For the benefit of our

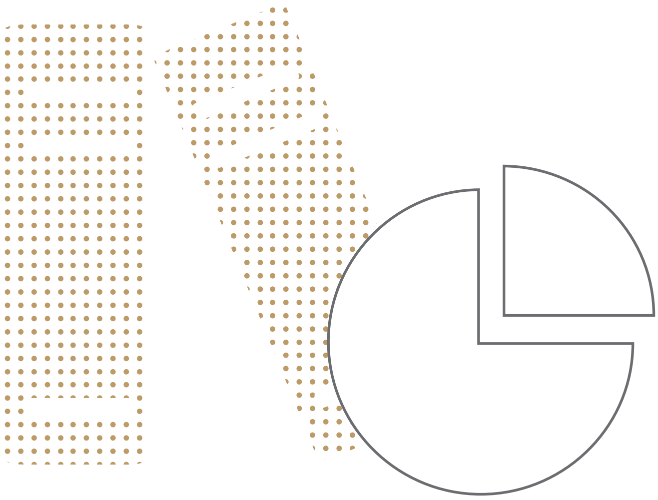
members

2016 Integrated Annual Report

2016
Integrated Annual Report

Discovery Health Medical Scheme's Integrated Annual 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. Below we describe what is in each chapter and its intended audience.

06 Financials



STATEMENT OF RESPONSIBILITY BY THE BOARD OF TRUSTEES

for the year ended 31 December 2016

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 2016, 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, No 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 2017. 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 87 to 89. The Annual Financial Statements, which are presented on pages 90 to 153 were approved by the Board of Trustees on 6 April 2017 and are signed on its behalf by:

M VAN DER NEST	D NAIDOO	M STREAK[1]
CHAIRPERSON	**TRUSTEE**	**PRINCIPAL OFFICER**

1 *Mr Streak was the Principal Officer during 2016, and resigned with effect from 31 December 2016.*

REPORT OF THE AUDIT COMMITTEE

for the year ended 31 December 2016

We are pleased to present our report for the financial year ended 31 December 2016. 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

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.

Audit Committee members, meeting attendance and assessment

The Committee consists of four independent members and three Trustee members and meets at least four times per year. The Committee met four times during 2016.

The executive officers of the Scheme and representatives of the Administrator attend meetings or parts of meetings by invitation. Internal Audit and the External Auditor attend meetings or parts of meetings by invitation. Internal Audit and the External Auditor are also afforded the opportunity to meet with the Committee, after each meeting, without the Administrator present.

Members of the Committee collectively keep up to date with key developments affecting their required skill set. The effectiveness of the Committee and its individual members is assessed annually. The last assessment was performed at the end of 2016. Based on the result of the assessment, the Committee is satisfied with its effectiveness.

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.

The membership and attendance of the members of the Committee are as follows:

		16 Mar	16 Aug	23 Aug	31 Oct
Independent Member/Chair	Mr Barry Stott	✓	✓	✓	✓
Trustees	Ms Daisy Naidoo[1]	✓	✓	✓	✓
	Mr Giles Waugh	✓	✓	✓	✓
	Mr Neil Morrison[2]	–	✓	✓	✓
Independent Members	Ms Susan Ludolph[3]	✓	✓	✓	✓
	Mr Steven Green	✓	✓	✓	✓
	Ms Philile Maphumulo[3]	✓	✓	✓	✓
	Mr Dave King[4]	✓	–	–	–

1 *Term as a Trustee ended on 23 June 2016.*

2 *Elected as a Trustee on 23 June 2016.*

3 *Appointed to the Committee on 20 January 2016.*

4 *Elected as a Trustee on 23 June 2016 and subsequently resigned as member of the Audit Committee.*

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 2016 to 31 December 2016 in accordance with section 36(2) of the Medical Schemes Act 131 of 1998 on 11 October 2016.

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 2016. The Committee approved the actual audit fees for the year ended 31 December 2015.

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.

REPORT OF THE AUDIT COMMITTEE *continued*

for the year ended 31 December 2016

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 Standards, the Medical Schemes Act 131 of 1998 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 the relevant Scheme charters, codes and relevant legal, regulatory and other obligations. The Committee is satisfied that there has been no material breach of these standards or material non-compliance with laws and regulations, except for the matters of non-compliance with the Act as detailed in Note 34 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.

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 2016, as well as the budget for the year ending 31 December 2017. Total members' funds exceeded R14.2 billion with a solvency level of 26.33% as at 31 December 2016. 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 2016 to cover its monthly claims expenditure 4.79 times.

On the basis of this review and taking note of the current net surplus of R1.3 billion, the Committee considers that:

- The Scheme's assets currently exceeds its liabilities; and
- 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
6 April 2017

INDEPENDENT AUDITOR'S REPORT

To the members of Discovery Health Medical Scheme

Report on the audit of financial statements

Opinion

We have audited the financial statements of Discovery Health Medical Scheme (the Scheme), set out on pages 90 to 153, which comprise the statement of financial position as at 31 December 2016, 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 Discovery Health Medical Scheme as at 31 December 2016, 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 judgment, 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 of R1,121 million at year-end, described in Notes 6 and 31 to the financial statements, is a provision recognised for claims incurred by members prior to year-end but only reported to the Scheme after year-end. The outstanding claims provision is calculated by the Scheme's actuaries using 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 that are used to project claims to an ultimate position which is subsequently used to estimate the outstanding claims provision. We identified this as a matter of most significance in our audit because of the impact of estimation uncertainty on the projected claim development pattern. A material change in the actual claims pattern or a change in timing or value can cause a material change in the provision.	For a sample of actual claims received in the 2016 financial year, we tested the accuracy of the service and process dates and no inconsistencies were identified during our testing. We made use of various data analytics to substantively test the different 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 difference noted. We obtained an understanding from the Scheme's actuaries regarding the process to calculate the outstanding claims provision. The Scheme applied a combination of BCL and CPE methods, which 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 difference was 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 based on the outcome of the procedures described above, we accepted the reasonability of Scheme's provision.

INDEPENDENT AUDITOR'S REPORT *continued*

Other information

The Scheme's trustees are responsible for the other information. The other information comprises the Statement of Responsibility by the Board of Trustees, the Audit Committee's Report and the Integrated Annual Report. Other information 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 identified above 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 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's 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 34 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 and November 2016. However, at 31 December 2016, the Scheme's accumulated funds expressed as a percentage of gross annual contributions was 26.33% which exceeds the statutory solvency requirement of 25%, as disclosed in note 34 of the financial statements.

PricewaterhouseCoopers Inc.

PricewaterhouseCoopers Inc.
Director: C Volschenk
Registered Auditor
Johannesburg
6 April 2017

STATEMENT OF FINANCIAL POSITION

as at 31 December 2016

R'000	Notes	2016	2015
ASSETS			
Non-current assets		**5 614**	1 071
Long Term Employee Benefit Plan asset	27	**5 614**	1 071
Current assets		**20 864 905**	18 897 501
Financial assets at fair value through profit or loss	2	**12 211 677**	11 399 332
Derivative financial instruments	7	**54 760**	–
Trade and other receivables	3	**2 058 008**	1 632 586
Cash and cash equivalents			
– Personal Medical Savings Account trust assets	4	**4 142 672**	3 667 456
– Medical Scheme assets	5	**2 397 788**	2 198 127
Total assets		**20 870 519**	18 898 572
FUNDS AND LIABILITIES			
Members' funds		**14 234 461**	12 929 011
Accumulated funds		**14 234 461**	12 929 011
Current liabilities		**6 636 058**	5 969 561
Outstanding claims provision	6	**1 121 394**	985 087
Derivative financial instruments	7	**4 376**	65 210
Personal Medical Savings Account trust liabilities	8	**4 204 043**	3 736 659
Trade and other payables	9	**1 306 245**	1 182 605
Total funds and liabilities		**20 870 519**	18 898 572

STATEMENT OF COMPREHENSIVE INCOME

for the year ended 31 December 2016

R'000	Notes	2016	Restated 2015
Risk contribution income	10	**43 626 398**	40 066 741
Relevant healthcare expenditure		**(38 035 898)**	(34 503 627)
Net claims incurred*	11	**(36 613 210)**	(33 160 818)
Claims incurred*	11	**(36 772 332)**	(33 231 554)
Third party claim recoveries	11	**159 122**	70 736
Accredited managed healthcare services (no risk transfer)	12	**(1 407 267)**	(1 305 790)
Net (loss) on risk transfer arrangements*	13	**(15 421)**	(37 019)
Risk transfer arrangement fees		**(366 344)**	(344 093)
Recoveries from risk transfer arrangements*		**350 923**	307 074
Gross healthcare result		**5 590 500**	5 563 114
Broker service fees	14	**(1 101 648)**	(982 874)
Expenses for administration	27	**(4 150 194)**	(3 874 896)
Other operating expenses	15	**(236 206)**	(198 387)
Net healthcare result		**102 452**	506 957
Other income		**1 524 116**	1 033 020
Investment income	21	**1 257 479**	1 018 998
Net gains on financial assets at fair value through profit or loss	22	**264 278**	6 504
Sundry income	23	**2 359**	7 518
Other expenditure		**(321 118)**	(263 837)
Expenses for asset management services rendered		**(31 076)**	(31 578)
Interest paid	24	**(290 042)**	(232 259)
Net surplus for the year		**1 305 450**	1 276 140
Other comprehensive income		**–**	–
Total comprehensive income for the year		**1 305 450**	1 276 140

* *See note 13 to the Annual Financial Statements for explanatory note on change of disclosure.*

STATEMENT OF CHANGES IN FUNDS AND RESERVES

for the year ended 31 December 2016

R'000	Note	2016 Accumulated funds	2015 Accumulated funds
Balance at beginning of the year		**12 929 011**	11 652 804
Total comprehensive income for the year		**1 305 450**	1 276 140
Reserves transferred from other medical schemes	25	**–**	67
Total member funds end of the year		**14 234 461**	12 929 011

STATEMENT OF CASH FLOWS

for the year ended 31 December 2016

R'000	Notes	2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES			
Cash flows generated from operations before working capital changes	29	**151 902**	555 793
Working capital changes:			
(Increase) in trade and other receivables	29.1	**(500 589)**	(99 229)
Increase in outstanding claims provision		**136 307**	139 292
Increase in Personal Medical Savings Accounts		**467 384**	485 916
Increase in trade and other payables	29.2	**123 640**	151 366
Cash generated by operations		**378 644**	1 233 138
Purchases of financial instruments	29.3	**(1 922 170)**	(6 176 902)
Proceeds from sale of financial instruments	29.4	**1 258 510**	4 339 081
(Increase) in Long Term Employee Plan Asset		**(7 544)**	–
Cash transferred from other medical scheme		**–**	67
Interest received	21	**1 206 486**	981 460
Dividend income	21	**50 993**	37 729
Interest paid	24	**(290 042)**	(232 259)
Net cash flows from operating activities		**674 877**	182 314
NET INCREASE IN CASH AND CASH EQUIVALENTS		**674 877**	182 314
Cash and cash equivalents at beginning of year		**5 865 583**	5 683 269
CASH AND CASH EQUIVALENTS AT END OF YEAR		**6 540 460**	5 865 583
Cash and cash equivalents comprise			
Personal Medical Savings Accounts trust assets	4	**4 142 672**	3 667 456
Medical Scheme assets	5	**2 397 788**	2 198 127
		6 540 460	5 865 583

ACCOUNTING POLICIES

for the year ended 31 December 2016

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 No. 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 6 April 2017.

