**	**792 666**	**792 666**
– Listed property investments	**382 024**	**–**	**–**	**–**	**–**	**382 024**	**382 024**
– Money market portfolios	**4 268 369**	**–**	**–**	**–**	**–**	**4 268 369**	**4 268 369**
Cash and cash equivalents:							
Medical Scheme assets	**–**	**–**	**5 880 362**	**–**	**–**	**5 880 362**	**5 880 362**
Personal Medical Savings Account trust assets			**4 609 149**	**–**	**–**	**4 609 149**	**4 609 149**
Trade and other receivables	**–**	**–**	**237 864**	**909 801**	**–**	**1 147 665**	**1 147 665**
Personal Medical Savings Accounts	**–**	**–**	**–**	**–**	**(4 656 633)**	**(4 656 633)**	**(4 656 633)**
Trade and other payables	**–**	**–**	**–**	**(2 526 588)**	**(538 930)**	**(3 065 518)**	**(3 065 518)**
Derivatives held for trading							
– Zero-cost collars	**–**	**(588)**	**–**	**–**	**–**	**(588)**	**(588)**
	14 005 644	**(588)**	**10 727 375**	**(1 616 787)**	**(5 195 563)**	**17 920 081**	**17 920 081**

R'000	Financial assets and liabilities at fair value through profit and loss – Designated upon initial recognition	Classified as held for trading	Loans and receivables	Insurance receivables and (payables)	Financial liabilities at amortised cost	Total carrying amount	Fair value amount
31 December 2016							
Investments							
– Offshore bond portfolio	1 245 709	–	–	–	–	1 245 709	1 245 709
– Listed equities	2 049 834	–	–	–	–	2 049 834	2 049 834
– Yield-enhanced bond portfolio	3 413 740	–	–	–	–	3 413 740	3 413 740
– Inflation-linked bond portfolio	610 476	–	–	–	–	610 476	610 476
– Money market portfolios	4 891 918	–	–	–	–	4 891 918	4 891 918
Cash and cash equivalents:							
Medical Scheme assets	–	–	2 397 788	–	–	2 397 788	2 397 788
Personal Medical Savings Account trust assets			4 142 672			4 142 672	4 142 672
Trade and other receivables	–	–	179 900	1 878 108	–	2 058 008	2 058 008
Personal Medical Savings Accounts	–	–	–	–	(4 204 043)	(4 204 043)	(4 204 043)
Trade and other payables	–	–	–	(784 555)	(521 690)	(1 306 245)	(1 306 245)
Derivatives held for trading							
– Zero-cost collars	–	50 384	–	–	–	50 384	50 384
	12 211 677	50 384	6 720 360	1 093 553	(4 725 733)	15 350 241	15 350 241

NOTES TO THE ANNUAL FINANCIAL STATEMENTS CONTINUED

for the year ended 31 December 2017

31 Financial risk management report *continued*

Credit risk

Credit risk is the risk of financial loss to the Scheme, if a counterparty to a financial instrument fails to meet its contractual obligations.

Key areas where the Scheme is exposed to credit risk are through its trade and other receivables, investments and cash.

Trade and other receivables

Trade and other receivables comprise of insurance receivables and loans and receivables. The main components of insurance receivables are in respect of contributions due from members and amounts recoverable from members in respect of claims debt.

Exposure to credit risk

The carrying amount of trade and other receivables represents the maximum credit exposure.

The Scheme ages and pursues unpaid accounts on a monthly basis. The tables below highlights Trade and other receivables which are due and past due (by number of days).

