



Audit Program Guidance for the 2015 Annual PHIAC 2 Returns

June 2015

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Section 1 - Audit Program Guidance for PHIAC 2 Annual Returns

Audit program guidance for PHIAC 2 Annual Returns

Exclusion Clause

The “*Audit Program Guidance for PHIAC 2 Annual Returns*” (the **Guidance**) is a publication produced by the Australian Prudential Regulation Authority (APRA) to assist auditors of Registered Private Health Insurers (the **Insurers**) in the audit of their clients’ PHIAC 2 Annual Return (the **Return**). Auditors should, however, be aware that this program is not designed to be a complete set of procedures and is not a set of binding rules. As systems in Insurers vary, the program should be tailored to each Insurer’s circumstances. Reference must also be made to the “*PHIAC 2 Guidance Note*” (refer Appendix A).

The Guidance is not to be considered a standalone document. Under no circumstances should auditors rely solely upon the Guidance to the exclusion of their duties to perform audit procedures to arrive at their audit opinion on the Return.

It is the responsibility of the auditor to ensure that audit programs and processes are consistent with their internal methodology and are fully compliant with the requirements of Australian Auditing Standards, Guidance Statements and other pronouncements issued by the Auditing and Assurance Standards Board (**AUASB pronouncements**).

The Guidance is specific to the Return and does not cover the audit requirements of the *Private Health Insurance Act 2007* (the **Act**) in respect of the PHIAC 1 Annual Return.

Introduction

The Guidance has been written to assist the auditors of Insurers in their audit of the Return. It takes into account the arrangements contained in:

- the Act
- the *Private Health Insurance (Health Benefits Fund Administration) Rules 2007* (the **Rules**)
- the *Private Health Insurance (Health Benefits Fund Administration) Amendment Rule 2013 (No. 1)*
- the *Private Health Insurance (Insurer Obligations) Rules 2009*
- the *Private Health Insurance (Risk Equalisation Administration) Rules 2007*,
- the PHIAC 2 Guidance Note, and
- PHIAC Circulars.

The provision of the audit certification to APRA must meet the deadline as outlined in PHIAC Circular No 145/06. This deadline applies, regardless of when the Insurer's financial year ends.

Purpose of PHIAC 2 Annual Return

APRA established, under the Act, a two-tier regime of prudential reporting with each tier considering the capital requirements in a different set of circumstances.

The first tier, addressed by the Solvency Standard contained in Schedule 2 of the Rules, is intended to ensure the basic liquidity of the health benefits fund (**the Fund**) conducted by the Insurer. The stated purpose of the Solvency Standard under Division 140 of the Act is:

"to ensure, as far as practicable, that at any time the financial position of a health benefits fund conducted by a private health insurer is such that the insurer will be able, out of the fund's assets, to meet all liabilities that are referable to the fund as those liabilities become due."

The second tier, covered by the capital adequacy standard contained in Schedule 3 of the Rules, is intended to secure the financial soundness of the Fund in a going concern sense and has a stated purpose under Division 143 of the Act:

"to ensure, as far as practicable, that there are sufficient assets in a health benefits fund conducted by a private health insurer to provide adequate capital for the conduct of the fund:

- a) in accordance with this Act; and*
- b) in the interests of the policy holders of the fund."*

The purpose of the audit of the Return is ensure that the information provided by the Insurers is accurate and allows APRA to prepare its report to Parliament in accordance with section 264-15 of the Act.

Scope of Audit

The auditor of a Fund is required to determine whether the information contained in the Return for the year to 30 June 2015, has been prepared in accordance with the requirements of the Act, the *PHIAC 2 Guidance Note* and the *Capital Adequacy Standards* contained within the Rules (refer Appendix A). The Return contains 10 embedded worksheets:

- Worksheet 1: Cover page
- Worksheet 2: CA Forecasts
- Worksheet 3: Solvency Forecasts
- Worksheet 4: Revenue of the Fund
- Worksheet 5: Expenses of the Fund
- Worksheet 6: Capital Transfers in/out of the Fund

- Worksheet 7: Assets of the Fund
- Worksheet 8: Liabilities of the Fund
- Worksheet 9: Related Party Disclosures
- Worksheet 10: Claims Data

Worksheet 2 and 3 are to be reviewed in accordance with Standard on Assurance Engagements ASAE 3450 *Assurance Engagements involving Corporate Fundraisings and / or Prospective Financial Information*.

Worksheets 4-10 are to be audited in accordance with Australian Auditing Standards.

