GENERAL

Call to halve solvency ratio for South African medical schemes

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BHF : info@fanews.co.za

South Africa's two biggest medical schemes are each obliged to hold close to R11 billion in reserve to meet solvency requirements.

“Imagine if half of these reserves could be released and more aggressively or appropriately invested. What could be achieved?” asked Christoff Raath from the Health Monitor Company. He was addressing delegates at the Board of Healthcare Funders' Southern African conference currently underway at the Champagne Sports Resort in the Drakensberg.

The current solvency model requires at least 25% of one year's gross contribution income to be held in reserve but preliminary research suggests that a risk-based approach could release significant funds and still ensure sufficient reserves.

“The origin of the 25% figure is a complete mystery,” Raath said. “The general consensus is that there is no scientific basis for it. It would not be unfair to call it a thumbsuck.”

The solvency reserve is intended to provide a buffer if something goes wrong. But for Raath the magnitude of catastrophe which would have to occur in order to deplete the reserves of the larger medical schemes is “akin to the black death – unimaginable”.

According to Raath, one of the biggest problems with the current solvency model is that it rewards loss-making schemes and penalises surplus-making schemes.

“It is effectively a tax on the members as contributions are invariably increased to maintain the solvency level,” he said.

In addition, new schemes face a significant cost as they build their reserves. And while open schemes fly close to the minimum requirement, restricted schemes are shedding their surplus reserves.

Faced with similar problems in Europe, actuaries are working on Solvency II, a system which is based on three pillars: quantitative, qualitative and reporting and disclosure.

This model looks at solvency capital requirements in the same way as an architect taking a calculated risk and building a house within a 200 year flood line.

“It is the kind of approach that makes pessimists very happy,” Raath joked. “You think of stuff that can go wrong, attach a probability and a value to each event and then decide on the kind of reserves that are needed.”

A similar solution is being sought in South Africa.

Do we need high solvency levels? Raath quoted research based on the annual reports of the Council for Medical Schemes (CMS) over the past decade. More than 1000 observations of actual financial results were examined. It showed that 76% of medical schemes recorded surpluses. No large open medical scheme lost more than 12.5% of reserves in a single year.

“There are some significant losses,” Raath said. “one scheme lost 30% of its reserves in a single year, but most of the ones that had problems were already under curatorship.”

“The present 25% may be an impediment to growth. All stakeholders recognise this,” Raath said. “I

want to suggest a simplified, pragmatic risk-based capital approach which excludes medical savings accounts. For the first time, the CMS is open to alternative models. We are hoping the Council will now endorse research to come up with a more appropriate model.”