	Total member and service provider claims receivables									
R'000	Active member claims receivables	Withdrawn member claims receivables	Service provider claims receivables	Total	Contribution receivables	Other risk transfer arrangements	Broker fee receivables	Other insurance receivables	Loans and receivables	Total
31 December 2017										
Not past due	**4 011**	**7 822**	**5 149**	**16 982**	**739 565**	**11 796**	**80**	**52 045**	**237 864**	**1 058 332**
Past due 30 – 60 days	**3 650**	**8 037**	**2 419**	**14 106**	**9 875**	**–**	**587**	**–**	**–**	**24 568**
Past due 61 – 90 days	**3 425**	**8 118**	**2 214**	**13 757**	**2 927**	**–**	**58**	**–**	**–**	**16 742**
Past due 91 – 120 days	**3 369**	**9 458**	**675**	**13 502**	**4 457**	**–**	**5**	**–**	**–**	**17 964**
Past due 121 – 150 days	**4 342**	**12 302**	**2 291**	**18 935**	**5 861**	**–**	**9**	**–**	**–**	**24 805**
Past due 151 – 180 days	**3 370**	**9 896**	**3 461**	**16 727**	**–**	**–**	**4**	**–**	**–**	**16 731**
181 days to more than one year	**36 628**	**207 642**	**23 287**	**267 557**	**–**	**–**	**947**	**–**	**–**	**268 504**
Gross receivables	**58 795**	**263 275**	**39 496**	**361 566**	**762 685**	**11 796**	**1 690**	**52 045**	**237 864**	**1 427 646**
Provision for impairments	**(36 628)**	**(207 642)**	**(23 271)**	**(267 541)**	**(11 493)**	**–**	**(947)**	**–**	**–**	**(279 981)**
Trade and other receivables neither past due nor impaired	**22 167**	**55 633**	**16 225**	**94 025**	**751 192**	**11 796**	**743**	**52 045**	**237 864**	**1 147 665**
31 December 2016										
Not past due	2 395	5 150	10 249	17 794	**1 615 128**	24 426	(90)	138 781	179 900	1 975 939
Past due 30 – 60 days	1 677	6 474	8 720	16 871	**8 712**	–	(78)	–	–	25 505
Past due 61 – 90 days	1 751	8 539	(2 511)	7 779	**6 972**	–	(13 524)	–	–	1 227
Past due 91 – 120 days	2 757	8 250	1 295	12 302	**(7 135)**	–	15 370	–	–	20 537
Past due 121 – 150 days	2 918	8 809	11 616	23 343	**15 709**	–	95	–	–	39 147
Past due 151 – 180 days	2 305	10 447	(4 980)	7 772	**–**	–	55	–	–	7 827
181 days to more than one year	29 308	227 748	(1 444)	255 612	**–**	–	120	–	–	255 732
Gross receivables	**43 111**	**275 417**	**22 945**	**341 473**	**1 639 386**	**24 426**	**1 948**	**138 781**	**179 900**	**2 325 914**
Provision for impairments	(26 707)	(220 454)	(10 122)	(257 283)	**(9 759)**	–	(864)	–	–	(267 906)
Trade and other receivables neither past due nor impaired	16 404	54 963	12 823	84 190	**1 629 627**	24 426	1 084	138 781	179 900	2 058 008

Based on past experience, the Scheme believes that no provision for impairment is required in respect of Contribution debtors that are past due and outstanding for less than 90 days. For member and service provider claims debtors and broker fee debtors that are past due and outstanding for less than 180 days, past experience has indicated that no provision is required. The Scheme has not renegotiated the terms of receivables and does not hold any collateral or guarantees as security.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS CONTINUED

for the year ended 31 December 2017

31 Financial risk management report *continued*

Credit risk *continued*

Provision for impairment

The Scheme establishes an allowance for impairment that represents its estimate of incurred losses in respect of trade and other receivables. The provision is based on the expected difference between the current carrying amount and the amount recoverable from the counter party.

The main components of this provision are:

- A specific loss component that relates to individually significant exposures; and
- A collective loss component established for groups of similar assets in respect of losses that have been incurred but not yet identified.

The collective loss allowance is determined based on historical data of payment statistics for similar financial assets.

The movement in the provision for impairment, for each component of trade and other receivables, during the year ended 31 December:

	Trade and other receivables				
	Insurance receivables				
R'000	Contribution receivables	Member and service provider claims receivables	Other risk transfer arrangements	Broker fee receivables	Total
Balance as at 1 January 2016	9 633	208 529	–	784	218 946
Increase in provision for impairment	126	76 422	–	81	76 629
Amounts utilised during the year	–	(27 668)	–	(1)	(27 669)
Balance as at 31 December 2016	9 759	257 283	–	864	267 906
Balance as at 1 January 2017	**9 759**	**257 283**	**–**	**864**	**267 906**
Increase in provision for impairment	**1 734**	**85 688**	**–**	**82**	**87 504**
Amounts utilised during the year	**–**	**(75 430)**	**–**	**1**	**(75 429)**
Balance as at 31 December 2017	**11 493**	**267 541**	**–**	**947**	**279 981**

31 Financial risk management report *continued*

Credit quality

The credit quality of Trade and other receivables that are neither past due nor impaired as presented on page 154 to 155 can be assessed by reference to historical information about counterparty default.

Contribution debtors

The Scheme collected over 96% (2016: 97%) of outstanding debt in January 2018. Therefore we can establish that the credit quality of contribution debtors is high. Consequently, no additional disclosure of the credit quality is provided.

