



**Auditors of Medical Schemes
Principal Officers
Boards of Trustees
Medical Scheme Administrators
Other interested parties**

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ISSUES ENCOUNTERED DURING THE EVALUATION OF MEDICAL SCHEME ADMINISTRATORS REGARDING THE AUDITING OF MEDICAL SCHEMES

Introduction

On-site evaluations of third party medical scheme administrators' compliance with the administration standards commenced in 2003, and subsequently the evaluation of compliance process was rolled out to self-administered schemes in 2008.

During these evaluations, operational ability and compliance by an administrator (third party and self-administered schemes) with all of the administration standards is physically tested by assessing substantiated evidence, detailed system functionality testing and similar actions. The following areas, as included in the administration standards, are evaluated:

1. General compliance (evaluation of administration agreements, financial soundness, indemnity and fidelity insurance in place etc.)
2. System assessment (high level business process flows and application software logical designs)
3. Member record management (processing of membership applications, changes thereto and compliance with member specific rules in terms of benefit design and option specific limitations).
4. Contribution management (contributions raised, received and allocated at individual member level in full compliance with the medical scheme rules and the Act; comprehensive application of the scheme's credit control policies and membership management including compliance with termination procedures).
5. Claims management (capturing, processing, validation and payment as well as the management of member savings accounts, in full compliance with the medical scheme rules and the Act).

A statutory body established in terms of the
Medical Schemes Act, 1998 (Act 131 of 1998)

Chairperson: Prof. W Pick Acting Registrar & CEO: P Matshidze



6. Financial management reporting (appropriate recording and reconciliation of financial transactions in the scheme's financial records, as well as complete and accurate reporting thereof as required).
7. Information management and data control (comprehensive off-site data storage, backup policy, disaster recovery and business continuity processes; confidentiality, security and integrity of data).
8. Customer services (appropriate customer services to members, providers, and brokers; broker remuneration management in full compliance with the Act).

Evaluation findings

The tests and verifications performed during the on-site evaluations revealed that certain audit functions and suitable reporting were being either neglected or inadequately performed. This, in turn, results in substantial risks, both in respect of medical schemes but also administrators due to the failure to comply with legislative requirements, the rules of medical schemes or accreditation standards. This situation calls for action to be taken.

Often the issues identified have an impact on the financial reporting of the medical scheme due to either the nature or monetary value of the transactions involved. One would expect such issues to have been addressed by medical schemes and their audit processes, both internal and external or the administrator's risk management and statutory audit processes. Regrettably these transactions are not disclosed appropriately or are not properly audited and therefore not reported on by auditors to the extent that an opinion is expressed on the actual financial performance of the Scheme and the contracted parties.

The office has established that the matters are not identified by external auditors, not because they are not following appropriate audit procedures but rather as a result of audit clerks who perform the audit tests and who may not be familiar with the Act, Regulations and the medical scheme rules. We therefore come to the conclusion that those involved in the audit process at scheme level may sometimes not have a comprehensive understanding of the functioning of medical schemes and the administration processes.

Listed below are some of the issues identified over the past 3 years:

Issue	Impact on scheme	Impact on administrator
1. The scheme's audit report reflects that the audit was performed in compliance with the Companies Act.	This could indicate that the scheme auditors view the audit of a medical scheme to be the same as that of a company, i.e. emphasis is placed on the verifying the balance sheet balances, whilst not enough emphasis is placed on the reliability of entries in the income statement.	None.
2.1 Contributions in respect of ancillary products are raised in respect of unrelated products (e.g. gym membership, funeral cover and loyalty programmes) and collected through the scheme.	The scheme contravenes Section 26(1)(c), (4) and (11) of the Act.	The raising and collection of such amounts through the scheme's system and/or bank accounts is in contravention of Section 26(1)(c), (4) and (11) of the Act. Serious non-compliance as the administrator fails to administer in terms of prevailing legislation and the