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 33.

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.

New standards, amendments and interpretations effective in 2016 and relevant to the Scheme:
The following standards and amendments for the current accounting period have been adopted. These new accounting standards and amendments have not had any material impact on the Scheme's financial results or disclosure in the financial statements.

Standard	Scope	Effective date
IAS 1 (Amendment): Presentation of financial statements	The amendments clarify guidance on materiality and aggregation, the presentation of subtotals, the structure of financial statements and the disclosure of accounting policies.	1 January 2016
IAS 19 (Amendment): Employee Benefits	Discount rate: regional market issue – This amendment clarifies that market depth of high-quality corporate bonds is assessed based on the currency in which the obligation is denominated, rather than the country where the obligation is located. When there is no deep market for high-quality corporate bonds in that currency, government bond rates must be used.	1 January 2016

ACCOUNTING POLICIES *continued*

for the year ended 31 December 2016

1 Basis of preparation *continued*

New standards, amendments and interpretations effective in 2016 and not relevant to the Scheme:

Standard	Scope	Effective date
IAS 16 (Amendment): Property, plant and equipment and IAS 38 (Amendment): Intangible assets	This amendment clarifies that the use of revenue-based methods to calculate the depreciation of an asset is not appropriate because revenue generated by an activity that includes the use of an asset generally reflects factors other than the consumption of the economic benefits embodied in the asset. The amendment also clarifies that revenue is generally presumed to be an inappropriate basis for measuring the consumption of the economic benefits embodied in an intangible asset.	1 January 2016
IAS 27 (Amendment): Separate financial statements	This amendment restores the option to use the equity method to account for investments in subsidiaries, joint ventures and associates in an entity's separate financial statements.	1 January 2016
IAS 34 (Amendment): Interim Financial Reporting	This amendment states that the required interim disclosures must either be in the interim financial statements or incorporated by cross-reference between the interim financial statements and wherever they are included within the greater interim financial report. Other information within the interim financial report must be available to users on the same terms as the interim financial statements and at the same time.	1 January 2016
IFRS 5 (Amendment): Non-current Assets Held for Sale and Discontinued Operations	This is an amendment to the changes in methods of disposal. Assets (or disposal groups) are generally disposed of either through sale or through distribution to owners. The amendment to IFRS 5 clarifies that changing from one of these disposal methods to the other should not be considered to be a new plan of disposal, rather it is a continuation of the original plan. There is therefore no interruption of the application of the requirements in IFRS 5. The amendment also clarifies that changing the disposal method does not change the date of classification.	1 January 2016
IFRS 7 (Amendment): Financial Instruments: Disclosures	Applicability of the offsetting disclosures to condensed interim financial statements – The amendment removes the phrase 'and interim periods within those annual periods' from paragraph 44R, clarifying that these IFRS 7 disclosures are not required in the condensed interim financial report. However, IAS 34 requires an entity to disclose an explanation of events and transactions that are significant to an understanding of the changes in financial position and performance of the entity since the end of the last annual reporting period. Servicing contracts – The amendment clarifies that a servicing contract that includes a fee can constitute continuing involvement in a financial asset. An entity must assess the nature of the fee and arrangement against the guidance for continuing involvement in paragraphs IFRS 7.B30 and IFRS 7.42C in order to assess whether the disclosures are required.	1 January 2016
IFRS 11 (Amendment): Joint arrangements	This amendment adds new guidance on how to account for the acquisition of an interest in a joint operation that constitutes a business. The amendments specify the appropriate accounting treatment for such acquisitions.	1 January 2016

1 Basis of preparation *continued*

New standards, amendments and interpretations effective in 2016 and not relevant to the Scheme:

Standard	Scope	Effective date
IFRS 10 (Amendment): Consolidated financial statements and IAS 28 (Amendment): Investments in associates and joint ventures	This amendment eliminates the inconsistency between IFRS 10 and IAS 28. If the non-monetary assets sold or contributed to an associate or joint venture constitute a 'business', then the full gain or loss will be recognised by the investor. A partial gain or loss is recognised when a transaction involves assets that do not constitute a business, even if these assets are housed in a subsidiary. The amendment also clarifies the application of the consolidation exception for investment entities and their subsidiaries.	1 January 2016
IFRS 14: Regulatory deferral accounts	This is an interim standard on the accounting for certain balances that arise from rate-regulated activities. Rate regulation is a framework where the price that an entity charges to its customers for goods and services is subject to oversight and/or approval by an authorised body.	1 January 2016
IAS 16 (Amendment): Property, plant and equipment and IAS 41 (Amendment): Agriculture	This amendment to IAS 16 has scoped in bearer plants, but not the produce on bearer plants. It further explains that a bearer plant not yet in the location and condition necessary to bear produce is treated as a self-constructed asset. The amendment to IAS 41 has adjusted the definition of a bearer plant, include examples of non-bearer plants and remove current examples of bearer plants from IAS 41.	1 January 2016

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 to the Scheme's results but may result in additional disclosure in the financial statements.

Standard	Scope	Effective date
IFRS 16: Leases IFRS 16 supersedes IAS 17: Leases, IFRIC 4: Determining whether an arrangement contains a lease, SIC 15: Operating lease – Incentives, and SIC 27: Evaluating the substance of transactions involving legal form of a lease	The new standard requires lessees to recognise assets and liabilities arising from all leases in the statement of financial position. Lessor accounting has not substantially changed in the new standard. A lessee will measure the lease liabilities at the present value of future lease payments. The lease asset will initially be the same amount as lease liabilities, including costs directly related to entering into the lease. Lease assets will be amortised in a similar way to other assets such as property, plant and equipment. A lessee will not be required to recognise assets and liabilities for short-term leases (less than 12 months), and leases for which the underlying asset is of low value (such as laptops and office furniture.)	1 January 2019
IFRS 15: Revenue from contracts with customers	Establishes principles for accounting the nature, amount, timing and uncertainty of revenue arising from an entity's contracts with customers.	1 January 2018
IFRS 9 (Amendment): Financial instruments	This standard introduces new requirements for the classification and measurement of financial assets by introducing a fair value through other comprehensive income category for certain debt instruments. It also contains a new impairment model which will result in earlier recognition of losses. No changes were introduced for the classification and measurement of financial liabilities, except for the recognition of changes in own credit risk in other comprehensive income for liabilities designated at fair value through profit or loss.	1 January 2018

ACCOUNTING POLICIES *continued*

for the year ended 31 December 2016

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.

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 assets and liabilities of the parties to amalgamations shall vest and become binding upon the party to which the transfer 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

Financial assets carried at amortised cost

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 2016

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 Accounts 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 that Act.

Advances on savings contributions are funded from the Scheme's funds and the risk of impairment 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 31.

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 2016

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.

21 Employee benefits *continued*

Other long term employee benefit

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 32 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 unrelated asset managers who apply various investment strategies to accomplish their respective investment objectives. The investment strategy does not include the use of leverage.

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 2016

R'000	2016	2015

1 Accounting policies

The accounting policies of the Scheme are set out on pages 93 to 101.

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:

R'000	2016	2015
Current assets	**12 211 677**	11 399 332
– Offshore bonds	**1 245 709**	1 335 137
– Equities	**2 049 834**	1 415 647
– Yield-enhanced bonds	**3 413 740**	3 058 012
– Inflation-linked bonds	**610 476**	464 574
– Money market instruments	**4 891 918**	5 125 962
	12 211 677	11 399 332

Reconciliation of the balance at the beginning of the year to the balance at the end of the year:

R'000	2016	2015
At the beginning of the year	**11 399 332**	9 474 520
Acquisitions	**1 922 170**	6 176 902
Disposals	**(1 127 159)**	(4 465 329)
Net gains on revaluation of financial assets at fair value through profit or loss (Note 22)	**17 334**	213 239
At the end of the year	**12 211 677**	11 399 332

A register of investments is available for inspection at the registered office of the Scheme.

3 Trade and other receivables

Insurance receivables

R'000	2016	2015
Contribution receivables	**1 629 627**	1 386 504
Contributions outstanding	**1 639 386**	1 396 137
Less: Provision for impairment	**(9 759)**	(9 633)
Member and service provider claims receivables	**84 190**	70 316
Amount due	**341 473**	278 845
Less: Provision for impairment	**(257 283)**	(208 529)
Other risk transfer arrangements	**24 426**	7 520
Recoveries due from other risk transfer arrangements	**6 718**	5 051
Share of outstanding claims provision (Note 6)	**17 708**	2 469
Broker fee receivables	**1 084**	111
Amounts due from brokers	**1 948**	895
Less: Provision for impairment	**(864)**	(784)
Other insurance receivables	**138 781**	60 869
Total receivables arising from insurance contracts	**1 878 108**	1 525 320

R'000	2016	2015

3 Trade and other receivables *continued*

	2016	2015
Loans and receivables		
Balance due by related party	**20 540**	12 024
Discovery Third Party Recovery Services (Pty) Ltd (Note 27)	**20 540**	12 024
Sundry accounts receivable	**157 670**	93 797
Interest receivable	**1 690**	1 445
Total receivables arising from loans and receivables	**179 900**	107 266
	2 058 008	1 632 586

At 31 December 2016 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)

	2016	2015
PERSONAL MEDICAL SAVINGS ACCOUNT TRUST PORTFOLIO		
(Managed by Aluwani Capital Partners (Pty) Ltd) (previously Momentum Asset Management)		
Balance at beginning of the year	**1 832 987**	1 594 575
Net additional Investments	**82 668**	120 220
Interest Income	**154 364**	118 267
Amortised cost adjustments	**1 372**	(75)
Balance at the end of the year	**2 071 391**	1 832 987
PERSONAL MEDICAL SAVINGS ACCOUNT TRUST PORTFOLIO		
(Managed by Taquanta Asset Managers (Pty) Ltd)		
Balance at beginning of the year	**1 834 469**	1 594 214
Net additional Investments	**86 660**	127 524
Interest Income	**150 152**	112 731
Balance at the end of the year	**2 071 281**	1 834 469
Total Personal Medical Savings Account trust assets	**4 142 672**	3 667 456

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 trust assets and Personal Medical Savings Account trust 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 7.64% (2015: 6.91%).