Active member claims debtors

A provision for impairment covering 62% (2016: 62%) of the debtors has been raised and the Trustees are satisfied that this is adequate.

Withdrawn member claims debtors

These amounts are due from members that have withdrawn from the Scheme. A provision for impairment covering 79% (2016: 80%) of the total amount due has been raised and the Trustees are satisfied that this is adequate.

Other insurance receivables and loans and receivables

These debtors mainly comprises of amounts due by hospitals, which are inherently of high quality. As agreed with the providers the majority of these receivables are recovered by reducing future provider payments providing a high certainty of recoverability and thus no further analysis has been performed on these receivables.

Financial assets held at fair value through profit or loss, cash and cash equivalents and derivative financial instruments

The Scheme's credit risk exposures as at 31 December were as follows:

R'000	2017	2016
– Offshore bonds	**1 463 064**	1 245 709
– Yield enhanced bonds	**3 721 190**	3 413 740
– Inflation linked bonds	**792 666**	610 476
– Listed property investments	**382 024**	–
– Money market instruments	**4 268 369**	4 891 918
– Cash and cash equivalents	**5 880 362**	2 397 788
– Derivative financial instruments	**–**	50 384
	16 507 675	12 610 015

NOTES TO THE ANNUAL FINANCIAL STATEMENTS CONTINUED

for the year ended 31 December 2017

31 Financial risk management report *continued*

Exposure to credit risk

The Scheme manages credit risk on its investment portfolios through the appointment of reputable and appropriate asset managers, extensive diversification and ongoing monitoring and management of credit risk exposures and portfolio holdings.

Cash and cash equivalents comprise cash deposits with financial institutions. The risks associated with these deposits are managed by monitoring the Scheme's exposure to external financial institutions against approved deposit limits per institution. Information regarding the credit quality of cash and cash equivalents is provided on pages 160 to 161.

Derivative counterparties are limited to high credit quality financial institutions.

The Scheme's credit risk policy guides the Scheme with respect to credit risk identification, measurement, monitoring and management in its oversight capacity. The policy provides for limits based on parameters such as:

- Instrument and counterparty exposure;
- Credit ratings;
- Geographical exposure;
- Industry exposure; and
- Expected loss.

Compliance with the limits are regularly monitored with a quarterly report back presented to the Scheme's Investment Committee.

The Scheme has assessed whether the above financial assets are impaired. Based on the risk management measures undertaken by the Scheme, there is no objective evidence that any financial assets are impaired below the fair market value stated above.

Credit ratings provide an opinion on the relative ability of an entity to meet its financial commitments, such as interest, dividends or the repayment of capital invested. They are used as indicators of the likelihood of receiving the amounts owed in accordance with the terms on which they were invested.

Definitions of the symbols are presented below.

Long-term rating scales

AAA: Highest credit quality

AAA ratings denote the lowest expectation of default risk and are assigned only in cases of exceptionally strong capacity for payment of financial commitments. This capacity is highly unlikely to be adversely affected by foreseeable events.

AA: Very high credit quality

AA ratings denote expectations of very low default risk and indicate very strong capacity for payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.

A: High credit quality

A ratings denote expectations of low default risk. The capacity for payment of financial commitments is considered strong. This capacity may, nevertheless, be more vulnerable to adverse business or economic conditions than is the case for higher ratings.

BBB: Good credit quality

BBB ratings indicate that expectations of default risk are currently low. The capacity for payment of financial commitments is considered adequate but adverse business or economic conditions are more likely to impair this capacity.

At 31 December 2017, 2.1% (2017: 1.8%) of the Scheme's financial assets at fair value through profit or loss are invested in instruments with this credit rating.

BB: Speculative

BB ratings indicate an elevated vulnerability to default risk, particularly in the event of adverse changes in business or economic conditions over time, however business or financial flexibility exists which supports the servicing of financial commitments.

At 31 December 2017, 0.7% (2016: 1%) of the Scheme's financial assets at fair value through profit or loss are invested in instruments with this credit rating.

31 Financial risk management report *continued*

Exposure to credit risk *continued*

B: Highly speculative

B ratings indicate that material default risk is present, but a limited margin of safety remains. Financial commitments are currently being met, however capacity for continued payment is vulnerable to deterioration in the business and economic environment.

At 31 December 2017, 0.5% (2016: 0.5%) of the Scheme's financial assets at fair value through profit or loss are invested in instruments with this credit rating.