<p>2.2 Ancillary product related amounts are recorded in the scheme's financial records, e.g. the debtors age analysis and general ledger.</p>	<p>The raising and collection of such amounts through the scheme's system and/or bank accounts is in contravention of Section 26(1)(c), (4) and (11) of the Act. Serious non-compliance with the Act.</p>	<p>accreditation standards.</p>
<p>3. One or more of the scheme's bank accounts are NOT in the name of the medical scheme. (E.g. in one instance one of the main bank accounts of the scheme, into which the debit order contributions were received, was in fact in the name of the administrator with an attempted session in favour of the Scheme.)</p>	<p>This is in contravention of Section 26(1)(c) and Regulation 23. Such scheme monies are deemed to vest inappropriately in another entity the result of which trustees have no ownership and control over scheme funds. Also, if the administrator or such other entity in whose name the bank account is becomes insolvent or is liquidated, the scheme is at risk as one would have to prove that the bank account should not be attached in favour of unrelated creditors associated with the administrator or such other entity to enable its creditors to be paid.</p>	<p>This is in contravention of Section 26(1)(c) and Regulation 23. The administrator or such other entity unlawfully controls assets belonging to client schemes. The administrator will gain financially at the expense of client schemes in the event of liquidation or seizure of assets on some or other form based on perceived lawful ownership.</p>
<p>4. Payments made towards contracted fees do not correspond with the signed agreements.</p>	<p>Incorrect or invalid amounts are paid from scheme funds in respect of contracts signed with e.g. an administrator, managed care organisation or other service providers. This results in incorrect and unreliable reporting of transactions and demonstrates poor governance.</p>	<p>An administrator's ability to accurately administer and report on a scheme's financial performance is compromised. Results in failure to comply with accreditation standards and contract.</p>
<p>5.1 Broker commissions are calculated and paid on contributions <u>raised</u> and not received.</p> <p>5.2 Broker commissions paid in advance in lieu of broker services still to be rendered.</p>	<p>Contravention of Regulation 28(5) and could have a negative financial impact on the scheme where broker commissions are paid but the relating member contributions are never received or incorrect payments are made.</p> <p>This is in contravention of Regulation 28(5) which requires broker commissions to be calculated and paid <u>monthly after</u> the receipt of the relevant contribution. This could also have a negative financial impact on</p>	<p>Contravention of Regulation 28(5) and could have a negative financial impact on the scheme where broker commissions are paid but the relating member contributions are never received. Also, this negatively impacts on the administrator's ability to appropriately manage broker remuneration management as required by the Act and administration standards.</p> <p>This is in contravention of Regulation 28(5) which requires broker commissions to be calculated and paid <u>monthly after</u> the receipt of the relevant contribution. This</p>



	<p>the scheme where members linked to the broker resign or fail to pay their contributions in respect of the periods for which the broker received the advance payments.</p>	<p>could also have a negative financial impact on the scheme where members linked to the broker resign or fail to pay their contributions in respect of the periods for which the broker received the advance payments.</p> <p>Also, this negatively impacts on the administrator's ability to appropriately manage broker remuneration management as required by the Act and administration standards.</p>
<p>5.3 Collection from members and payment of "professional fees" to brokers.</p>	<p>This is in contravention of Regulation 28(6)(b) which requires such fees to be directly negotiated and paid between the member and the respective broker.</p>	<p>This is in contravention of Regulation 28(6)(b) which requires such fees to be directly negotiated and paid between the member and the respective broker.</p> <p>Also, this negatively impacts on the administrator's ability to appropriately manage broker remuneration management as required by the Act and administration standards.</p>
<p>5.4 Broker commissions are calculated and paid to brokers in respect of members for whom no signed broker appointment letters / notes have been obtained by the scheme.</p>	<p>The absence of broker appointment letters/ notes from members indicates that such members were "allocated" to a particular broker without even being aware of it. This would result in a broker being remunerated where no broker services are contracted as such and rendered to the member.</p>	<p>This negatively impacts on the assessment of the administrator's ability to appropriately manage broker remuneration management as required by the Act and administration standards.</p>
<p>5.5 Broker commissions are calculated and paid to non-accredited or unlicensed brokers or for periods during which a broker is not accredited or licensed by the Financial Services Board.</p>	<p>This is in contravention of Section 65(3) which requires that broker commissions may only be paid to brokers accredited by the Council. Non-compliance with the Act and results in financial loss to the scheme.</p>	<p>Non-compliance with the Act and this negatively impacts on the assessment of the administrator's ability to appropriately manage broker remuneration management as required by the Act and administration standards.</p>
<p>6. Stale cheques are written back to the income statement before the expiry of 3 year prescription period.</p>	<p>This is in contravention of good accounting practices, the administration standards and legislation governing prescription practices in common law.</p>	<p>Contravenes the administration agreement and accreditation standards.</p>
<p>7. A particular administrator audit</p>	<p>This is in contravention of section</p>	<p>This is in contravention of</p>