NOTES TO THE ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 December 2016

R'000	2016	2015
5 Cash and cash equivalents – medical scheme assets		
Current accounts	**940 981**	842 123
Money market instruments	**1 456 807**	1 356 004
	2 397 788	2 198 127
At 31 December 2016 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	**1 103 686**	982 618
Outstanding claims provision – covered by risk transfer arrangements	**17 708**	2 469
	1 121 394	985 087
Analysis of movement in outstanding claims		
Balance at beginning of the year	**985 087**	845 795
Payments in respect of prior year	**(951 858)**	(872 043)
Over/(under) provision in prior year (Note 11)	**33 229**	(26 248)
Outstanding claims provision raised in current year	**1 088 165**	1 011 335
Not covered by risk transfer arrangements	**1 070 457**	1 008 866
Covered by risk transfer arrangements (Note 3)	**17 708**	2 469
Balance at end of the year	**1 121 394**	985 087
Analysis of outstanding claims provision		
Estimated gross claims	**1 192 494**	1 059 065
Less:		
Estimated recoveries from savings plan accounts (Note 8)	**(71 100)**	(73 978)
Balance at end of the year	**1 121 394**	985 087

R'000	2016	2015
7 Derivative financial instruments		
Financial assets held at fair value through profit or loss		
Current assets		
– Derivative financial instruments	**54 760**	–
Financial liabilities held at fair value through profit or loss		
Current liabilities		
– Derivative financial instruments	**(4 376)**	(65 210)
Derivative financial asset/(liability) at the end of the year	**50 384**	(65 210)
Reconciliation of the balance at beginning of the year to the balance at the end of the year:		
Derivative financial (liability)/asset at the beginning of the year	**(65 210)**	16 731
Net realised (gains)/losses on derivative financial instruments (Note 29.4)	**(131 351)**	126 248
Realised gains on derivative financial instruments	**(136 710)**	(36 137)
– Equity portfolio derivatives	**(693)**	(2 852)
– Zero-cost equity collars	**–**	(785)
– Zero-cost currency collars	**(136 017)**	(32 500)
Realised losses on derivative financial instruments	**5 359**	162 385
– Bond portfolio derivatives	**3 719**	–
– Zero-cost currency collars	**1 640**	162 385
Net fair value gains/(losses) on derivative financial instruments (Note 22)	**246 944**	(208 189)
Gains on revaluation of derivative financial instruments to fair value	**255 039**	8 823
– Equity portfolio derivatives	**9 138**	8 823
– Zero-cost equity collars	**91 072**	–
– Zero-cost currency collars	**154 829**	–
Losses on revaluation of derivative financial instruments to fair value	**(8 095)**	(217 012)
– Equity portfolio derivatives	**–**	(5 738)
– Zero-cost equity collars	**–**	(63 629)
– Zero-cost currency collars	**–**	(147 645)
– Bond portfolio derivatives	**(8 095)**	–
Derivative financial asset/(liability) at the end of the year	**50 384**	(65 210)

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 32).

NOTES TO THE ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 December 2016

8 Personal Medical Savings Account trust liabilities

R'000	2016	2015
(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	**3 736 659**	3 250 743
Add:		
Personal Medical Savings Accounts contributions received or receivable	**10 429 814**	9 693 015
For the current year (Note 10)	**10 429 814**	9 693 015
Interest on Personal Medical Savings Accounts (Note 24)	**287 923**	232 141
Transfers received from other medical schemes	**13 691**	19 815
Less:		
Claims paid to or on behalf of members (Note 11)	**(9 942 225)**	(9 199 956)
Refunds on death or resignation	**(321 819)**	(259 099)
Balance due to members on Personal Medical Savings Accounts held in trust at the end of the year	**4 204 043**	3 736 659

It is estimated that claims to be paid out of members' Personal Medical Savings Accounts in respect of claims incurred in 2016 but not reported will amount to approximately R71 100 056 (2015: R73 978 313) (Note 6).

As at 31 December 2016 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.

9 Trade and other payables

R'000	2016	2015
Insurance payables		
Contributions received in advance	**137 260**	119 036
Contribution refunds due to employers	**1 804**	1 494
Reported claims not yet paid	**548 257**	506 752
Balance at the beginning of the year	**506 752**	334 519
Net movement for the year	**41 505**	172 233
Broker fee creditors	**97 234**	87 618
Accredited brokers	**97 234**	87 618
Total liabilities arising from insurance contracts	**784 555**	714 900
Financial liabilities		
Balance due to related parties	**469 924**	437 982
Discovery Health (Pty) Ltd (Note 27)	**469 924**	437 982
Unallocated funds	**2 438**	11 727
Total accruals	**49 328**	17 996
General accruals	**49 268**	17 996
Leave pay provision	**60**	–
Total arising from financial liabilities	**521 690**	467 705
	1 306 245	1 182 605

At 31 December 2016 the carrying amounts of insurance and other payables approximate their fair values due to the short term maturities of these liabilities.

R'000	2016	Restated 2015
10 Risk contribution income		
Gross contributions per registered Scheme rules	**54 056 212**	49 759 756
Less:		
Personal Medical Savings Account contributions (Note 8)	**(10 429 814)**	(9 693 015)
	43 626 398	40 066 741
11 Net claims incurred		
Current year claims per registered Scheme rules	**46 578 250**	42 292 218
Claims not covered by risk transfer arrangements*	**46 227 327**	41 985 144
Claims covered by risk transfer arrangements (Note 13)*	**350 923**	307 074
Movement in outstanding claims provision	**136 307**	139 292
(Over)/under provision in prior year (Note 6)	**(33 229)**	26 248
Adjustment for current year	**169 536**	113 044
	46 714 557	42 431 510
Less:		
Claims charged to members' Personal Medical Savings Accounts (Note 8)	**(9 942 225)**	(9 199 956)
Claims incurred	**36 772 332**	33 231 554
Third party claim recoveries	**(159 122)**	(70 736)
	36 613 210	33 160 818

* *See note 13 to the Annual Financial Statements for explanatory note on change of disclosure.*

Risk transfer arrangements

During 2016 the Scheme had six (2015: four) risk transfer arrangements in place. The methodologies used to determine the claims covered by these arrangements are set out below.

1. 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 2016 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 2016 PLPM rate is multiplied by the lives exposure for this arrangement's membership.

2. 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.

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

   The cost of the dental group of 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 2016

11 Net claims incurred *continued*

4. 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.

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

   The Scheme contracted with two providers as Designated Service Providers (DSP) to provide acute medication dispensing services for Smart plan (newly introduced benefit option in 2016) members. The Scheme remunerates the DSP's 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	2016	2015

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.

R'000	2016	2015
Discovery Health (Pty) Ltd		
Active Disease Risk Management Services and Disease Risk Management Support Services	**453 235**	420 464
Hospital Benefit Management Services	**420 400**	390 431
Managed Care Network Management Services and Risk Management Services	**390 788**	363 010
Pharmacy Benefit Management Services	**142 844**	131 885
	1 407 267	1 305 790

R'000	2016	Restated 2015

13 Net (loss) on risk transfer arrangements*

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

R'000	2016	Restated 2015
Risk transfer arrangements fees	**(366 344)**	(344 093)
Recoveries under risk transfer arrangements (Note 11)	**350 923**	307 074
	(15 421)	(37 019)

* *For certain of these arrangements, the Scheme settles claims on behalf of the risk transfer providers. These claims are subsequently recovered from these providers. In prior periods, these recoveries were disclosed as part of "Recoveries under risk transfer arrangements". During the year under review, this disclosure has been reviewed to only include the estimated recoveries under risk transfer arrangements in line with industry practice. This disclosure change has no impact on the Gross healthcare result, the Net healthcare result or the Net surplus previously presented. Total recoveries under risk transfer arrangements and net claims incurred during 2015 was previously presented as R95 million higher, representing the amount of actual recoveries under risk transfer arrangements.*

R'000	2016	Restated 2015
14 Broker service fees		
Brokers' fees	**1 101 648**	982 874
	1 101 648	982 874
15 Other operating expenses		
Association fees	**1 616**	240
Audit fees	**11 594**	5 432
Audit services for the year ended 2016	**1 661**	–
Audit services for the year ended 2015	**2 462**	2 015
Audit services for the year ended 2014	**–**	2 550
Other services	**7 471**	867
Audit and Risk Committee fees (Note 16)*	**1 755**	1 246
Audit Committee	**1 167**	835
Risk Committee	**588**	411
Bank charges	**10 681**	10 379
Clinical Governance Committee fees	**375**	74
Council for Medical Schemes	**40 631**	38 202
Debt collecting fees	**3 850**	3 222
Dispute Committee fees	**871**	478
Fidelity Guarantee Insurance	**226**	224
General meeting costs	**8 986**	3 218
Investment Committee fees	**323**	125
Investment reporting fees	**3 416**	2 571
Legal fees	**816**	542
Net impairment losses (Note 17)	**75 167**	71 193
Nomination Committee fees (Note 18)	**571**	132
Other expenses	**25 499**	20 732
Principal Officer fees – Remuneration	**5 706**	5 126
Principal Officer fees – Unvested Long Term Employee Benefit	**1 438**	1 502
Printing, postage and stationery	**735**	550
Product Committee fees	**–**	66
Professional fees	**9 548**	10 877
Remuneration Committee fees	**109**	68
Scheme office costs	**6 314**	4 538
Staff costs (Note 19)	**20 127**	13 279
Sundry amounts written off	**293**	192
Stakeholder Relations Committee fees	**129**	142
Trustees' remuneration and consideration expenses (Note 20)	**5 430**	4 037
	236 206	198 387

* *Enhanced note disclosure has been presented as these committees are separately remunerated.*

NOTES TO THE ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 December 2016

R'000	2016	Restated 2015
16 Audit and Risk Committees fees*		
Audit Committee fees	**1 167**	835
B Stott – Independent Member (Chairperson)[1]	**603**	468
D Eriksson – Independent Member[2]	**–**	54
N Novick – Independent Member[3]	**–**	132
S Green – Independent Member	**158**	121
D King – Independent Member[4]	**64**	60
S Ludolph – Independent Member[5]	**163**	–
P Maphumulo – Independent Member[5]	**179**	–
Risk Committee fees	**588**	411
B Stott – Independent Member (Chairperson)[1]	**161**	126
D Eriksson – Independent Member[2]	**–**	45
N Novick – Independent Member[4]	**–**	97
S Green – Independent Member	**128**	98
D King – Independent Member[3]	**57**	45
S Ludolph – Independent Member[5]	**113**	–
P Maphumulo – Independent Member[5]	**129**	–
	1 755	1 246

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.