CCC: Possibility of default

Obligations for which there is a current perceived possibility of default. Timely repayment of principal and interest is dependent on favourable business economic or financial conditions.

At 31 December 2017, 0% (2016: 1.6%) of the Scheme's financial assets at fair value through profit or loss are invested in instruments with this credit rating.

CC: Very high levels of credit risk

Default of some kind appears probable.

At 31 December 2017, 0% (2016: 0%) of the Scheme's financial assets at fair value through profit or loss are invested in instruments with this credit rating.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS CONTINUED

for the year ended 31 December 2017

31 Financial risk management report *continued*

The following table discloses the Scheme's asset credit ratings using official credit ratings. The credit risk policy limits investments in non-investment grade instruments to a maximum of 10% after considering official credit ratings and asset manager assigned internal credit ratings where official ratings are not available. Less than 2% (2016: 4%) of the instruments are invested in non-investment grade instruments after consideration of internally assigned credit ratings.

	Long-term rating					Long-term rating					
R'000	Total	Govt	AAA	AA+ to AA–	A+ to A–	BBB– to BBB+	BB– to BB+	B– to B+	CCC+ to CCC–	CC+	Not rated
2017											
At fair value through profit or loss:	**10 627 313**	**401 511**	**1 296 569**	**6 269 204**	**508 718**	**246 993**	**102 274**	**84 548**	**3 251**	**–**	**1 714 245**
– Offshore bond portfolio	**1 463 064**	**–**	**231 344**	**284 611**	**79 924**	**122 725**	**102 274**	**60 967**	**3 251**	**–**	**577 968**
– Yield enhanced bond portfolio	**3 721 190**	**–**	**698 624**	**2 036 167**	**185 757**	**84 617**	**–**	**23 581**	**–**	**–**	**692 444**
– Inflation linked bond portfolio	**792 666**	**373 927**	**–**	**410 154**	**8 585**	**–**	**–**	**–**	**–**	**–**	**–**
– Money market portfolios	**4 268 369**	**27 584**	**366 601**	**3 538 272**	**234 452**	**39 651**	**–**	**–**	**–**	**–**	**61 809**
– Listed property investments	**382 024**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**382 024**
Cash and cash equivalents	**5 880 362**	**–**	**4 037 907**	**1 655 954**	**29 089**	**101 169**	**15 141**	**–**	**–**	**–**	**41 102**
Total*	**16 507 675**	**401 511**	**5 334 476**	**7 924 158**	**537 807**	**348 162**	**117 415**	**84 548**	**3 251**	**–**	**1 755 347**
2016											
At fair value through profit or loss:	10 161 843	565 317	1 380 392	3 200 030	3 718 408	223 471	128 709	57 319	189 501	–	698 696
– Offshore bond portfolio	1 245 709	–	242 723	451 776	221 380	113 316	128 709	57 319	4 460	–	26 026
– Yield enhanced bond portfolio	3 413 740	60 997	565 333	1 035 608	1 066 578	110 155	–	–	29 068	–	546 001
– Inflation linked bond portfolio	610 476	445 255	16 688	10 204	138 329	–	–	–	–	–	–
– Money market portfolios	4 891 918	59 065	555 648	1 702 442	2 292 121	–	–	–	155 973	–	126 669
Cash and cash equivalents	2 397 788	6 608	201	1 953 693	370 752	–	–	–	15 409	–	51 125
Total*	12 559 631	571 925	1 380 593	5 153 723	4 089 160	223 471	128 709	57 319	204 910	–	749 821

* *Excludes derivative financial assets.*

At the reporting date the credit ratings shown are the most conservative of Moody's, Fitch and S&P and have been provided in a Fitch format.

The Scheme's investments in pooled funds and collective investment schemes (funds) are subject to the terms and conditions of the respective funds' offering documentation and are susceptible to market price risk arising from uncertainties about future values of those funds. The investment manager makes investment decisions after extensive due diligence of the underlying fund, its strategy and the overall quality of the underlying funds' managers. All of the funds in the investment portfolio are managed by portfolio managers who are compensated by the respective funds for their services. Such compensation generally consists of an asset-based fee and a performance-based incentive fee and is reflected in the valuation of the investment in each of the funds.