Where the auditor is unable to provide an unqualified conclusion that the Return reflects the provisions of the above legislation, a qualified audit report must be provided to APRA, which details the nature of the qualification.

As the revised Solvency Standard came into effect on 1 July 2014, insurers are required to complete worksheet 3 of the Return - Solvency Forecast. Consequently, auditors are now required to conduct an audit of, and provide assurance in relation to, worksheet 3 for the year ending 30 June 2015.

Audit Approach

Due to the nature of the Return, a large proportion of the data will be extracted from already audited sources. Where possible, reliance can be placed on the work performed in forming an opinion on the *Corporations Act 2001 (the Corporations Act)* financial statements, other audited accounts and the audited PHIAC 1 Return.

Given the overlaps, APRA expects that the auditor of the Return is the same as the registered auditor of the Corporations Act financial statements.

Despite the presence of the Corporations Act financial statements, auditors should be aware that the audit is of the Fund and not the private health insurer as an entity. Under section 137-1 of the Act, a private health insurer must keep assets of a health benefits fund distinct and separate from assets of other health benefits funds and from all other money, assets or investments of the insurer. As such, where the Insurer has activities outside of the Fund, the reliance on the Corporations Act financial statements alone may not be applicable. That is, where values required in the Return have not been audited elsewhere, auditors are required to apply Australian Auditing Standards to enable them to provide reasonable assurance over those disaggregated amounts.

Assurance must be gained over the source data used to prepare the Return (such as the trial balance and underlying accounting records) by performing procedures necessary to gain sufficient and appropriate evidence in order to form an opinion as to whether the Return has been prepared in accordance with the Act, the *PHIAC 2 Guidance Note* and

Rules. Such procedures must be completed with reference to the requirements of the AUASB pronouncements.

Auditors should note that APRA has the power to issue directions under the Act or determine a supervisory adjustment under the Rules. These may affect the calculation of the capital adequacy requirements. Prior to commencing audit procedures, the auditor must enquire as to whether any such directions or determinations have been issued, and if so, assess the impact on the calculation, and the audit of the Return.

Materiality - Application to PHIAC 2 Annual Return

The level of materiality applied in auditing the Corporations Act financial statements may not be appropriate in the context of the audit of the Return. There is a risk that a misstatement material to the Return may go undetected.

The materiality for the Return must be calculated independently of that applied for the purposes of the Corporations Act financial statements. The auditor must ensure that materiality is determined and applied in accordance with ASAE 3450 and Auditing Standard ASA 320: *Materiality in Planning and Performing an Audit*.

Security of Spreadsheet - Integrity of Data and Formulae

The Return is prepared in a Microsoft Excel or XML-coded template. Auditors should ensure that the most current version of the template, as available from APRA's website, has been used in the preparation of the Return.

The Excel template contains specific cell placements and the XML template specific line structure which record data. There are no locks or passwords over the cells or structure so as to facilitate ease of data input. Auditors should nevertheless ensure that the template has not been amended from what has been provided on APRA's website.

The Excel Return also contains a data sheet as the last sheet which is critical to APRA's data upload system. Auditors should ensure that the data sheet has not been tampered with and that the integrity of the default links has been maintained.

Major Inherent Risk Areas

Prior to commencing the audit of the Return, the auditor must perform risk assessment procedures to identify and assess the risks of material misstatement of the information contained in the Return. These risks may or may not be consistent with those identified for financial statement audit purposes in accordance with ASA 315 *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*.

In order to appreciate the impact of any errors in the Return, the auditor must understand the basis of the calculation that determines the capital adequacy of the Fund. The method of calculation is provided in the Rules.

The following are considered to be some of the major inherent risk areas from APRA's perspective:

Outstanding Claims

The unrepresented and outstanding claims in Section 1 and outstanding claims liability in Section 3 of Worksheet 8 *Liabilities of the Health Benefits Fund* are key components in the Return. They have the same meaning under AASB 1023. These provisions relate to the various insurance activities conducted by the Fund (e.g. health insurance, overseas student health cover, overseas visitor cover, etc.) and are calculated by employing actuarial methods and assumptions to arrive at a central estimate of claims and risk margins that have been incurred at the balance sheet date but are yet to be presented, plus a provision for the cost of settling these claims.

To ensure consistency of reporting, all unpaid claims (including those that have been processed but not actually paid) at balance date must be included in both the unrepresented and outstanding claims in Section 1 and outstanding claims liability in Section 3, rather than trade creditors or other current liabilities.