1 *Ex Officio member of the Board of Trustees, as Audit and Risk Committee chairperson.*
2 *Resigned 1 July 2015.*
3 *Resigned 31 December 2015.*
4 *Resigned 23 June 2016.*
5 *Appointed 20 January 2016.*

* *Enhanced note disclosure has been presented as these committees are separately remunerated.*

R'000	2016	2015
17 Net impairment losses		
Insurance and other receivables		
Contributions that are not collectable	**126**	2 527
Movement in provision	**126**	2 527
Members' and service providers' portions that are not recoverable	**76 422**	61 005
Movement in provision	**76 422**	61 005
Amounts due by brokers that are not recoverable	**81**	184
Movement in provision	**81**	184
Payables/receivables written off	**(1 462)**	7 505
Less:		
Previously written off receivables recovered	**–**	(28)
	75 167	71 193
18 Other Committee fees		
Nomination Committee fees		
P Goss – Independent Member (Chairperson)	**201**	44
T Wixley – Independent Member	**184**	44
R Shough – Independent Member	**186**	44
	571	132
19 Staff costs		
Salaries and bonuses	**16 466**	11 837
Pension costs – defined contribution plans	**1 160**	745
Medical and other benefits	**699**	499
Long Term Employee Benefit Service Cost	**1 563**	394
Increase/(decrease) in leave pay accrual	**239**	(196)
	20 127	13 279
Number of employees at 31 December	**11**	11

NOTES TO THE ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 December 2016

20 Trustees' remuneration and consideration expenses

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

31 December 2016	Services as Trustee R'000	Committee fees					Committee fees			Trustee Travel R'000	Total 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		
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**

31 December 2015	Services as Trustee R'000	Committee fees					Committee fees			Trustee Travel R'000	Total 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		
M Van Der Nest SC (Chairperson)	602	–	–	–	–	–	–	53	91	–	746
P Maserumule	314	–	–	155	–	–	–	–	71	–	540
N Graves SC	336	–	–	115	–	79	101	53	–	–	684
Z van der Spuy	324	–	–	–	122	79	–	–	–	86	611
G Waugh	306	113	98	–	–	102	79	–	–	–	698
D Naidoo	336	113	106	124	–	–	79	–	–	–	758
Total	**2 218**	**226**	**204**	**394**	**122**	**260**	**259**	**106**	**162**	**86**	**4 037**

NOTES TO THE ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 December 2016

R'000	2016	2015
21 Investment income		
Financial assets at fair value through profit or loss:	**1 200 503**	971 034
Dividend income	**50 993**	37 729
Interest income	**1 149 510**	933 305
Cash and cash equivalents interest income	**56 976**	47 964
Investment income per Statement of Comprehensive Income	**1 257 479**	1 018 998
The Scheme's total interest income is summarised below.		
Financial assets not at fair value through profit or loss:	**56 976**	48 155
Interest received from Administrator (Note 23)	**–**	191
Cash and cash equivalents interest income	**56 976**	47 964
Financial assets at fair value through profit or loss:		
Interest income	**1 149 510**	933 305
Total interest income	**1 206 486**	981 460
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 :	**17 334**	213 239
Fair value gains on financial assets at fair value through profit or loss:	**180 725**	315 387
– Equities	**126 213**	23 368
– Money market instruments	**598**	671
– Offshore bonds	**–**	290 923
– Inflation-linked bonds	**5 574**	425
– Yield-enhanced bonds	**48 340**	–
Fair value losses on financial assets at fair value through profit or loss :	**(163 391)**	(102 148)
– Equities	**(64 229)**	(58 738)
– Money market instruments	**(2 759)**	(539)
– Offshore bonds	**(88 161)**	(32 099)
– Inflation-linked bonds	**(7 845)**	(5 918)
– Yield-enhanced bonds	**(397)**	(4 854)
Net fair value gains/(losses) on derivative financial instruments:	**246 944**	(208 189)
Fair value gains on derivative financial instruments:	**255 039**	8 823
Fair value losses on derivative financial instruments:	**(8 095)**	(217 012)
Net fair value gains on cash and cash equivalents	**–**	1 454
	264 278	6 504

R'000	2016	2015

23 Sundry income

Interest received from Administrator (Note 21)	–	191
Prescribed amounts written back	**2 433**	3 678
(Reversal of stale cheques written back)/Stale cheques written back	**(74)**	3 649
	2 359	7 518

24 Interest paid

Financial assets not at fair value through profit or loss:		
Interest on Personal Medical Savings accounts (Note 8)	**287 923**	232 141
Interest paid to Administrator (Note 27)	**2 119**	118
	290 042	232 259

25 Reserves transferred from other medical schemes

Movement in and reserves transferred from amalgamated:		
Altron Medical Scheme	–	198
PG Bison Medical Scheme	–	(131)
	–	67

For further detail in respect of the above transfers, refer to note 26.

26 Amalgamations

The effective date of the amalgamations with Altron Medical Scheme and PG Bison Medical Scheme (refer note 25) was prior to 2015 and there have been no movements in these reserves during the year under review. The transactions recorded in 2015 are movements in reserves subsequent to the amalgamation date relating to contributions, claims and operating expenses adjustments.

27 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 2016

27 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	2016	2015
Statement of Comprehensive Income transactions		
Compensation		
Short term employee benefits	**(26 381)**	(21 704)
Unvested Long Term Employee Benefit	**(3 000)**	(1 502)
Contributions and claims		
Gross contributions received	**724**	795
Claims paid from the Scheme	**(281)**	(252)
Claims paid from the Personal Medical Savings Account	**(163)**	(202)
Interest paid on Personal Medical Savings Accounts	**1**	2
Statement of Financial Position transactions		
Long Term Employee Benefit Plan asset	**5 614**	1 071
Plan asset	**9 738**	5 136
Plan liability	**(4 124)**	(4 065)
Contribution debtors	**35**	17
Personal Medical Savings Account balances	**(10)**	(28)
Trustee remuneration payable	**–**	(58)

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 third parties, 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	2016	2015
27 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	**(4 150 194)**	(3 874 896)
Interest received on monthly balances (Note 23)	**–**	191
Interest paid on monthly balances (Note 24)	**(2 119)**	(118)
Statement of Financial Position transactions		
Balance due to Discovery Health (Pty) Ltd (Note 9)*	**(351 510)**	(327 895)
Discovery Health (Pty) Ltd – Managed care organisation		
Statement of Comprehensive Income transactions		
Accredited managed healthcare services (no risk transfer) (Note 12)	**(1 407 267)**	(1 305 790)
Statement of Financial Position transactions		
Balance due to Discovery Health (Pty) Ltd at year end (Note 9)*	**(118 414)**	(110 087)
Discovery Health (Pty) Ltd – Brokers		
Statement of Comprehensive Income transactions		
Broker fees paid	**(14 135)**	–
Discovery Health (Pty) Ltd – Wellness experiences		
Statement of Comprehensive Income transactions		
Claims paid from the Scheme	**(9 541)**	(12 306)
Statement of Financial Position transactions		
Claims due to provider	**(93)**	–
Discovery Third Party Recovery Services (Pty) Ltd		
Statement of Comprehensive Income transactions		
Third party collection fees	**(22 030)**	(17 695)
Statement of Financial Position transactions		
Balance due to the Scheme at year end (Note 3)	**20 540**	12 024
Southern RX Distributors (Pty) Ltd		
Statement of Comprehensive Income transactions		
Claims paid from the Scheme	**(145 325)**	(71 392)
Statement of Financial Position transactions		
Claims due to provider	**(1 837)**	(1 168)
Grove Nursing Services (Pty) Ltd		
Statement of Comprehensive Income transactions		
Claims paid from the Scheme	**(9 677)**	(3 686)
Statement of Financial Position transactions		
Claims (due to)/from provider	**(35)**	1

* *Total amount due to Discovery Health (Pty) Ltd for the current financial year is R470 million (2015: R438 million), disclosed in Note 9.*

NOTES TO THE ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 December 2016

27 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 is automatically renewed each year unless notification of termination is received or following the cancellation of the Administrator's accreditation or the issue of a lawful directive to this effect by the Council for Medical Schemes in terms of the Act. The Scheme and the Administrator shall be entitled to terminate the agreement by giving notice in writing of not less than 90 days and not more than 180 days. The outstanding balance bears interest at a prime-linked rate and is due within 30 days.

The administration fees are an all-inclusive fee, calculated on a Per Member Per Month basis. The total expense for administration cost increases in line with membership growth, however, the Per Member Per Month fee has increased at a rate lower than inflation for a number of years.

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 agreements

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.

Accredited managed healthcare services (no risk transfer)

Managed healthcare services is the cost of managing healthcare expenditure, such as 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.

The managed care agreement is in accordance with instructions given by the Board of Trustees. The agreement is automatically renewed each year unless notification of termination is received or following the cancellation of Discovery Health (Pty) Ltd's accreditation or the issue of a lawful directive to this effect by the Council for Medical Schemes in terms of the Act. The Scheme and Discovery Health (Pty) Ltd shall be entitled to terminate the agreement by giving notice in writing of not less than 90 days and not more than 180 days. The outstanding balance bears interest at a prime-linked rate and is due within 30 days.

27 Related party transactions *continued*

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

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
- Pharmacy Benefit Management Services

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 2016 to 31 December 2016 to Discovery Third Party Recovery Services (Pty) Ltd for the amount of R14 million (2015: 12 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 direct to the consumer. The amounts were paid through the normal broker fee channels. This is a new agreement effective from 2016.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 December 2016

28 Surplus/(deficit) from operations per benefit plan

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
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**
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)
Claims incurred	(1 159 318)	(9 728 653)	(48 001)	(1 346 843)	(6 817 367)	(3 396 783)	(836 103)	(1 818 786)
Third party claim recoveries	1 340	18 811	102	6 396	33 086	11 807	2 254	13 164
Net (loss)/income 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)
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)**
Gross healthcare result	**(297 167)**	**(116 230)**	**1 916**	**460 338**	**2 036 784**	**710 028**	**155 442**	**966 984**
Broker service fees	(11 360)	(165 057)	(828)	(42 828)	(259 350)	(102 255)	(20 642)	(86 194)
Expenses for administration	(39 938)	(562 224)	(2 975)	(185 567)	(957 550)	(348 811)	(67 157)	(366 937)
Other operating expenses	(2 063)	(28 989)	(153)	(9 580)	(49 421)	(18 009)	(3 469)	(18 938)
Net healthcare result	**(350 528)**	**(872 500)**	**(2 040)**	**222 363**	**770 463**	**240 953**	**64 174**	**494 915**
Investment income	10 968	154 294	818	50 982	263 050	95 799	18 438	100 903
Net 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
Sundry income	20	308	(1)	95	498	184	33	184
Other income	**13 358**	**187 987**	**991**	**61 875**	**319 088**	**116 543**	**22 457**	**121 784**
Expenses for asset management services rendered	(272)	(3 820)	(23)	(1 259)	(6 505)	(2 369)	(453)	(2 490)
Interest paid	(3 806)	(53 555)	–	(83)	(91 299)	(33 251)	(6 402)	(35 016)
Other expenditure	**(4 078)**	**(57 375)**	**(23)**	**(1 342)**	**(97 804)**	**(35 620)**	**(6 855)**	**(37 506)**
Net (deficit)/surplus for the year	**(341 248)**	**(741 888)**	**(1 072)**	**282 896**	**991 747**	**321 876**	**79 776**	**579 193**