These investments are included in financial assets at fair value through profit or loss in the statement of financial position and no other risks relating to these investments have been identified other than those already disclosed in previous sections of this report.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS CONTINUED

for the year ended 31 December 2017

31 Financial risk management report *continued*

Credit risk *continued*

The exposure to investments in unconsolidated structured entities is disclosed in the following table:

Name and description	2017 R'000	Authorised programme/ market size	% of authorised programme size/market size	Fair value hierarchy	Debt ranking	Credit ranking	Underlying assets
Asset backed commercial paper	1	R25 billion	0.00%	Level 2 – 100%	Senior secured	A+	Instalment sales agreements Corporate loans Credit card receivables Bonds Equipment leases
Residential mortgage-backed securitisations	478 065	R6.39 billion	0.75%	Level 1 – 67.09% Level 2 – 32.91%	Senior secured	AAA: 81.55% Not rated: 18.45%	Prime home loans
Asset backed securitisations	319 613	R39.5 billion	3.51%	Level 1 – 48.51% Level 2 – 51.49%	Senior secured: 99.14% Junior debt: 0.86%	AA- to AAA: 78.92% Not rated: 21.08%	Vehicle loans Corporate loans Unsecured loans Equipment leases
Commercial mortgage-backed securitisations	19 624	R5.5 billion	0.36%	Level 2 – 100%	Senior secured	AAA	Commercial property
Collateralised loan obligations	41 450	R5 billion	0.83%	Level 1 – 68.63% Level 2 – 31.37%	Senior secured	AAA	Vehicle loans
Collective investment schemes	2 664	R52.8 billion	0.01%	Level 2		AA+	ABSA Money Market Fund
	10 661	R12.6 billion	0.08%	Level 2		AA-	Nedgroup Investments Core Income Fund Class C2
	44 048	R24.4 billion	0.18%	Level 2		AA+	Investec Money Market Fund
	2 627	R26.4 billion	0.01%	Level 2		AA+	Standard Bank Corporate Money Market Fund
	5 023	R13.7 billion	0.04%	Level 2		AA+	Investec Corporate Money Market Fund
	901 589	R4.5 billion	0.02%	Level 2		A	Investec Global Strategic Income Fund

31 Financial risk management report *continued*

Credit risk *continued*

Name and description	2016 R'000	Authorised programme/ market size	% of authorised programme size/market size	Fair value hierarchy	Debt ranking	Credit ranking	Underlying assets
Asset backed commercial paper	–	R25.3 billion	0.00%	Level 1 – 100%	Senior secured – 0.01% Secured – 99.99%	F1+: 100%	Instalment sales agreements Corporate loans Credit card receivables Bonds Equipment leases
Residential mortgage-backed securitisations	354 568	R43.6 billion	0.81%	Level 1 – 93.52% Level 2 – 6.48%	Senior secured – 78.65% Secured – 18.39% Senior Unsecured – 2.96%	A to AAA: 91.50% BBB: 2.16% Not Rated: 6.34%	Prime home loans
Asset backed securitisations	249 368	R27.7 billion	0.90%	Level 1 – 71.11% Level 2 – 28.89%	Senior secured – 89.89% Secured – 5.64% Senior Unsecured – 4.47%	A to AAA: 71.11% BBB: 0.34% Not Rated: 28.55%	Vehicle loans Corporate loans Unsecured loans Equipment leases
	24 401	R2.5 billion	0.98%	Level 1 – 100%	Senior secured	AA to AAA: 100%	Commercial property
Collateralised loan obligations	54 337	R17 billion	0.32%	Level 1 – 100%	Senior secured – 0.01% Secured – 59.41% Unsecured – 40.58%	AA to AAA: 100%	Vehicle loans
Collective investment schemes	3 692	R52.8 billion	0.01%	Level 2		AA+	ABSA Money Market Fund
	917	R14.0 billion	0.01%	Level 2		AA+	Nedgroup Investments Money Market Class C2
	1 468	R26.4 billion	0.01%	Level 2		AA+	Standard Bank Corporate Money Market Fund
	848	R13.7 billion	0.01%	Level 2		AA+	Investec Corporate Money Market Fund
	672 885	R4.5 billion	0.02%	Level 2		A	Investec Target Return Fund

NOTES TO THE ANNUAL FINANCIAL STATEMENTS CONTINUED

for the year ended 31 December 2017

31 Financial risk management report *continued*

Liquidity risk

Liquidity risk is the risk that the Scheme will not have sufficient liquid funds available to settle financial obligations as they fall due.

The Scheme's approach to managing liquidity is to ensure, with significant conservative margin, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Scheme's reputation. In order to meet the conflicting objective of enhancing returns while also providing high liquidity, the combined Scheme portfolios have explicit constraints that guarantee liquidity of at least 20% of the Scheme assets within a period of one week.

The Scheme has complied with the requirements regarding the nature and categories of assets as prescribed by Section 35 and Regulation 30 of the Act.