Given the level of judgement applied by the Insurer in determining the actuarial methodologies and assumptions, there is an inherent risk in the valuation of the outstanding claim liability. It is expected that the auditor will use actuarial audit support experts to independently assess the reasonableness of the methodology and assumptions applied in arriving at the best estimate and risk margin.

Risk Equalisation

The risk equalisation liability (or asset) component reflects the best estimate of the net amount of payments to, and recoveries from, the Risk Equalisation Trust Fund (**RETF**) in respect of the period up to the balance sheet date. This amount is not known in certainty as the actual figure is dependent upon the benefit payments of all other Insurers and is not determined until after the balance sheet date. As this estimate is subject to significant levels of judgement by the Insurer, it is an area of inherent risk.

It is expected that the auditor will use actuarial audit support experts to independently assess the reasonableness of the methodology and assumptions applied in arriving at the best estimate.

Risk Equalisation Outstanding Claims Liability Component

The risk equalisation outstanding claims liability (or asset) component reflects the central estimate of the net amount of payments to, and recoveries, from the RETF in respect of the outstanding claims liability. This amount is not known in certainty as the calculation of this provision is dependent upon the inherent uncertainty in the valuation of the outstanding

claims liability (as described above) and the ultimate recovery is dependent on the benefit payments of all other Insurers for a future period.

Given the level of judgement applied by the Insurer in determining the actuarial methodologies and assumptions, there is an inherent risk in the valuation of the risk equalisation outstanding claims liability component.

It is expected that the auditor will use actuarial audit support experts to independently assess the reasonableness of the methodology and assumptions applied in arriving at the best estimate.

Unexpired Risk Liability and Future Claims Liability

The unexpired risk liability has the same meaning given in the liability adequacy test in AASB 1023 whilst the future claims liability is defined in the Rules. These estimates are subject to actuarial methods and assumptions and, as they require significant levels of judgement to be applied by the Insurer, are areas of inherent risk.

It is expected that the auditor will use actuarial audit support experts to independently assess the reasonableness of the methodology and assumptions applied.

Section 2 - Controls Testing Program

Introduction

The auditor must perform an assessment of the processes, controls and procedures that the Insurer has in place in respect of preparing a Return in compliance with the requirements of the Act. Where the auditor can independently validate that the controls over the preparation and review of the Return are operating effectively, reliance may be placed on them. The auditor may wish to consider the use of work performed by the internal auditor (refer Auditing Standard *ASA 610 Using the Work of Internal Auditors*).

It is the responsibility of the auditor to ensure that audit programs and processes are consistent with their internal methodology and are fully compliant with the requirements of the AUASB pronouncements.

Areas of Focus

Assess the processes, controls and procedures surrounding the preparation of the Return. Consideration must be given, but not limited, to (where applicable):

- controls over the input of source data into the underlying processing systems
- general computer and access controls surrounding the underlying processing systems
- controls over the transfer of data from the underlying systems to the general ledger
- controls over the extraction of data required for the Return from the general ledger and/or the underlying processing systems
- controls over the data entry into the spreadsheet template used for the Return, including internal consistency checks and reconciliations to source data
- controls over the preparation of the Return including evidence of independent review, analytical review and data reasonableness checks, and
- controls over the data integrity, including version control, limited access, password protection and final reasonableness review by the officer signing the Return.

The auditor must also consider, where applicable, the effectiveness and integrity of the governance, finance and compliance functions within the Insurer. Areas for focus may include, but not limited, to:

- integrity and level of oversight of senior management, the Audit Committee and the Board
- senior management's attitude towards controls and establishing a robust control environment

- the compliance culture within the Insurer and the processes in place to report and monitor breaches and non-compliance with laws and regulations, including any whistleblower policy
- the Insurer's track record of corrective actions in respect of identified breaches
- the policies and procedures in place to ensure key staff are kept abreast of the laws and regulations applicable to their roles within the Insurer
- the historical accuracy of previous estimates, forecasts and budgets
- the quality and depth of staff resources within the finance department.

Impact on Testing

The auditor may adjust the level of detailed substantive testing required in order to gain sufficient and appropriate evidence to form a conclusion based on the results of the controls testing.

Section 3 - Substantive Testing Program

Worksheet 2 – Capital Adequacy (CA Forecasts)

Overview

Worksheet 2 – CA Forecasts - consists of 2 sections:

- Central estimates
- Stressed estimates

the information from which APRA will use to calculate the stress test amount in the Capital Adequacy Standard.