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

2016	Essential Core R'000	Essential Priority R'000	Coastal Saver R'000	Coastal Core R'000	KeyCare Plus R'000	KeyCare Core R'000	KeyCare Access R'000	Smart R'000	Total R'000
Risk contribution income	**1 013 633**	**297 133**	**5 385 228**	**2 413 696**	**4 207 970**	**220 866**	**57 055**	**227 033**	**43 626 398**
Net claims incurred	(660 685)	(205 856)	(4 491 692)	(1 962 720)	(3 964 639)	(127 085)	(22 924)	(112 715)	36 613 210)
Claims incurred	(665 369)	(206 777)	(4 514 656)	(1 973 413)	(3 993 633)	(128 916)	(23 551)	(114 163)	(36 772 332)
Third party claim recoveries	4 684	921	22 964	10 693	28 994	1 831	627	1 448	159 122
Net income/(loss) 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)	(39 701)	(8 360)	(204 472)	(94 660)	(250 933)	(15 471)	(5 423)	(10 005)	(1 407 267)
Relevant healthcare expenditure	**(700 386)**	**(214 216)**	**(4 696 164)**	**(2 057 380)**	**(4 184 382)**	**(142 556)**	**(31 270)**	**(123 855)**	**(38 035 898)**
Gross healthcare result	**313 247**	**82 917**	**689 064**	**356 316**	**23 588**	**78 310**	**25 785**	**103 178**	**5 590 500**
Broker service fees	(26 669)	(7 510)	(174 400)	(65 440)	(124 596)	(6 517)	(1 794)	(6 208)	(1 101 648)
Expenses for administration	(129 091)	(27 182)	(664 984)	(307 902)	(436 502)	(14 540)	(6 115)	(32 719)	(4 150 194)
Other operating expenses	(6 662)	(1 404)	(34 320)	(15 889)	(42 119)	(2 598)	(908)	(1 684)	(236 206)
Net healthcare result	**150 825**	**46 821**	**(184 640)**	**(32 915)**	**(579 629)**	**54 655**	**16 968**	**62 567**	**102 452**
Investment income	35 499	7 465	182 695	84 590	224 314	13 832	4 846	8 986	1 257 479
Net gains on financial assets at fair value through profit or loss	7 236	1 604	38 516	17 766	46 306	2 820	1 013	1 507	264 278
Sundry income	65	13	343	158	411	25	10	13	2 359
Other income	**42 800**	**9 082**	**221 554**	**102 514**	**271 031**	**16 677**	**5 869**	**10 506**	**1 524 116**
Expenses for asset management services rendered	(874)	(184)	(4 516)	(2 090)	(5 540)	(342)	(119)	(220)	(31 076)
Interest paid	(57)	(2 591)	(63 409)	(143)	(380)	(23)	(11)	(16)	(290 042)
Other expenditure	**(931)**	**(2 775)**	**(67 925)**	**(2 233)**	**(5 920)**	**(365)**	**(130)**	**(236)**	**(321 118)**
Net surplus/(deficit) for the year	**192 694**	**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 2016

28 Surplus/(deficit) from operations per benefit plan continued

2015	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
Risk contribution income	**830 871**	**9 626 771**	**43 280**	**1 763 910**	**8 085 165**	**4 009 464**	**1 043 009**	**2 465 336**
Net claims incurred*	(1 090 864)	(9 344 752)	(39 684)	(1 224 311)	(5 841 078)	(3 172 290)	(836 186)	(1 516 002)
Claims incurred*	(1 091 535)	(9 354 646)	(39 725)	(1 227 405)	(5 855 182)	(3 178 190)	(837 485)	(1 521 065)
Third party claim recoveries	671	9 894	41	3 094	14 104	5 900	1 299	5 063
Net (loss)/income on risk transfer arrangements*	(4 040)	(54 466)	(450)	–	–	–	(5 969)	–
Risk transfer arrangement fees	(9 876)	(126 167)	(916)	–	–	–	(13 327)	–
Recoveries from risk transfer arrangements*	5 836	71 701	466	–	–	–	7 358	–
Accredited managed healthcare services (no risk transfer)	(11 999)	(174 863)	(785)	(55 739)	(267 757)	(105 682)	(21 745)	(97 571)
Relevant healthcare expenditure	**(1 106 903)**	**(9 574 081)**	**(40 919)**	**(1 280 050)**	**(6 108 835)**	**(3 277 972)**	**(863 900)**	**(1 613 573)**
Gross healthcare result	**(276 032)**	**52 690**	**2 361**	**483 860**	**1 976 330**	**731 492**	**179 109**	**851 763**
Broker service fees	(10 775)	(159 699)	(682)	(40 608)	(224 310)	(95 695)	(19 802)	(70 895)
Expenses for administration	(39 226)	(571 646)	(2 567)	(182 213)	(875 309)	(345 486)	(71 177)	(318 954)
Other operating expenses	(1 819)	(26 511)	(119)	(8 465)	(40 677)	(16 035)	(3 297)	(14 852)
Net healthcare result	**(327 852)**	**(705 166)**	**(1 007)**	**252 574**	**836 034**	**274 276**	**84 833**	**447 062**
Investment income	10 405	151 633	473	33 587	232 309	91 660	18 856	84 714
Net gains on financial assets at fair value through profit or loss	106	1 529	6	294	1 481	800	188	154
Sundry income	69	1 002	3	321	1 542	606	124	564
Other income	**10 580**	**154 164**	**482**	**34 202**	**235 332**	**93 066**	**19 168**	**85 432**
Expenses for asset management services rendered	(288)	(4 189)	(19)	(1 348)	(6 461)	(2 539)	(521)	(2 380)
Interest paid	(3 177)	(46 308)	–	(5)	(70 993)	(27 999)	(5 758)	(25 912)
Other expenditure	(3 465)	(50 497)	(19)	(1 353)	(77 454)	(30 538)	(6 279)	(28 292)
Net (deficit)/surplus for the year	**(320 737)**	**(601 499)**	**(544)**	**285 423**	**993 912**	**336 804**	**97 722**	**504 202**

* *See note 13 to the Annual Financial Statements for explanatory note on change of disclosure.*

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

2015	Essential Core R'000	Essential Priority R'000	Coastal Saver R'000	Coastal Core R'000	KeyCare Plus R'000	KeyCare Core R'000	KeyCare Access R'000	Total R'000
Risk contribution income	**870 164**	**302 973**	**4 784 988**	**2 179 506**	**3 803 900**	**205 967**	**51 437**	**40 066 741**
Net claims incurred*	(578 249)	(186 734)	(3 915 586)	(1 713 148)	(3 585 417)	(91 452)	(25 065)	(33 160 818)
Claims incurred*	(580 074)	(187 273)	(3 925 543)	(1 717 962)	(3 597 787)	(92 312)	(25 370)	(33 231 554)
Third party claim recoveries	1 825	539	9 957	4 814	12 370	860	305	70 736
Net income/(loss) on risk transfer arrangements*	–	–	–	–	30 742	–	(2 836)	(37 019)
Risk transfer arrangement fees	–	–	–	–	(190 971)	–	(2 836)	(344 093)
Recoveries from risk transfer arrangements*	–	–	–	–	221 713	–	–	307 074
Accredited managed healthcare services (no risk transfer)	(34 605)	(8 835)	(187 572)	(88 982)	(229 779)	(14 735)	(5 141)	(1 305 790)
Relevant healthcare expenditure	**(612 854)**	**(195 569)**	**(4 103 158)**	**(1 802 130)**	**(3 784 454)**	**(106 187)**	**(33 042)**	**(34 503 627)**
Gross healthcare result	**257 310**	**107 404**	**681 830**	**377 376**	**19 446**	**99 780**	**18 395**	**5 563 114**
Broker service fees	(22 914)	(7 483)	(150 846)	(60 125)	(111 395)	(6 056)	(1 589)	(982 874)
Expenses for administration	(113 121)	(28 882)	(613 181)	(290 883)	(402 605)	(13 849)	(5 797)	(3 874 896)
Other operating expenses	(5 271)	(1 340)	(28 489)	(13 523)	(34 964)	(2 243)	(782)	(198 387)
Net healthcare result	**116 004**	**69 699**	**(110 686)**	**12 845**	**(529 518)**	**77 632**	**10 227**	**506 957**
Investment income	20 861	7 662	162 740	53 623	138 494	8 882	3 099	1 018 998
Net losses on financial assets at fair value through profit or loss	(23)	68	1 045	381	456	13	6	6 504
Sundry income	201	51	1 079	513	1 328	85	30	7 518
Other income	**21 039**	**7 781**	**164 864**	**54 517**	**140 278**	**8 980**	**3 135**	**1 033 020**
Expenses for asset management services rendered	(850)	(212)	(4 529)	(2 156)	(5 600)	(360)	(126)	(31 578)
Interest paid	(3)	(2 341)	(49 733)	(8)	(21)	(1)	–	(232 259)
Other expenditure	**(853)**	**(2 553)**	**(54 262)**	**(2 164)**	**(5 621)**	**(361)**	**(126)**	**(263 837)**
Net surplus/(deficit) for the year	**136 190**	**74 927**	**(84)**	**65 198**	**(394 861)**	**86 251**	**13 236**	**1 276 140**

* *See note 13 to the Annual Financial Statements for explanatory note on change of disclosure.*

NOTES TO THE ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 December 2016

R'000	2016	2015
29 Cash flows from operations before working capital changes		
Net surplus for the year	**1 305 450**	1 276 140
Adjustments for:		
Impairment losses (Note 15)	**75 167**	71 193
Interest received (Note 21)	**(1 206 486)**	(981 460)
Dividend income (Note 21)	**(50 993)**	(37 729)
Interest paid (Note 24)	**290 042**	232 259
Unvested Long Term Employee Benefit	**3 000**	1 894
Net gains on financial assets at fair value through profit or loss (Note 22)	**(264 278)**	(6 504)
	151 902	555 793
Reconciliation of movements in the cash flow statement		
29.1 Increase in trade and other receivables	**(500 589)**	(99 229)
Opening balance	**1 632 586**	1 604 550
Closing balance	**(2 058 008)**	(1 632 586)
Impairment losses	**(75 167)**	(71 193)
29.2 Increase in trade and other payables	**123 640**	151 366
Opening balance	**(1 182 605)**	(1 031 239)
Closing balance (Note 9)	**1 306 245**	1 182 605
29.3 Purchases of financial instruments	**(1 922 170)**	(6 176 902)
Financial assets at Fair value (Note 2)	**(1 922 170)**	(6 176 902)
29.4 Proceeds from sale of financial instruments	**1 258 510**	4 339 081
Financial assets at Fair value (Note 2)	**1 127 159**	4 465 329
Derivative financial instruments (Note 7)	**131 351**	(126 248)

30 Events after the reporting period

No significant events occurred between the reporting date and the date the financial statements were authorised for issue.

31 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.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 December 2016

31 Insurance risk management report *continued*

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

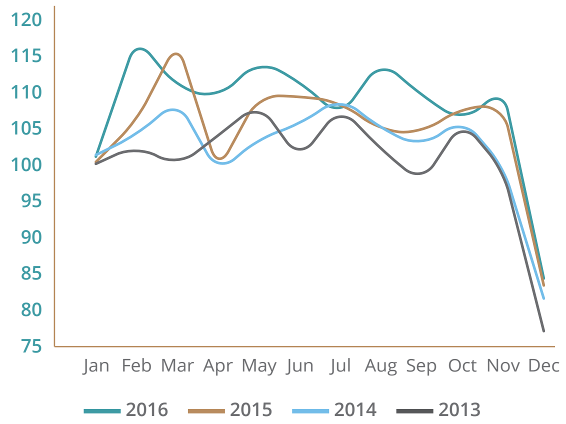
Hospital benefit risk

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.

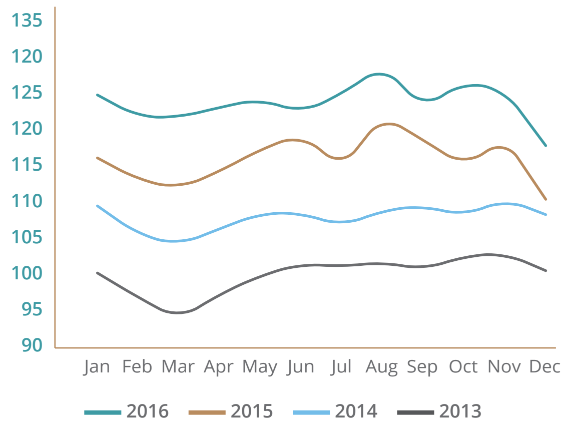
An increase in the admission rate is often linked to increases in the number of beneficiaries at older ages or with chronic conditions. The increase in cost per event is driven by annual tariff and other cost increases. An increased cost per event can also be caused by an increased case-mix, severity 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 2013.