Approximately 98% (R1.8 billion) (2016: 94% – R1.6 billion) of the Scheme's insurance claim liabilities are settled within three months after the claim was incurred and the balance of the claims liability is settled within six months. The Scheme's remaining insurance liabilities are generally settled within 30 days.

A maturity analysis for financial liabilities carried at amortised cost, excluding liabilities arising from insurance contracts is provided below:

	Less than 1 year	Between 1 and 2 years	Between 2 and 5 years
As at 31 December 2017			
Personal Medical Savings Accounts (Note 8)	**4 656 633**	–	–
Trade and other payables (Note 9)	**538 930**	–	–
	5 195 563	–	–
As at 31 December 2016			
Personal Medical Savings Accounts (Note 8)	4 204 043	–	–
Trade and other payables (Note 9)	521 690	–	–
	4 725 733	–	–

Fair value estimation

Financial instruments

The fair value of financial instruments traded in active markets is based on quoted market prices at the reporting date. The quoted market price used for financial assets held by the Scheme is the current closing price.

The fair value of financial instruments that are not traded in an active market (for example, investments in pooled funds and collective investment schemes) is determined by using valuation techniques. These valuation techniques maximise the use of observable market data where it is available and rely as little as possible on entity-specific estimates. Specific valuation techniques used to value financial instruments include quoted market prices or dealer quotes for similar instruments.

The carrying value less impairment provision of trade receivables and payables are assumed to approximate their fair values due to their short term nature.

Personal Medical Savings Accounts

The members' Personal Medical Savings Accounts contain a demand feature. In terms of Regulation 10 of the Act, any credit balance on a member's Personal Medical Savings Account must be taken as a cash benefit when the member terminates his or her membership of the Scheme or benefit plan, and enrols in another benefit plan or medical scheme without a savings account or does not enrol in another medical scheme. Therefore the carrying values of the members' Personal Medical Savings Accounts are deemed to be equal to their fair values, which is the amount payable on demand.

31 Financial risk management report *continued*

Fair value hierarchy for financial assets measured at fair value

Assets measured at fair value

	Fair value measurement at end of the year using:			
R'000	R'000	Level 1	Level 2	Level 3
2017				
Financial assets at fair value through profit or loss:				
Offshore bonds	**1 463 064**	**601 503**	**861 561**	**–**
Equities	**3 378 331**	**3 313 762**	**64 569**	**–**
Yield-enhanced bonds	**3 721 190**	**2 291 984**	**1 429 206**	**–**
Inflation-linked bonds	**792 666**	**790 243**	**2 423**	**–**
Listed property investments	**382 024**	**382 024**	**–**	**–**
Money market instruments	**4 268 369**	**2 227 191**	**2 041 178**	**–**
	14 005 644	**9 606 707**	**4 398 937**	**–**
2016				
Financial assets at fair value through profit or loss:				
Offshore bonds	1 245 709	–	1 245 709	–
Equities	2 049 834	2 049 608	226	–
Yield-enhanced bonds	3 413 740	1 872 474	1 541 266	–
Inflation-linked bonds	610 476	587 154	23 322	–
Money market instruments	4 891 918	2 408 873	2 483 045	–
	12 211 677	6 918 109	5 293 568	–

The fair value assets are classified using a fair value hierarchy that reflects the significance of the inputs used in determining the measurements.

The fair value hierarchy has the following levels:

Level 1 – These are assets measured using quoted prices in an active market.

Level 2 – These are assets measured using inputs other than quoted prices included within Level 1 that are either directly or indirectly observable.

Level 3 – These are assets measured using inputs that are not based on observable market data.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS CONTINUED

for the year ended 31 December 2017

31 Financial risk management report *continued*

Fair value hierarchy for financial assets measured at fair value *continued*

The table below details the valuation techniques and observable inputs for assets falling under Level 2:

Description	Fair value as at 31 December 2017 R'000	Fair value as at 31 December 2016 R'000	Valuation techniques	Observable input
Financial assets at fair value through profit or loss:				
Unlisted:				
Debt securities	**2 293 190**	2 810 297	Reference to listed benchmark bond	Risk free yield to maturity curve, risk free zero curve
Money market securities	**2 041 178**	2 483 271	Discounted cash flow valuation, Black – Scholes model	Published exchange swap curve, published interest rate curve, published credit spread curve/implied credit spread curve, risk free yield to maturity curve, risk free zero curve, swap yield to maturity curve, swap zero curve
Unlisted equity	**64 569**	–	Discounted cash flow valuation	Risk free yield to maturity curve, risk free zero curve
	4 398 937	5 293 568		

Capital management

The Scheme is subject to the capital requirement imposed by Regulation 29 (2) of the Act, which requires a minimum solvency ratio of accumulated funds expressed as a percentage of gross annual contributions of 25%.