The information provided in this worksheet is based on monthly forecasts for the next 12 months.

Review Procedures

Review procedures may include, but should not be limited to:

1. Obtain an understanding of the processes undertaken by the Insurer to determine the forecast amounts for each item.
2. When assessing the appropriateness of the forecasts, consider (but do not limit the procedures to) the following:
 - agree the amounts in Sections 1 and 2 to underlying source data and estimation models e.g. historical data, forecasts, strategic plans and budgets for the next 12 months
 - consider the accuracy of previous forecasts by comparing them to actual results achieved
 - discuss the methodologies and assumptions applied by the Insurer, including its anticipated growth policies. Determine whether this is in line with the auditor's expectations given knowledge of the client and the industry
 - determine whether the forecasts for each item have been prepared in accordance with the requirements of the Capital Adequacy Standard and the *PHIAC 2 Guidance Note*, as appropriate
 - where actuarial methods and assumptions have been employed, consider the use of actuarial audit support to review the methods and assumptions for reasonableness
 - ensure there is appropriate evidence to support all material assumptions
 - confirm the mathematical accuracy of the underlying model and the correct application of stated assumptions, and
 - ensure that the forecasts have been approved by senior management and where relevant, consistent with internal policies and guidelines.

Worksheet 3 – Forecasts for Cash Management Amount (Solvency Forecasts)

Overview

Worksheet 3 – Forecasts for Cash Management Amount - consists of 1 section:

- Cashflow projections

the information from which APRA will use to calculate the cash management amount under the Solvency Standard.

The data provided in this worksheet gives important information on liquidity risk in the health benefits fund. The central estimate forecasts of cash flows in the next 30 days put the stressed net cash outflow in context, and the projections out to 90 days give an indication of likely compliance with the Solvency Standard.

Review Procedures

Review procedures may include, but should not be limited to:

3. Obtain an understanding of the processes undertaken by the Insurer to determine the forecast amounts for each item.
4. When assessing the appropriateness of the forecasts, consider (but do not limit the procedures to) the following:
 - agree the amounts in Section 1 to underlying source data and estimation models (if any) e.g. historical data, forecasts, bank accounts, maturity of investments, as well as the timing and volatility of revenue and expenses
 - consider the accuracy of previous cashflow projections by comparing them to actual results achieved
 - discuss the methodologies and assumptions applied by the Insurer, including its anticipated cash inflows and outflows. Determine whether this is in line with the auditor's expectations given knowledge of the client and the industry
 - determine whether the forecasts for each item have been prepared in accordance with the requirements of the Solvency Standard and the *PHIAC 2 Guidance Note*, as appropriate
 - where actuarial methods and assumptions have been employed, such as in relation to the Stressed Net Cash Outflow Amount, consider the use of actuarial audit support to review the methods and assumptions for reasonableness
 - ensure there is appropriate evidence to support all material assumptions
 - confirm the mathematical accuracy of any underlying cashflow estimation model and the correct application of stated assumptions, and

- ensure that the forecasts have been approved by senior management and where relevant, consistent with the liquidity management plan, internal policies and guidelines.

Worksheet 4 – Revenue of the Fund

Overview

Worksheet 4 contains the following sections:

1. Insurance Revenue
 - a. HIB Premium Revenue
 - b. HRB Premium Revenue
 - c. Insurance Discounts and Promotions
2. Other Business Revenue
 - a. Gross HRB Revenue – non insurance activities
 - b. Net other Operational Revenue
3. Net Investment Income

Audit Procedures

Audit procedures may include, but should not be limited to:

1. Agree or reconcile the total of amounts entered by the Insurer in each section to the audited trial balance
2. Agree the split by services covered/product/benefit type by state/territory of residence to the audited trial balance and/or audited underlying accounting records, where applicable
3. Agree that only revenue relating to the Fund has been disclosed in the Return
4. Determine whether the amounts entered for each item have been prepared in accordance with the requirements of the *PHIAC 2 Guidance Note* and AASB 1023
5. Where details cannot be agreed to audited sources, consider what other procedures will be required to achieve a sufficient level of audit assurance over the split (e.g. substantive analytical procedures)
6. Discuss any differences with the Insurer and obtain support for any material reconciling items.