Hospital Admission Rate
(Indexed to Jan 2013 = 100)



Total Cost Per Event
(Indexed to Jan 2013 = 100)

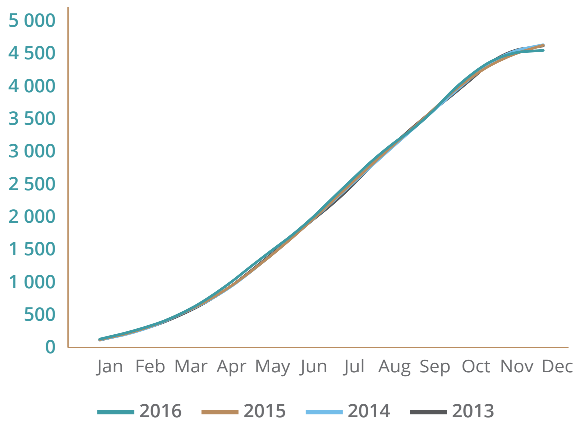


Day-to-day benefits risk

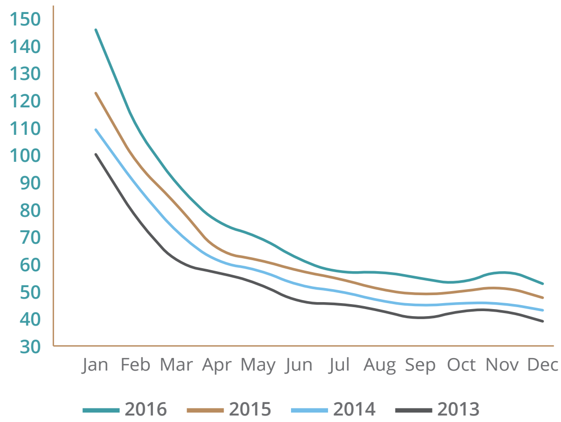
For the Above Threshold Benefit component, the frequency and severity of claims are driven by the number and disease burden of claimants. The mix of members between the different benefit options will also have an impact on the claims.

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

Claimants Per 1000 From Above Threshold Benefits
(Indexed to Jan 2013 = 100)



Cost Per ATB Claimant
(Indexed to Jan 2013 = 100)



31 Insurance risk management report *continued*

Chronic benefits risk

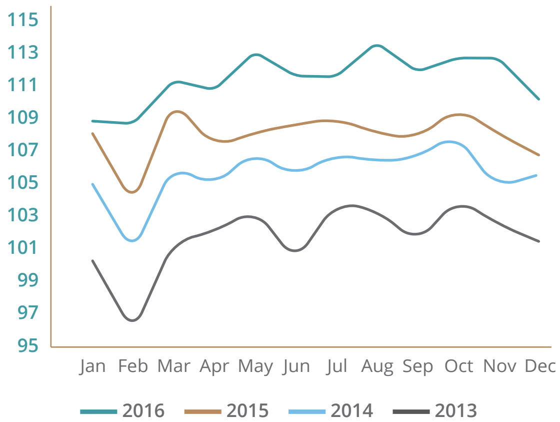
The main factors impacting the frequency and severity of chronic claims are the number of claimants and the cost per claimant respectively.

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.

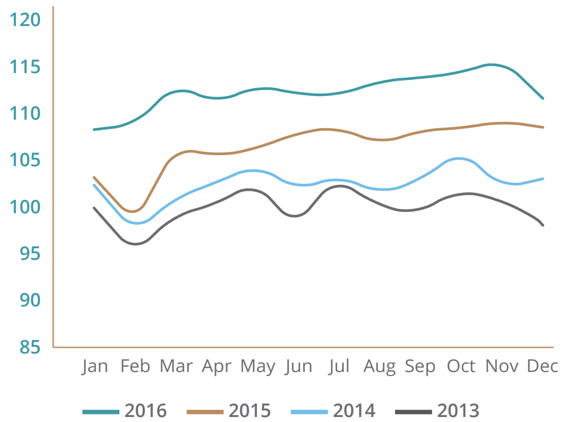
Higher increases in chronic claimants are linked to increases in the number of beneficiaries at older ages. In addition, changes relating to the eligibility for chronic benefits will also impact costs. An increase in the number of items per claimant will drive up the costs of chronic claims per claimant. 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.

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 2013.

Chronic Claimants Per 1000 Beneficiaries
(Indexed to Jan 2013 = 100)



Chronic Cost Per Claimant
(Indexed to Jan 2013 = 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.
- The work of the Clinical Policy Unit, which evaluates the effectiveness of new technologies and recommends whether the Scheme should cover these.
- The development of protocols around various high cost conditions, such as lower back surgery.
- The establishment of a unit to focus on reducing surgical consumable 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.
- The Scheme manages and mitigates 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.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 December 2016

31 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 (2015: four) risk transfer agreements in which suppliers are paid to provide certain minimum benefits to Scheme members, as and when it is 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 also 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 covers Smart plan (newly introduced in 2016) 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 against 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 2016 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.

31 Insurance risk management report *continued*

Concentration of insurance risk *continued*

Based on the processing patterns and claims development up to the end of December 2016 in respect of treatment dates during 2016, the provision for outstanding claims as at 31 December 2016 is R1 121 million (2015: R985 million).

R'000	**2016**	2015
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	**26 807 352**	24 063 065
Chronic claims incurred	**2 271 897**	2 052 610
Out-of-hospital risk claims incurred	**7 745 832**	7 033 552

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 2016 R'000**	Impact on outstanding claims provision 2015 R'000
In-hospital claims incurred	1% reduction in claims processing	**318 755**	233 675
Chronic claims incurred	1% reduction in claims processing	**7 682**	8 687
Out-of-hospital risk claims incurred	1% reduction in claims processing	**78 728**	67 418

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 94% (2015: 98%) of this provision is settled within three months after the claim was incurred. 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 who 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 assumptions regarding utilisation trends, the impact of new technology and the expected demographic profile of the Scheme membership.

32 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.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 December 2016

32 Financial risk management report *continued*

Overview *continued*

The Scheme manages the financial risks as follows:

- The Investment Committee, a committee of the Board of Trustees, determines, recommends, implements and maintains investment policies and procedures. The Investment Committee advises the Board of Trustees on the strategic and operating matters in respect of the investment of Scheme funds and meets at least quarterly.
- 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.
- Asset management agreements and mandates are concluded and reviewed by the Scheme's in-house legal counsel.
- An independent valuation is performed by a third party.

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 (previously Momentum Asset Management) 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 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**			✓
31 December 2015				
Investments	**11 399 332**			
Offshore bonds	1 335 137	✓		✓
Equities	1 415 647		✓	
Yield enhanced bonds	3 058 012			✓
Inflation linked bonds	464 574			✓
Money market instruments	5 125 962			✓

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.

32 Financial risk management report *continued*

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 has invested 10 % (2015: 12%) of its investable assets in offshore bond portfolios (reference currency is the US dollar). Derivative financial instruments are utilised by bond managers within these portfolios to manage various currency exposures. At 31 December 2016 this equates to R1 246 million (2015: R1 335 million) (Note 2).

▪ 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 rate with respect to its offshore bond portfolios. The current contract expires during 2017 and was entered into with the cap at R14.77 (9.5% above the floor level) to the US Dollar. The spot level (the floor) was entered into at R13.49 to the US Dollar.

The collar is not designated as a hedge instrument and hedge accounting is thus not applicable to the collar. The collar is categorised as fair value through profit or loss.

At the time of expiry the following transactions could occur depending on the 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 surplus (Note 7).

▪ Currency risk sensitivity analysis

A 5% depreciation in the Rand would result in a gain on offshore bonds of R62 million (2015: R67 million) and a 15% depreciation in the Rand would result in a gain of R187 million (2015: R200 million). A 5% appreciation in the Rand would result in a loss of R62 million (2015: R67 million) and a 15% appreciation in the Rand would result in a loss of R187 million (2015: R200 million). This impact would be recognised in the Net Surplus. The sensitivity is based on the assumption that the Rand has strengthened or weakened against the US Dollar by 5% or 15%, with all other variables held constant. The analysis is performed without taking into account the effect of the currency hedges. If you consider the impact of hedging through the use of zero cost currency collars, all Rand appreciation below the current floor level of the zero cost currency collar is covered on a one-for-one basis i.e. for every Rand lost on the actual offshore bond portfolio you gain a Rand on the zero cost currency collar. Given current cap level pricing on zero cost currency collars, neither a 5% nor 15% depreciation of the Rand would impact overall currency gains of the actual offshore bond portfolio.

Price risk

The Scheme is exposed to equity securities price risk due to equity investments held by the Scheme that are classified as fair value through profit and loss. The Scheme is indirectly exposed to commodity risk through its investments in listed equities. The value of the Scheme's equity investments amounted to R2 billion (2015: R1.4 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 are performed by asset managers in accordance with the mandate set by the Scheme.

The Scheme purchased derivative financial instruments to protect the solvency of the Scheme as a result of fluctuations in the equity market.

▪ 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 at risk for the first 5% drop in equity prices). 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 16% and 18% above the pre-determined level. These contracts expire during 2017.

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 2016

32 Financial risk management report *continued*

Price risk *continued*

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, the counterparty would be required to pay the difference between the floor and the index level to the Scheme.

- **Equity price risk sensitivity analysis**

A 5% increase in the price of equities within the equity portfolios would result in a gain of R102 million (2015: R73 million) and a 15% increase would result in a gain of R307 million (2015: R218 million). A 5% decrease would result in a loss of R102 million (2015: R73 million) and a decrease of 15% would result in a loss of R307 million (2014: R218 million). This impact would be recognised in the Net Surplus. The sensitivity is based on the assumption that equity prices had increased or decreased by 5% or 15%, with all other variables held constant. The analysis is performed without taking into account the affect of the equity hedges.

If we considered the effect of the current open hedges, gains on the equity portfolios for 5% and 15% increases in equity prices would not effect returns as the caps on these hedges are set at higher levels i.e. 16% to 18%. For a drop of 5% and 15% in equity prices, the above stated losses would reduce to approximately R18 million and R27 million respectively.

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 2016	**0 – 3 Months R'000**	**3 – 12 Months R'000**	**> 12 Months R'000**	**Total R'000**
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**

As at 31 December 2015	0 – 3 Months R'000	3 – 12 Months R'000	> 12 Months R'000	Total R'000
Cash and cash equivalents	2 198 127	–	–	2 198 127
Money market instruments carried at fair value through profit or loss	–	5 125 962	–	5 125 962
Yield enhanced bonds carried at fair value through profit or loss	–	3 058 012	–	3 058 012
Inflation linked bonds carried at fair value through profit or loss	–	464 574	–	464 574
Offshore bonds carried at fair value through profit or loss	–	1 335 137	–	1 335 137

The following table summarises the weighted average interest rate for monetary financial instruments:

%	**2016**	2015
Money market instruments carried at fair value through profit or loss	**7.40**	6.09
Cash and cash equivalents	**7.23**	5.85

The weighted average interest rate on short-term bank deposits (namely call account deposits) was 6.70% (2015 – 5.95%). These deposits have an average maturity of 25 days (2015 – 25 days).