The Scheme's objectives when managing capital are to maintain the capital requirements of the Act, and to safeguard the Scheme's ability to continue as a going concern in order to provide benefits for its stakeholders.

The calculation of the regulatory capital requirement is set out below.

R'000	2017	2016
Total members' funds per Statement of Financial Position	**16 684 435**	14 234 461
Less: cumulative unrealised net gain on remeasurement of investments to fair value	**(298 722)**	–
Accumulated funds per Regulation 29	**16 385 712**	14 234 461
Gross annual contribution income	**59 710 735**	54 056 212
Solvency margin		
= Accumulated funds / gross annual contribution income x 100	**27.44%**	26.33%

At 31 December 2017, the Scheme's regulatory capital level of 27.44% (2016: 26.33%) was R1.46 billion (2016: R719 million) more than the statutory capital requirement of 25%.

32 Critical accounting estimates and judgements

Critical accounting estimates and assumptions

The Scheme 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 are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

Outstanding claims provision

The critical estimates and judgements relating to the outstanding claims provision are set out under Note 30.

Other risk transfer arrangements

The critical estimates and judgements relating to other risk transfer arrangements are set out under Note 11.

Impairment of assets

The critical estimates made by the Scheme are set out under Note 31 and judgements relating to the impairment of assets are set out under Note 7 of the Accounting policies.

33 Non-compliance matters

The Council for Medical Schemes issued Circular 11 of 2006 (the Circular) dealing with issues to be addressed in the audited financial statements of medical schemes. The Circular requires that all non-compliance matters noted should be disclosed in the audited financial statements, irrespective of whether the auditor considers it to be material or immaterial.

During the year the Scheme did not comply with the following Sections and Regulations of the Act.

- **Statutory Scheme Solvency**

  Under the Act, medical schemes are required to hold a minimum of 25% of gross annual contribution income as a reserve or accumulated funds (also known as the solvency ratio). The solvency ratio is a measure of a scheme's ability to absorb unexpected changes in claims experience, demographics (e.g. average age, chronic profile, etc.) and legislative environments, and therefore reflects a scheme's financial strength.

  During 2017, the Scheme's solvency level dropped below 25% during January. The reason for the drop below 25% was attributable to the impact of annual contribution increases (schemes are required to hold reserves equal to annualised inflation-adjusted contributions from the first day of the financial year). Negative claims experience during November, in line with historic trends, also caused the solvency ratio to drop below 25%.

  At 31 December 2017, the Scheme's accumulated funds expressed as a percentage of gross annual contributions was 27.44% (2016: 26.33%), which exceeds the statutory solvency requirement of 25%.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS CONTINUED

for the year ended 31 December 2017

33 Non-compliance matters *continued*

- **Sustainability of Benefit Plans**

In terms of Section 33 (2) of the Act, each benefit plan is required to be self-supporting in terms of membership and financial performance, and be financially sound.

For the year ended 31 December 2017 the following plans did not comply with Section 33 (2):

	Net healthcare result (R'000)	Net surplus/ (deficit) (R'000)
Benefit plan		
Executive	**(334 418)**	**(324 005)**
Classic Comprehensive	**(963 232)**	**(819 810)**
Classic Comprehensive Zero MSA	**(2 763)**	**(1 514)**
KeyCare Plus	**(535 785)**	**(212 254)**

The performance of all benefit options is monitored on a continuous basis with a view to improving their financial outcomes, and different strategies are continually evaluated to address the deficit in these plans while considering the overall financial stability of the Scheme.

When structuring benefit options, the financial sustainability of all the options is considered. The different financial positions reflect the different disease burdens in each option, among many other factors. The Scheme's strategy on the sustainability of plans has to balance short- and long-term financial considerations, fairness to both healthy and sick members, and continued affordability of cover for members with different levels of income and healthcare needs. While the Scheme is committed to complying wherever possible with the applicable legislation, it also focuses intensively on the overall stability and financial position of the Scheme as a whole and not only individual benefit plans.

In addition, DHMS continually provides the Registrar with updates on both the Scheme and individual benefit option performance through the monthly management accounts and quarterly monitoring meetings.