Worksheet 5 – Expenses of the Fund

Overview

Worksheet 5 contains the following sections:

1. Insurance claims
 - a. HIB
 - b. HRB
2. Other Business Expenses
 - a. All other business expenses
 - b. Claims handling expenses (recognised in 2a)
3. Non-operating expenses

Audit Procedures

Audit procedures may include, but should not be limited to:

1. Agree or reconcile the total of amounts entered by the Insurer in each section to the audited trial balance.
2. Agree the split by services covered / product / benefit type by state / territory of residence to the audited trial balance and / or audited underlying accounting records, where applicable.
3. Agree that only expenses relating to the Fund have been disclosed in the Return
4. Determine whether the amounts entered for each item have been prepared in accordance with the requirements of the *PHIAC 2 Guidance Note* and AASB 1023
5. Where details cannot be agreed to audited sources, consider what other procedures will be required to achieve a sufficient level of audit assurance over the split (e.g. substantive analytical procedures).
6. Discuss any differences with management and obtain support for any material reconciling items.

Worksheet 6 – Capital Transfers in/out of the Fund

Overview

Worksheet 6 includes information on the remaining balance sheet movements, being capital transfers in and capital distributions and transfers out of the Fund.

Audit Procedures

Audit procedures may include, but should not be limited to:

1. Agree all amounts disclosed in 1a and 1b to the audited trial balance and/or audited statutory financial statements
2. Agree that only capital transfers into or out of the Fund have been disclosed in the Return
3. Discuss any differences with the Insurer and obtain support for any material reconciling items. Where details cannot be agreed to audited sources, consider what procedures will be required to achieve a satisfactory level of assurance.

Worksheet 7 – Assets of the Fund

Overview

Worksheet 7 consists of 4 sections:

1. Directly held assets
2. Indirectly held assets
3. Other assets
4. Counterparty disclosure

the information from which is used to monitor compliance with the Capital Adequacy and Solvency Standards.

Audit Procedures

Audit procedures may include, but should not be limited to:

Section 1 – Directly Held Assets

1. Agree the amounts in Section 1 to the Balance Sheet and accompanying notes of the audited statutory financial statements if applicable.
2. Ensure that only assets held by the Fund have been disclosed
3. Where necessary, agree additional detail to the audited trial balance and audited underlying accounting records.
4. Agree the split of assets by APRA investment type activity to audited underlying accounting records. Ensure classification is in accordance with the *PHIAC 2 Guidance Note*. Emphasis should be given to the classification of assets and investments as this directly impacts the capital adequacy reserves.

Section 2 – Indirectly Held Assets

5. Agree the total of amounts in Section 2 to the appropriate line items in the Balance Sheet and accompanying notes of the audited statutory financial statements if applicable.
6. Agree underlying assets by class to statements received from investee, such as the managed fund in which these investments are held.
7. Agree the split of assets by APRA investment type activity to audited underlying accounting records. Ensure classification is in accordance with the *PHIAC 2 Guidance Note*. Emphasis should be given to the classification of assets and investments as this directly impacts the capital adequacy reserves.

Section 3 – Other Assets

8. Agree the amounts in Section 3 to the Balance Sheet and accompanying notes of the audited statutory financial statements if applicable.

9. Where necessary, agree additional detail to the audited trial balance and audited underlying accounting records.

Ensure classification of assets is in accordance with the *PHIAC 2 Guidance Note*. Emphasis should be given to the classification of assets and investments as this directly impacts the adequacy reserves.

Section 4 – Counterparty disclosure

10. Agree the amounts by counterparty type and credit grade rating for each to audited underlying accounting records.
11. Agree amounts in calculations in 4b to underlying accounting records.
12. Ensure calculations in 4b have been performed in accordance with the requirements of the Capital Adequacy Standard, as described in the *PHIAC 2 Guidance Note*.
13. Where details cannot be agreed to audited sources, or estimates have been used as inputs to the calculation, consider what other procedures will be required to achieve a sufficient level of audit assurance over the amount. Assess the reasonableness of any estimates.

Worksheet 8 – Liabilities of the Fund

Overview

Worksheet 8 consists of 5 sections:

1. Insurance liabilities
2. Other liabilities
3. Prudent liabilities
4. Subordinated debt
5. Supervisory arrangements

the information from which is used to monitor compliance with the Capital Adequacy and Solvency Standards.

Audit Procedures

Audit procedures may include, but should not be limited to:

Total Fund Liabilities

1. Ensure the sum of the values in Sections 1 and 2 agree to the total value of liabilities in the audited statutory financial statements if applicable
2. Ensure that only liabilities incurred by the Fund have been disclosed.