32 Financial risk management report *continued*

Interest rate risk *continued*

- **Interest rate risk sensitivity analysis**

A 1% increase in local interest rates would result in a gain of R332k (2015: loss of R9.5 million), and a 2% increase would result in a loss of R240k (2015: loss of R14.1 million). A 1% decrease in local interest rates would result in a gain of R1.1 million (2015: gain of R11.1 million) and a decrease of 2% would result in a loss of R2.7 million (2015: gain of R16.9 million). This impact would be recognised in the Net Surplus. The sensitivity is based on the assumption that local interest rates had increased or decreased by 1% or 2%, with all other variables held constant.

A 1% increase in foreign interest rates would result in a loss of R64 million (2015: R66 million) and a 2% increase would result in a loss of R127 million (2015: R 133 million). A 1% decrease in foreign interest rates would result in a gain of R64 million (2015: R66 million) and a decrease of 2% would result in a gain of R127 million (2015: R133 million). This impact would be recognised in the Net Surplus. The sensitivity is based on the assumption that foreign interest rates had increased or decreased by 1% or 2%, with all other variables held constant.

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.

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 2016 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. Continuous monitoring takes place to ensure that appropriate liquid assets are held to meet the Scheme's liabilities, are dependent upon the performance of the investment portfolio and that a suitable match of assets exists for all liabilities.

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

The Scheme's investment objectives are to maximise the return on its investments on a long-term basis at minimal risk, subject to any constraints imposed by legislation or the Board of Trustees. The Scheme diversifies its investment portfolio by investing in short-term deposits, bond, money market and equity portfolios managed by reputable asset managers.

The Investment Committee monitors the performance of the Scheme's asset managers to ensure that the Scheme receives the benefit of top performing asset managers.

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.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 December 2016

32 Financial risk management report *continued*

Breakdown of investments *continued*

R'000	Segregated Funds	Collective Investment Schemes	Policy of Insurance	Total
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 December 2015				
Investments	10 064 195	716 812	618 325	11 399 332
Offshore bonds	–	716 812	618 325	1 335 137
Equities	1 415 647	–	–	1 415 647
Yield enhanced bonds	3 058 012	–	–	3 058 012
Inflation linked bonds	464 574	–	–	464 574
Money market instruments	5 125 962	–	–	5 125 962
Cash and cash equivalents:	842 123	1 356 004	–	2 198 127
	10 906 318	2 072 816	618 325	13 597 459

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 products aimed at achieving out performance of the targeted (benchmark) return.

For the first portfolio, the weighted modified duration of the portfolio shall not exceed 180 days. The weighted term to maturity of the portfolio shall not exceed 2 years. The term of each individual instrument is also limited.

The second portfolio has a number of liquidity restrictions ranging from a minimum of 20% of the assets under administration being available within 24 hours to an average portfolio duration of 180 days.

The performance of these portfolios is measured against the Short Term Fixed Income (STeFI) Composite Index.

The local money market portfolios comprise approximately 40% (2015: 45%) 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.

The one portfolio 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. The benchmark for this portfolio is the 3-month Johannesburg Interbank Agreed Rate (JIBAR).

The second portfolio is a specialist yield-enhanced bond portfolio investing in a broad spectrum of fixed interest and yield-enhanced debt instruments. The benchmark for this portfolio is 20% BEASSA All Bond Index (ALBI) and 80% STeFI. Mid-2016, the Scheme transitioned this portfolio to AA SteFI+ mandate which incorporates money market, fixed interest and yield enhanced debt and thereby reducing overall duration (interest rate risk) on this portfolio. The new portfolio's benchmark is the STeFI.

The mandates set specific exposure limits depending on the credit rating of the individual counterparty and sets exposure limits to unrated investments. These portfolios comprise approximately 28% (2015: 27%) of the Scheme's financial assets at fair value through profit or loss.

32 Financial risk management report *continued*

Breakdown of investments *continued*

Offshore portfolios

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

The primary objective of the first portfolio was the generation of a high level of income by means of investments in high-yielding fixed or floating rate securities of varying maturities denominated in a spread of currencies. The portfolio was structured as a collective investment undertaking with the Barclays Capital Global Aggregate as its benchmark index. During 2016, this product offering was terminated by the asset manager and the Scheme transferred the proceeds to a different fund offering that aims both to provide income and to protect and maximize 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 the fund's assets are denominated in major currencies and exposure to minor currencies is managed on a cautious basis. The fund is benchmarked against ICE LIBOR Spot/Next Overnight USD.

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% (2015: 12%) of the Scheme's financial assets at fair value through profit or loss.

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 and achieving outperformance of the benchmarks on 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 returns of the portfolio are measured against the JSE Bond Exchange and Actuarial Society of South Africa (JSE BEASSA IGOV Index).

These portfolios comprise approximately 5% (2015: 4%) of the Scheme's Financial assets at fair value through profit or loss.

Equity portfolios:

The Scheme has three equity portfolios each managed by an independent asset manager.

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. The portfolios are managed on a moderate risk basis.

The portfolios may only be invested in South African equities and are subject to a maximum cash allocation of 5%. The portfolios are prohibited from investing in Discovery Limited or its subsidiaries and tobacco companies (as per the Scheme's responsible investment policy) and must comply with the Act.

The performance of the portfolios is measured against the benchmark, which is the FTSE/JSE Shareholder weighted index (SWIX) less tobacco (as per the Scheme's responsible investment policy).

These portfolios comprise approximately 17% (2015: 12%) 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 2016

32 Financial risk management report *continued*

Breakdown of investments *continued*

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

	Financial assets and liabilities at fair value through profit and loss						
	Designated upon initial recognition R'000	Classified as held for trading R'000	Loans and receivables R'000	Insurance receivables and (payables) R'000	Financial liabilities at amortised cost R'000	Total carrying amount R'000	Fair value amount R'000
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**	**2 516 317**	**1 093 553**	**(521 690)**	**15 350 241**	**15 350 241**

32 Financial risk management report *continued*

	Financial assets and liabilities at fair value through profit and loss						
	Designated upon initial recognition R'000	Classified as held for trading R'000	Loans and receivables R'000	Insurance receivables and (payables) R'000	Financial liabilities at amortised cost R'000	Total carrying amount R'000	Fair value amount R'000
31 December 2015							
Investments							
– Offshore bond portfolio	1 335 137	–	–	–	–	1 335 137	1 335 137
– Listed equities	1 415 647	–	–	–	–	1 415 647	1 415 647
– Yield-enhanced bond portfolio	3 058 012	–	–	–	–	3 058 012	3 058 012
– Inflation-linked bond portfolio	464 574	–	–	–	–	464 574	464 574
– Money market portfolios	5 125 962	–	–	–	–	5 125 962	5 125 962
Cash and cash equivalents:							
Medical Scheme assets	–	–	2 198 127	–	–	2 198 127	2 198 127
Personal Medical Savings Account trust assets	–		3 667 456	–	–	3 667 456	3 667 456
Trade and other receivables	–	–	107 266	1 525 320	–	1 632 586	1 632 586
Personal Medical Savings Accounts	–	–	(3 736 659)		–	(3 736 659)	(3 736 659)
Trade and other payables	–	–	–	(714 900)	(467 705)	(1 182 605)	(1 182 605)
Derivatives held for trading							
– Zero-cost collars	–	(65 210)	–	–	–	(65 210)	(65 210)
– Other	–	–	–	–	–	–	–
	11 399 332	(65 210)	2 236 190	810 420	(467 705)	13 913 027	13 913 027

NOTES TO THE ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 December 2016

32 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 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 0 – 30 days	**1 677**	**6 474**	**8 720**	**16 871**	**8 712**	**–**	**(78)**	**–**	**–**	**25 505**
Past due 31 – 60 days	**1 751**	**8 539**	**(2 511)**	**7 779**	**6 972**	**–**	**(13 524)**	**–**	**–**	**1 227**
Past due 61 – 90 days	**2 757**	**8 250**	**1 295**	**12 302**	**(7 135)**	**–**	**15 370**	**–**	**–**	**20 537**
Past due 91 – 120 days	**2 918**	**8 809**	**11 616**	**23 343**	**15 709**	**–**	**95**	**–**	**–**	**39 147**
Past due 121 – 150 days	**2 305**	**10 447**	**(4 980)**	**7 772**	**–**	**–**	**55**	**–**	**–**	**7 827**
151 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**
31 December 2015										
Not past due	1 239	4 217	8 796	14 252	1 379 759	7 520	11 394	60 869	107 266	1 581 060
Past due 0 – 30 days	2 330	6 583	2 119	11 032	9 595	–	317	–	–	20 944
Past due 31 – 60 days	4 023	7 653	(5 731)	5 945	4 514	–	(242)	–	–	10 217
Past due 61 – 90 days	1 904	6 598	6 834	15 336	6 261	–	(22)	–	–	21 575
Past due 91 – 120 days	2 321	9 872	(1 112)	11 081	(3 992)	–	(441)	–	–	6 648
Past due 121 – 150 days	3 015	9 977	(5 904)	7 088	–	–	11	–	–	7 099
151 days to more than one year	24 476	183 021	6 614	214 111	–	–	(10 122)	–	–	203 989
Gross receivables	**39 308**	**227 921**	**11 616**	**278 845**	**1 396 137**	**7 520**	**895**	**60 869**	**107 266**	**1 851 532**
Provision for impairments	(22 196)	(178 471)	(7 862)	(208 529)	(9 633)	–	(784)	–	–	(218 946)
Trade and other receivables neither past due nor impaired	17 112	49 450	3 754	70 316	1 386 504	7 520	111	60 869	107 266	1 632 586

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 2016

32 Financial risk management report *continued*

Exposure to 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 2015	7 106	177 458	–	600	185 164
Increase in provision for impairment	2 527	61 005	–	184	63 716
Amounts utilised during the year	–	(29 934)	–	–	(29 934)
Balance as at 31 December 2015	9 633	208 529	–	784	218 946
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**

32 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 pages 138 to 139 can be assessed by reference to historical information about counterparty default.

Contribution debtors

The Scheme collected over 97% (2015: 98%) of outstanding debt in January 2017. 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% (2015: 56%) 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 80% (2015: 78%) 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	2016	2015
– Offshore bonds	**1 245 709**	1 335 137
– Yield enhanced bonds	**3 413 740**	3 058 012
– Inflation linked bonds	**610 476**	464 574
– Money market instruments	**4 891 918**	5 125 962
– Cash and cash equivalents	**2 397 788**	2 198 127
– Derivative financial instruments	**50 384**	–
	12 610 015	12 181 812

NOTES TO THE ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 December 2016

32 Financial risk management report *continued*

Exposure to credit risk

The Scheme manages credit risk 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 144 to 145.

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 rating scales

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.

Short-term rating scales

F1: Highest short-term credit quality

F1 indicates the strongest intrinsic capacity for timely payment of financial commitments; they may have an added “”+”” to denote any exceptionally strong credit feature.