- **Investments in Employer Groups and Medical Scheme Administrators**

Section 35 (8) (a) and (c) of the Act states that a medical scheme shall not invest any of its assets in the business of an employer who participates in the Scheme, or any administrator or any arrangement associated with the Scheme. The Scheme has investments in certain employer groups and companies associated with medical scheme administration within its diversified investment portfolio. This situation occurs industry-wide. CMS granted DHMS exemption from these sections of the Act up to 21 April 2018.

- **Investments in other assets in territories outside the Republic of South Africa**

The Scheme's offshore bond managers utilise derivative instruments to aid with efficient portfolio construction and management, and to reduce the overall risk within our portfolios. The derivatives used are highly liquid and are either exchange traded or governed by International Swaps and Derivatives Association agreements. The derivative instruments are not used for speculation and there is no gearing or leverage applied. Investments in derivatives in territories outside the Republic of South Africa are, however, prohibited in terms of Category 7 (b) of Annexure B to the Regulations of the Act.

The Scheme was granted an exemption to invest in offshore derivatives, subject to certain conditions, up to 31 December 2018.

33 Non-compliance matters *continued*

- **Contributions received after due date**

  Section 26 (7) of the Act states that all subscriptions or contributions shall be paid directly to a medical scheme not later than three days after payment becomes due. There are instances where the Scheme received contributions after the three days; however, there are no contracts in place agreeing to this practice. It is important to note that the Scheme has no control over the timely payment of contributions. The legal obligation resides with the members/employers to pay contributions within the prescribed period.

  However, DHMS employs robust credit control processes dealing with the collection of outstanding contributions, including the suspension of membership for non-payment.

- **Broker fees paid**

  In terms of Regulation 28 (5) of the Act, broker fees shall be paid on a monthly basis on receipt by a medical scheme of the relevant monthly contribution in accordance with the maximum amount payable per Regulation 28 (2), limited to one broker as required by Regulation 28 (8).

  In some instances brokers were compensated prior to receipt of the relevant monthly contribution, the amount paid was more than the prescribed amount and more than one broker per member was paid. In the instances where brokers were paid above the prescribed amount or more than one broker was paid, the value is negligible and represents less than 0.01% of the total broker fees paid for the year. The exceptions relate to transactions that do not occur frequently and the Administrator has developed exception reporting to identify and correct these transactions, and has a well-established claw-back system to rectify commission overpayments.

- **Minimum amount invested in cash [Category 1 (a) (i) and 1 (a) (ii)]**

  Explanatory note 2 to Annexure B to the Regulations of the Act requires a medical scheme to have a minimum of 20% of its Regulation 30 assets invested in cash [Category 1 (a) (i) and 1 (a) (ii)]. As at 31 March 2017, the Scheme did not meet this requirement as it held 19.79% in cash [Category 1 (a) (i) and 1 (a) (ii)]. The non-compliance was due to a difference in interpretation between the CMS and DHMS of the relevant clauses of Regulation 30 of the Act. The Scheme has amended its calculation methodology to be aligned with the CMS interpretation.

  Prior to Circular 2 of 2018: Personal Medical Savings Accounts and scheme rules, Personal Medical Savings Account (PMSA) assets were included as part of the Scheme's assets during the period July to December 2017. The PMSA assets were included in assessing compliance with the requirement for a minimum of 20% of Regulation 30 assets being invested in cash [Category 1 (a) (i) and 1 (a) (ii)]. After excluding PMSA assets from Scheme assets, there were certain months where this requirement was not met.

  As at 31 December 2017, 32.51% of Scheme assets were invested in cash [Category 1 (a) (i) and 1 (a) (ii)] and therefore met the minimum 20% requirement. This requirement has been met using the amended calculation methodology and excluding PMSA assets.

- **Waiting periods**

  Section 29A of the Act states the instances when medical schemes may impose waiting periods upon a person in respect of whom an application is made for membership or admission as a dependent. The waiting periods range from a three month general waiting period to a twelve month condition-specific waiting period. During the year under review there were isolated instances where waiting periods were not applied in accordance with the Act. For the instances identified, the incorrect application of waiting periods has been rectified and a review conducted which confirmed that no claims were rejected as a result of the waiting periods being incorrectly applied.

- **Prescribed minimum benefits**

  Section 29 (1) (o) and Regulation 8 provides the scope and level of minimum benefits that the Scheme must provide to members and dependants. During the year under review there were isolated instances where the Scheme did not pay claims in accordance with the scope and level of minimum benefits. The claims were reprocessed and correctly paid prior to the end of the benefit year.