Section 1 – Insurance Liabilities

3. Agree or reconcile the amounts in Section 1 to the Balance Sheet and accompanying notes of the audited statutory financial statements if applicable.
4. Where necessary, agree additional detail to the audited trial balance and audited underlying accounting records.
5. Agree the split by HIB / HRB to the audited trial balance and / or audited underlying accounting records, where applicable.
6. Determine whether the amounts entered for each item have been prepared in accordance with the requirements of the *PHIAC 2 Guidance Note* and AASB 1023
7. Where details cannot be agreed to audited sources, consider what other procedures will be required to achieve a sufficient level of audit assurance over the split (e.g. substantive analytical procedures).
8. Any discrepancies must be discussed with the Insurer and sufficient audit evidence obtained for material reconciling items.

Section 2 – Other Liabilities

9. Agree or reconcile the amounts in Section 2 to the Balance Sheet and accompanying notes of the audited statutory financial statements if applicable.
10. Where necessary, agree additional detail to the audited trial balance and audited underlying accounting records.

Capital Adequacy Standard Liabilities

Section 3 – Prudent Liabilities

11. Ensure calculations in Section 3 have been performed in accordance with the requirements of the Capital Adequacy Standard, as described in the *PHIAC 2 Guidance Note*.
12. Where details cannot be agreed to audited sources, or estimates have been used as inputs to the calculation, consider what other procedures will be required to achieve a sufficient level of audit assurance over the amount. Assess the reasonableness of any estimates.
13. Where actuarial methods and assumptions have been employed, consider the use of actuarial audit support actuary to review the methods and assumptions for reasonableness

Section 4 – Subordinated Debt

14. Review the level of subordinated debt used by the Fund to finance its capital requirements and confirm that this is in line with the auditor's understanding of the business of the Insurer.

Where subordinated debt has been used, sight appropriate approval from APRA for the current year return and sight the subordinated debt contract focussing on (but not limiting procedures to) the amount per the contract, the parties involved in the contract and that the debt is subordinate in obligation to all other liabilities.

Section 5 – Supervisory Adjustments

15. Where amounts are shown in Section 5, sight notice in writing from APRA prescribing the amount, factor figure and / or methodology.
16. Where no such prescription has been made by APRA, ensure nil for all items.

Worksheet 9 – Related Party Disclosures

Overview

Worksheet 9 contains details of related party transactions and balances.

'Related Party' is defined in AASB 124 *Related Party Disclosures* (AASB 124) as:

"a person or entity that is related to the entity that is preparing its financial statements (in this Standard referred to as the 'reporting entity')."

- (a) *A person or a close member of that person's family is related to a reporting entity if that person:*
 - (i) *has control or joint control of the reporting entity;*
 - (ii) *has significant influence over the reporting entity; or*
 - (iii) *is a member of the key management personnel of the reporting entity or of a parent of the reporting entity.*
- (b) *An entity is related to a reporting entity if any of the following conditions applies:*
 - (i) *The entity and the reporting entity are members of the same group (which means that each parent, subsidiary and fellow subsidiary is related to the others).*
 - (ii) *One entity is an associate or joint venture of the other entity (or an associate or joint venture of a member of a group of which the other entity is a member).*
 - (iii) *Both entities are joint ventures of the same third party.*
 - (iv) *One entity is a joint venture of a third entity and the other entity is an associate of the third entity.*
 - (v) *The entity is a post-employment benefit plan for the benefit of employees of either the reporting entity or an entity related to the reporting entity. If the reporting entity is itself such a plan, the sponsoring employers are also related to the reporting entity.*
 - (vi) *The entity is controlled or jointly controlled by a person identified in (a).*
 - (vii) *A person identified in (a)(i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity)."*

Further definitions from AASB 124 are as follows:

"Close members of the family of a person are those family members who may be expected to influence, or be influenced by, that person in their dealings with the entity and include:

- (a) that person's children and spouse or domestic partner;*
- (b) children of that person's spouse or domestic partner; and*

(c) dependants of that person or that person's spouse or domestic partner.

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, including any director (whether executive or otherwise) of that entity."

The terms 'control', 'joint control' and 'significant influence' are defined in AASB 10, AASB 11 Joint Arrangements and AASB 128 Investments in Associates and Joint Ventures and are used in this Standard with the meanings specified in those Standards.

Audit Procedures

1. Agree all details to audited related party note in the statutory financial statements and supporting audit work papers.
2. Ensure all related parties are identified in accordance with the requirements of AASB 124.

