

IN THE HIGH COURT OF SOUTH AFRICA
GAUTENG DIVISION, PRETORIA

Case number: 26370/21

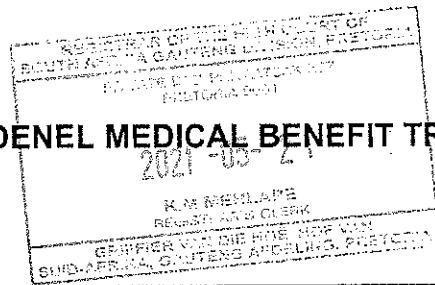
In the *ex parte* application of:

DENEL SOC LIMITED

Applicant

In re:

VARIATION OF THE TRUST DEED OF THE DENEL MEDICAL BENEFIT TRUST



NOTICE OF MOTION

TAKE NOTICE that the Applicant will apply on an *ex parte* basis to this Honourable Court on a date and time arranged with the registrar at 10h00 or as soon thereafter as counsel may be heard (*alternatively* on such other date as may be determined by the Deputy Judge President), for an order in the following terms:

- 1 A rule *nisi* is issued calling on the Trustees of the Denel Medical Benefit Trust (the “**Trustees**”), the “Employee beneficiaries” as defined in the Trust Deed of the Denel Medical Benefit Trust, including dependants of deceased “Employee beneficiaries” who are recognised by the Applicant and the Trustees as continuation and widow(er) members of the Denel Medical Benefit Trust (collectively the “**Employee Beneficiaries**”), and any other

interested parties to show cause on the "**Return Day**") why a final order should not be made in the following terms:

1.1 In terms of section 13 of the Trust Property Control Act 57 of 1988, the Trust Deed of the Denel Medical Benefit Trust is varied in accordance with the amendments contained in the table that is attached to this Notice of Motion as "**A**";

1.2 Directing that any party who opposes the confirmation of the rule *nisi* on the return date must pay the Applicant's costs.

(the "**rule nisi**").

2 The Applicant is granted leave to serve the rule *nisi* and this application on the Trustees, the Employee Beneficiaries and other interested parties by way of substituted service as follows:

2.1 on the Trustees, by emailing a copy of the rule *nisi* and this application (including the founding affidavit, its annexures, and other supporting affidavits) to the email address of the Principal Officer of the Denel Medical Benefit Trust;

2.2 on the Employee beneficiaries:

2.2.1 by email where the Applicant has an email address on record for an Employee beneficiary, which email must contain:

2.2.1.1 the rule *nisi*;

2.2.1.2 this notice of motion;

- 2.2.1.3 an internet link where the rule *nisi*, this notice of motion, the founding affidavit, and the annexures to the founding affidavit can be accessed and downloaded;
- 2.2.1.4 the contact details of Applicant's attorneys of record;
- 2.2.1.5 an invitation to the Employee beneficiary to contact the Applicant's attorneys of record if the Employee beneficiary wants a copy of the rule nisi, this notice of motion, and the founding affidavit and the annexures to the founding affidavit to be made available for collection free of charge; and
- 2.2.1.6 a written offer in respect of each Employee beneficiary that will:
 - 2.2.1.6.1 record the amount of the subsidy that Denel is obliged to provide, as at a date specified in the offer, in respect of that Employee beneficiary;
 - 2.2.1.6.2 describe the benefits and other terms of an individual

annuity policy that will be issued to the Employee beneficiary if the Employee beneficiary accepts the offer of the individual annuity policy; and

2.2.1.6.3 set out all of the other terms and conditions of the offer (the **"Individual Annuity Policy Offer"**);

2.2.2 where Denel has a postal address on record for an Employee beneficiary but no email address by registered mail, which registered mail correspondence must include:

2.2.1.1 the rule *nisi*;

2.2.1.2 this notice of motion;

2.2.1.3 an internet link where the rule nisi, this notice of motion, the founding affidavit, and the annexures to the founding affidavit can be accessed and downloaded;

2.2.1.4 the contact details of the Applicant's attorneys of record;

- 2.2.1.5 an invitation to the Employee beneficiary to contact Denel's attorneys of record if the Employee beneficiary wants a copy of the rule *nisi*, this notice of motion, and the founding affidavit and the annexures to the founding affidavit to be made available for collection free of charge; and
- 2.2.1.6 the Individual Annuity Policy Offer for that Employee beneficiary.

2.3 In addition to paragraphs 2.1 and 2.2, the Applicant will:

- 2.3.1 send the following SMS to each Employee Beneficiary for whom the Applicant has a mobile phone number on record:

"Denel SOC Limited has applied to the High Court of South Africa, Gauteng Division, Pretoria, for an Order amending the trust deed of the Denel Medical Benefits Trust.

The Court has ordered Denel to send this message to you to notify you of the proceedings and its Order. Further documentation is available at an internet link where the rule nisi, the notice of motion, the founding affidavit, and the annexures to the founding affidavit can be accessed and downloaded

or by calling Denel's attorneys of record on 021 410 2500 between the hours of 09:00 to 16:00 on any day other than a Saturday or Sunday or public holiday."