<p>report included a matter of emphasis stating that the annual financial statements had been prepared on the going concern basis but was dependent on the <u>continued financial support from the medical scheme.</u></p>	<p>35(8) which states that no medical scheme may invest any of its assets in the business of or grant loans to an administrator or any person associated with an administrator.</p>	<p>section 35(8) which states that no medical scheme may invest any of its assets in the business of or grant loans to an administrator or any person associated with an administrator.</p>
<p>8. Loan accounts between the medical scheme and administrator.</p>	<p>This is in contravention of section 35(8) which states that no medical scheme may invest any of its assets in the business of or grant loans to an administrator or any person associated with an administrator.</p>	<p>This is in contravention of section 35(8) which states that no medical scheme may invest any of its assets in the business of or grant loans to an administrator or any person associated with an administrator.</p>
<p>9. Non-performance of general ledger control account reconciliations, e.g. member contribution debt reconciliations, member debt reconciliations, savings control account reconciliations, etc.</p>	<p>This is in contravention of good accounting practices and the administration standards. It also casts doubt on the accuracy and completeness of monthly financial report of the scheme's affairs.</p>	<p>This is in contravention of good accounting practices and the administration standards.</p>
<p>10. Cash received from members not banked into a bank account in the name of the scheme within one business day of receipt thereof – the particular scheme treated such amounts as petty cash.</p>	<p>This is in contravention of regulation 23 – thus non-compliance with the Act.</p>	<p>This is in contravention of regulation 23.</p>
<p>11. A particular self-administered medical scheme was found to have outsourced their bank reconciliation process to a third party.</p>	<p>This is of great concern considering the high volume of transactions going through scheme bank accounts and the level of control one would expect the scheme to exercise over their own flow of funds. Lack of executive oversight.</p>	<p>Not applicable.</p>
<p>12. Unallocated receipts recorded on the debtors' age analysis but not recorded separately in the general ledger and reported separately in the financial statements.</p>	<p>Not recording or disclosing unallocated receipts separately could give a distorted picture on the outstanding contributions of a medical scheme and could have a significant impact on the board of trustees' assessment of the effectiveness of its credit control processes.</p> <p>This could also impact on the processes surrounding the suspension and/or termination of membership in respect of outstanding contributions.</p>	<p>Not recording or disclosing unallocated receipts separately could give a distorted picture on the outstanding contributions of a medical scheme and could have a significant impact on the board of trustees' assessment of the effectiveness of its credit control processes.</p> <p>This could also impact on the processes surrounding the suspension and/or termination of membership in</p>



		respect of outstanding contributions.
13. No reconciliations and/or follow up performed in respect of provider debt (e.g. claims already paid reversed to a provider).	This may have a negative impact on the financial position of a scheme in terms of the active recovery of outstanding amounts.	This may have a negative impact on the financial position of a scheme in terms of the active recovery of outstanding amounts.
14.1 Interest on savings balances to the credit of a member not calculated in terms of the rules of the medical scheme.	Non-compliance with the Act and rules.	Non-compliance with the Act and rules.
14.2 Savings balances to the credit of the member are only refunded or transferred upon request by the member, resulting in old credit balances carried in the books of the scheme.	This is in contravention of regulation 10(4) and (5) and the rules of the medical scheme.	Non-compliance with the regulations and rules of the medical scheme.
15. Insufficient disaster recovery and business continuity plans in place.	This could pose significant risks to a medical scheme in terms of loss of scheme data and information, inability to process and pay claims, loss of membership, etc.	The loss of data and inability to process claims correctly pose significant risks to the administrator and client schemes with dire consequences. Failure to comply with various standards for accreditation.
16. In many instances the monthly provisions for bad debts and bad debts written off were not done in accordance with a scheme approved credit control policy, or in terms of the accounting policy as included in the financial statements.	This is contrary to good accounting practice and not complying with the administration standards. Results in inaccurate reporting and lack of management.	This is contrary to good accounting practice and not complying with the administration standards.

Way forward

This office will engage with the accounting and audit professions with a view to gain a better understanding of the audit processes being followed given the matters raised herein and to establish a modus operandi to address these matters and rectify them in an appropriate way.

Board of Trustees and Principal Officers are equally alerted to these shortcomings as they are responsible for compiling the financial statements and management accounts whilst internal audit committees of medical schemes should pay particular attention to the reliability and quality of information presented to address deficiencies.



Information sessions are likely to be scheduled to assist stakeholders in ensuring improved accounting and audit processes as we believe that a better understanding of the above will enhance the quality of reporting in terms of the audit report and audit management letter, which in turn should enhance the overall financial and internal controls and governance of medical schemes.

A handwritten signature in black ink, appearing to read 'Danie Kolver'.

Danie Kolver
HEAD OF ACCREDITATION