Worksheet 10 – Claims Data

Overview

Worksheet 10 contains details of claims payments made in respect of the HIB.

Audit Procedures

1. Agree claims data to underlying records.
2. Where details cannot be agreed to audited sources, consider what other procedures will be required to achieve a sufficient level of audit assurance over the amount. Assess the reasonableness of any estimates.
3. Where actuarial methods and assumptions have been employed, consider the use of actuarial audit support actuary to review the methods and assumptions for reasonableness.

Section 4 - Completion Program

Pro forma audit opinion

[TO BE PREPARED ON AUDIT FIRM LETTERHEAD]

INDEPENDENT AUDITOR'S REPORT

To [Title of Those Charged with Governance] of [name of insurer]

Section A - Reasonable Assurance on Worksheets 4-10

We have audited the following worksheets in the attached PHIAC 2 Annual Return (**the Return**) of [name of insurer], as issued by APRA for the purpose of providing an Annual Report to Parliament for the year ended 30 June 2015:

4. Revenue of the Fund
5. Expenses of the Fund
6. Capital Transfers
7. Assets of the Fund
8. Liabilities of the Fund
9. Related Party Disclosures
10. Claims Data

Responsibilities of Management and Directors

Management and the Directors of [name of insurer] are responsible for the preparation and fair presentation of the Return and the information it contains, in accordance with the requirements of the *Private Health Insurance Act 2007 (the Act)*, *Schedule 2 (the Capital Adequacy Standard)* of the *Private Health Insurance (Health Benefits Fund Administration) Rules 2013 (the Rules)* and the *PHIAC 2 Guidance Note*. This includes such internal control as management determines is necessary to enable the preparation and fair presentation of the Return that is free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on the Return based on our audit. We conducted our audit in accordance with Australian Auditing Standards. Those Auditing Standards require that we comply with relevant ethical requirements and plan and perform the audit to obtain reasonable assurance whether, in all material respects, the Return has been prepared in accordance with the Act, the Rules and the *PHIAC 2 Guidance Note*.

Our audit did not involve an analysis of the prudence of business decisions made by those charged with governance. Our audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the Return. The procedures selected depend on our judgement, including assessment of the risks of material misstatement of the Return, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the insurer's preparation and fair presentation of the Return 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 insurer's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the Return.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Independence

In conducting our audit we have met the independence requirements of the Australian professional accounting bodies.

Opinion

In our opinion, in all material respects, worksheets 4 to 10 of the Return of [name of insurer], in respect of the year ended 30 June 2015, have been prepared in accordance with the *Private Health Insurance Act 2007 (the Act)*, *Schedule 2 (the Capital Adequacy Standard)* of the *Private Health Insurance (Health Benefits Fund Administration) Rules 2013* and the *PHIAC 2 Guidance Note*.

Basis of Restriction on Distribution

The Return has been prepared for the purpose of fulfilling the reporting requirements of the insurer under the Act the Rules and the *PHIAC 2 Guidance Note*. We disclaim any assumption of responsibility for any reliance on this report or on the Return to which it relates to any party other than the insurer and APRA, or for any purpose other than that for which it was prepared.

Section B - Limited Assurance on Worksheets 2 and 3

We have reviewed the following worksheet in the attached PHIAC 2 Annual Return (**the Return**) of [name of insurer], as issued by APRA for the purpose of providing an Annual Report to Parliament for the year ended 30 June 2015:

2. Forecasts for Stress Test Amount
3. Forecasts for Cash Management Amount

both referred to herein as **the forecasts**.

The stated basis of preparation used in the preparation of the forecasts by the insurer (the responsible party) is the *Private Health Insurance Act 2007 (the Act)*, *Schedules 2 (the Solvency Standard)* and *3 (the Capital Adequacy Standard)* of the *Private Health Insurance (Health Benefits Fund Administration) Rules 2013 (the Rules)* and the *PHIAC 2 Guidance Note*.

Management's Responsibility

Management and the Directors of [name of insurer] are responsible for the preparation and fair presentation of the Return and the information it contains including the best estimate assumptions underlying the forecasts, in accordance with the requirements of the Act, the Rules and the *PHIAC 2 Guidance Note*. This includes such internal control as management determines is necessary to enable the preparation of forecasts that are free from material misstatement, whether due to fraud or error.

Our Responsibility

Our responsibility is to express a limited assurance conclusion on the forecasts, the best estimate assumptions underlying the forecasts, and the reasonableness of the forecasts themselves, based on our work. We have conducted our engagement in accordance with the Standard on Assurance Engagements ASAE 3450 *Assurance Engagements involving Corporate Fundraisings and/or Prospective Financial Information*.