32 Financial risk management report *continued*

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 2016 1.8% (2015: 2.8%) of the Scheme's Financial assets at fair value through profit or loss 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 2016 1% (2015: 0.6%) of the Scheme's Financial assets at fair value through profit or loss invested in instruments with this credit rating.

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 2016 0.5% (2015: 0.5%) of the Scheme's Financial assets at fair value through profit or loss 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 2016 1.6% (2015: 2.6%) of the Scheme's financial assets at fair value through profit or loss invested in instruments with this credit rating.

CC: Very high levels of credit risk

Default of some kind appears probable.

At 31 December 2016 0% (2015: 0.1%) of the Scheme's financial assets at fair value through profit or loss invested in instruments with this credit rating.

NOTES TO THE ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 December 2016

32 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 4% (2015: 4%) of the instruments are invested in non-investment grade instruments after consideration of internally assigned credit ratings.

		Short-term rating		Long-term rating		Long-term rating							
R'000	Total	F1+	F1	Govt	AAA	AA+ to AA–	A+ to A–	BBB– to BBB+	BB– to BB+	B– to B+	CCC+ to CCC–	CC+	Not rated
2016													
At fair value through profit or loss:	**10 161 843**	**833 313**	**5 779**	**565 317**	**1 380 392**	**2 360 938**	**3 718 408**	**223 471**	**128 709**	**57 319**	**189 501**	**–**	**698 696**
– Offshore bond portfolio	**1 245 709**	**843**	**5 282**	**–**	**242 723**	**445 651**	**221 380**	**113 316**	**128 709**	**57 319**	**4 460**	**–**	**26 026**
– Yield enhanced bond portfolio	**3 413 740**	**54 870**	**497**	**60 997**	**565 333**	**980 241**	**1 066 578**	**110 155**	**–**	**–**	**29 068**	**–**	**546 001**
– Inflation linked bond portfolio	**610 476**	**(21 377)**	**–**	**445 255**	**16 688**	**31 581**	**138 329**	**–**	**–**	**–**	**–**	**–**	**–**
– Money market portfolios	**4 891 918**	**798 977**	**–**	**59 065**	**555 648**	**903 465**	**2 292 121**	**–**	**–**	**–**	**155 973**	**–**	**126 669**
Cash and cash equivalents	**2 397 788**	**1 640 731**	**–**	**6 608**	**201**	**312 962**	**370 752**	**–**	**–**	**–**	**15 409**	**–**	**51 125**
Total*	**12 559 631**	**2 474 044**	**5 779**	**571 925**	**1 380 593**	**2 673 900**	**4 089 160**	**223 471**	**128 709**	**57 319**	**204 910**	**–**	**749 821**
2015													
At fair value through profit or loss:	9 983 685	856 196	10 142	592 441	1 400 390	1 959 844	3 879 452	346 423	116 706	55 001	290 665	7 525	468 900
– Offshore bond portfolio	1 335 137	11 766	10 110	62 487	208 689	217 671	307 201	218 849	116 706	55 001	9 645	7 525	109 487
– Yield enhanced bond portfolio	3 058 012	16 323	32	205 127	549 463	1 058 456	740 692	127 165	–	–	35 339	–	325 415
– Inflation linked bond portfolio	464 574	(31 702)	–	318 724	1 015	15 271	161 266	–	–	–	–	–	–
– Money market portfolios	5 125 962	859 809	–	6 103	641 223	668 446	2 670 293	409	–	–	245 681	–	33 998
Cash and cash equivalents	2 198 127	1 370 052	–	–	40 756	528 382	203 198	3	–	–	20 468	–	35 268
Total*	12 181 812	2 226 248	10 142	592 441	1 441 146	2 488 226	4 082 650	346 426	116 706	55 001	311 133	7 525	504 168

* *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 2016

32 Financial risk management report *continued*

Credit risk (continued)

Credit quality (continued)

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

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
Commercial mortgage-backed securitisations	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
	–	R12.6 billion	0.00%	Level 2		AA-	Nedgroup Investments Core Income Fund Class C2
	–	R9.2 billion	0.00%	Level 2		AA+	Momentum Money Market Fund B6
	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

32 Financial risk management report *continued*

Credit risk (continued)

Credit quality (continued)

Name and description	2015 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	5 086	R25.3 billion	0.02%	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	429 092	R69.4 billion	0.62%	Level 1 – 97.06% Level 2 – 2.94%	Senior secured – 26.24% Secured – 72.44% Senior Unsecured – 1.32%	A to AAA: 93.17% Bbb: 1.67% F1+: 2.22% Not Rated: 2.94%	Prime Home Loans
Asset backed securitisations	233 452	R28.2 billion	0.83%	Level 1 – 79.69% Level 2 – 20.31%	Senior secured – 16.89% Secured – 79.69% Senior Unsecured – 3.42%	A to AAA: 79.01% BBB: 0.39% CCC: 2.17% Not Rated: 18.43%	Vehicle Loans Corporate Loans Unsecured Loans Equipment Leases
Commercial mortgage-backed securitisations	10 242	R2.5 billion	0.41%	Level 1 – 100%	Senior secured	AA to AAA: 100%	Commercial Property
Collateralised loan obligations	64 033	R33.5 billion	0.19%	Level 1 – 100%	Senior secured – 0.01% Secured – 59.41% Unsecured – 40.58%	AA to AAA: 100%	Vehicle Loans
Collective investment schemes	8 135	R52.8 billion	0.02%	Level 2		AA+	ABSA Money Market Fund
	1 317 999	R14.0 billion	9.42%	Level 2		AA+	Nedgroup Investments Money Market Class C2
	1 325	R12.6 billion	0.01%	Level 2		AA-	Nedgroup Investments Core Income Fund Class C2
	751	R9.2 billion	0.01%	Level 2		AA+	Momentum Money Market Fund B6
	4 818	R26.4 billion	0.02%	Level 2		AA+	Standard Bank Corporate Money Market Fund
	1 421	R13.7 billion	0.01%	Level 2		AA+	Investec Corporate Money Market Fund
	716 812	R4.5 billion	0.02%	Level 2		A	Investec Global Strategic Income Fund

NOTES TO THE ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 December 2016

32 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 94% (R1.6 billion) (2015: 98% – R1.5 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 2016			
Personal Medical Savings Accounts (Note 8)	**4 204 043**	–	–
Trade and other payables (Note 9)	**521 690**	–	–
	4 725 733	–	–
As at 31 December 2015			
Personal Medical Savings Accounts (Note 8)	3 736 659	–	–
Trade and other payables (Note 9)	467 705	–	–
	4 204 364	–	–

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.

32 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
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**	**–**
2015				
Financial assets at fair value through profit or loss:				
Offshore bonds	1 335 137	–	1 335 137	–
Equities	1 415 647	1 413 048	2 599	–
Yield-enhanced bonds	3 058 012	1 477 038	1 545 635	35 339
Inflation-linked bonds	464 574	454 127	10 447	–
Money market instruments	5 125 962	2 334 946	2 545 335	245 681
	11 399 332	5 679 159	5 439 153	281 020

During the 2015 financial year, investments in African Bank to the value of R281 million were classified under level 3 as a result of no trading activity in these instruments due to the curatorship. The valuation was determined using a discounted cash flow methodology based on information available in the market and incorporates certain assumptions applicable to these instruments. The discount rate was determined by adding a premium to comparative rates of similar institutions operating in the unsecured lending market. During the year under review, trading activity resumed on African Bank instruments and these have now been reclassified to Level 2.

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 2016

32 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 2016 R'000**	Fair value as at 31 December 2015 R'000	Valuation techniques	Observable Input
Financial assets at fair value through profit or loss:				
Unlisted:				
Debt securities	**2 810 297**	2 891 219	Reference to listed benchmark bond	Risk free yield to maturity curve risk free zero curve
Money market securities	**2 483 271**	2 547 934	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
	5 293 568	5 439 153		

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 to be 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	**2016**	2015
Total members' funds per Statement of Financial Position	**14 234 461**	12 929 011
Less: cumulative unrealised net gain on remeasurement of investments to fair value	**–**	–
Accumulated funds per Regulation 29	**14 234 461**	12 929 011
Gross annual contribution income	**54 056 212**	49 759 756
Solvency margin		
= Accumulated funds / gross annual contribution income x 100	**26.33%**	25.98%

At 31 December 2016, the Scheme's regulatory capital level of 26.33% (2015: 25.98%) was R719 million (2015: R488 million) more than the statutory capital requirement of 25%.

33 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 31.

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 32 and judgements relating to the impairment of assets are set out under Note 7 of the Accounting policies.

34 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 as 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 2016, the Scheme's solvency level dropped below 25% during January and November. The reason for the drop below 25% in January 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, caused the solvency ratio to drop below 25%.

  At 31 December 2016, the Scheme's accumulated funds expressed as a percentage of gross annual contributions was 26.33% (2015: 25.98%), which exceeds the statutory solvency requirement of 25%.

- **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 2016 the following plans did not comply with Section 33 (2):

	Net healthcare result (R'000)	Net surplus/ (deficit) (R'000)
Benefit plan		
Executive	**(350 528)**	**(341 248)**
Classic Comprehensive	**(872 500)**	**(741 888)**
Classic Comprehensive Zero MSA	**(2 040)**	**(1 072)**
Coastal Saver	**(184 640)**	**(31 011)**
Coastal Core	**(32 915)**	**67 366**
KeyCare Plus	**(579 629)**	**(314 518)**

NOTES TO THE ANNUAL FINANCIAL STATEMENTS *continued*

for the year ended 31 December 2016

34 Non-compliance matters *continued*

The performance of all benefit options is monitored on a continuous basis with a view to improving their financial outcomes, and we continually evaluate different strategies to address the deficit in these plans.

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.

- **Investment 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 Medical Schemes Act 131 of 1998.

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

  During August and September, a breach of the Scheme's foreign derivative exemption (Category 7 (b) of Annexure B) occurred where the Investec Target Return Bond Fund portfolio (collective investment scheme) derivative exposure was greater than 2.5% due to large foreign exchange fluctuations as a result of Brexit. The breach was rectified on 21 September 2016. This was duly reported to the CMS on 26 October 2016. It should be noted despite the recorded breach at an Investec Target Return Bond Fund portfolio level, the fair value of the Scheme's total offshore derivative exposures was only 0.19% of the aggregate fair value of Scheme liabilities and minimum accumulated funds at 31 August 2016.

34 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.

  DHMS however employ 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 0.02% 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.

- **Claims paid in excess of 30 days**

  Section 59 (2) of the Act states that: "A medical scheme shall, in the case where an account has been rendered, subject to the provisions of this Act and the rules of the medical scheme concerned, pay to a member or a supplier of service, any benefit owing to that member or supplier of service within 30 days after the day on which the claim in respect of such benefit was received by the medical scheme."

  During the process of transitioning to a new claims administration platform, quality assurance processes were significantly extended to ensure valid, accurate and complete processing of claims on the new claims administration platform. This process resulted in a delay in the processing of claims payments. A total number of 34 claims were identified that were paid later than 30 days after claims notification date. The value of exceptions should be considered in the context of net claims incurred of R36.6 billion during 2016. Exceptions identified pertained to a specific event i.e. transitioning to a new claims administration platform and thus no further action is required. The claims administration platform is set up to ensure payments occur within regulatory requirements.