Our limited assurance engagement consisted of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. It is substantially less in scope than a reasonable assurance engagement conducted in accordance with Australian Auditing Standards and consequently does not enable us to obtain reasonable assurance that we would become aware of all significant matters that might be identified in a reasonable assurance engagement. Accordingly, we do not express a reasonable assurance conclusion.

Conclusion

Based on our limited assurance engagement, which is not a reasonable assurance engagement, nothing has come to our attention which causes us to believe that:

1. management's best estimate assumptions do not provide reasonable grounds for the preparation of the forecasts in the Return of [name of insurer] for the year ended 30 June 2015; and
2. in all material respects, the forecasts:
 - a. are not prepared on the basis of management's best estimate assumptions; and

- b. are not presented fairly in accordance with the *Private Health Insurance Act 2007, Schedules 2 (the Solvency Standard) and 3 (the Capital Adequacy Standard)* of the *Private Health Insurance (Health Benefits Fund Administration) Rules 2013* and the *PHIAC 2 Guidance Note*; and

3. the forecasts themselves are unreasonable.

The forecasts have been prepared by management and adopted by the directors in order to provide APRA with the data necessary to calculate the stress test amount in the Capital Adequacy Standard and the cash management amount in the Solvency Standard. There is a considerable degree of subjective judgement involved in preparing the forecasts since they relate to events and transactions that have not yet occurred and may not occur. Actual results are likely to be different from the forecast since anticipated events or transactions frequently do not occur as expected and the variation may be material.

Management's best estimate assumptions on which the forecasts are based relate to future events and/or transactions that management expect to occur and actions that management expect to take and are also subject to uncertainties and contingencies, which are often outside the control of the insurer. Evidence may be available to support management's best estimate assumptions on which the forecasts are based; however such evidence is generally future-oriented and therefore speculative in nature. We are therefore not in a position to obtain the level of assurance necessary to express a reasonable assurance conclusion on those best estimate assumptions, and accordingly provide a lesser level of assurance on the reasonableness of management's best estimate assumptions. The limited assurance conclusion expressed in this assurance report has been formed on the above basis.

The forecasts have been prepared by management for the purpose of fulfilling the reporting requirements of the insurer under the Act, the Rules and the *PHIAC 2 Guidance Note*. We disclaim any assumption of responsibility for any reliance on this report, or on the forecasts to which they relate, for any purpose other than that for which it was prepared. We have assumed, and relied on representations from certain members of management of [name of insurer] that all material information concerning the prospects and proposed operations of [name of insurer] has been disclosed to us and that the information provided to us for the purpose of our work is true, complete and accurate in all respects. We have no reason to believe that those representations are false.

[Firm Name]

[Name of Partner]

[Location]

[Date]

Letter of representation

Throughout the Return, there are several areas where the Insurer has exercised its judgement. In these circumstances, the auditor should consider items such as, but are not limited, to:

- assumptions used in forecasts, and
- completeness and accuracy of disclosure of all related party loans.

Section 5 - Appendix A: Standards and Guidance Notes

The **Solvency Standard** and **Capital Adequacy Standard** as an extract of the Rules are located on APRA's website under the reference:

<http://phiac.gov.au/industry/regulatory-framework/>

The **PHIAC 2 Guidance Note** is located on APRA's website under the reference:

<http://phiac.gov.au/industry/return-forms-audit-guidance/>

Section 6 - Appendix B: Abbreviations

ASB 139	AASB 139 Financial Instruments: Recognition and Measurement
AASB 1023	AASB 1023 General Insurance Contracts
the Act	Private Health Insurance Act 2007
APRA	Australian Prudential Regulation Authority
AUASB	Auditing and Assurance Standards Board
AUASB pronouncements	Australian Auditing Standards, Guidance Statements and other pronouncements issued by the AUASB
Corporations Act	Corporations Act 2001
the Fund	the health benefits fund conducted by the Insurer
the Guidance	the Audit Program Guidance for PHIAC 2 Annual Returns
HIB	health insurance business
HRB	health-related business
Insurer	the registered private health insurer under the Act
PHIAC	the Private Health Insurance Administration Council
RETF	Risk Equalisation Trust Fund
the Return	the PHIAC 2 Annual Return
the Rules	the Private Health Insurance (Health Benefits Fund Administration) Rules 2007