2.3.2 post on the Applicant's website:

2.3.2.1 the rule *nisi*;

2.3.2.2 the notice of motion and the founding affidavit and the annexures to the founding affidavit or an internet link where they can be accessed and downloaded;

2.3.2.4 the contact details of the Applicant's attorneys of record; and

2.3.2.5 an invitation to contact Denel's attorneys of record if an Employee beneficiary or any other interested party wants a copy of the rule nisi, this notice of motion, and the founding affidavit and the annexures to the founding affidavit to be made available for collection free of charge.

2.3.3 cause the following notice to be published in the legal notices section of three consecutive editions of two newspapers with national circulation:

"Denel SOC Limited has applied to the High Court of South Africa, Gauteng Division, Pretoria, for an Order amending the trust deed of the Denel Medical Benefits Trust. Further documentation is available at an internet link where the rule nisi, the notice of motion, the founding affidavit, and the annexures to the founding affidavit can be accessed and downloaded or by calling Denel's attorneys of record on 021 410 2500 between the hours of 09:00 to 16:00 on any day other than a Saturday or Sunday or public holiday."

- 3 The Applicant is granted leave to deliver an affidavit setting out its compliance with paragraph 2 above by no later than five days before the return date.
- 4 Any Trustee, Employee beneficiary or other interested party who wishes to oppose confirmation of the rule *nisi* or otherwise to participate in the hearing on the Return Day, must take the following steps in order to do so:
 - 4.1 Give notice of his or her intention to oppose to the Applicant's attorneys of record within 5 days upon receipt of the *rule nisi* and, in the notice, appoint an address within 15 kilometres of the office of the Registrar of this court at which he or she will accept notice and service of all documents in these proceedings;
and

- 4.2 Deliver an answering affidavit 20 days after delivery of the notice of intention to oppose.
- 5 The Applicant is granted leave to deliver its replying affidavits no later than 15 days after receipt of the aforementioned answering affidavits.
- 6 Granting further and/or alternative relief.

TAKE NOTICE FURTHER THAT the affidavit of **KHOHLONG WILLIAM HLAKOANE** annexed hereto will be used in support thereof.

TAKE NOTICE FURTHER THAT the Applicant consents to the service of all notices, affidavits, and other pleadings by email at tmodubu@ensafrica.com and smatebese@ensafrica.com.

KINDLY PLACE THE MATTER ON THE ROLL FOR HEARING ACCORDINGLY.

Dated at **JOHANNESBURG** on this the 21st day of **MAY 2021**.


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c/o **MACINTOSH CROSS**

FARQUHARSON

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**TO: THE REGISTRAR OF THE ABOVE
HONOURABLE COURT PRETORIA**

ANNEX 'A'

<p>Trust Deed Amendments</p>	
<p>Deletions.</p>	<p>Clause 7.3 and Clause 11.2.2 of the Trust deed are deleted without any consequential changes in the clause numbering.</p>
<p>Clause 3.1. The addition of the following new definitions:</p>	<p><i>3.12 "Expense Fund"</i></p> <p><i>Assets of the Trust that are earmarked by the Trustees to meet the expenses of the Trust after the Scheme Implementation Date.</i></p> <p><i>3.13 "Group Annuity Policy"</i></p> <p><i>The Group Annuity Policy to be acquired and held by the Trust.</i></p> <p><i>3.14.1 Subject to clause 3.14.2, each of the following:</i></p> <p><i>3.14.1.1 The insurer will be an insurer that is identified by the Trustees and approved in writing by Denel, provided that Denel's approval of the insurer will not be required if the insurer is one of Old Mutual Life Assurance Company (South Africa) Limited, Momentum Metropolitan Life Limited and Sanlam Life Insurance Limited.</i></p> <p><i>3.14.1.2 The benefits under the policy will be paid in respect of all of the Employee beneficiaries (including</i></p>

Recognised Dependants) that are named in the policy.

3.14.1.3 The benefits under the policy will be an annuity equal to 120% of the benefits that are required to be paid in terms of Denel's current subsidy policy on the basis that all beneficiaries are on the Discovery Health Essential Comprehensive option even if they do not belong to the Discovery Health Medical Scheme or have not opted for the Essential Comprehensive option (determined on the basis of the cost, as at the date of the issue of the policy or such earlier date that Denel may specify).

3.14.1.4 The annuity will increase in January every year by CPI + 4% using the CPI published in respect of October in the preceding year, subject to a minimum inflation rate of 0%. In the event of deflation, the increase will be 4%, but the cumulative increases since date of the issue of the policy will not exceed CPI + 4% p.a. This means that the insurer will "clawback" the impact of setting inflation at a minimum of 0% where there has been deflation.

3.14.1.5 The annuity and the annual increases are to be guaranteed by the insurer.

3.14.1.6 The policy must confer on the policyholder (the Trust or, pursuant to a transfer of these rights by

the Trust, Denel) a right to surrender the entire policy or part of the policy insofar as it relates to an Employee beneficiary.

3.14.1.7 The rights of the policyholder under the policy in respect of each Employee beneficiary will be capable of transfer by the Trust to Denel in one or more transfers from time to time, without any requirement that the insurer consents or agrees to that transfer.

3.14.1.8 The policy will provide for an individual annuity policy to be issued to the relevant Employee beneficiary if this is required by the policyholder (the Trust or, pursuant to a transfer of these rights by the Trust, Denel). The individual annuity policy will not include a right to surrender the individual annuity policy.

3.14.1.9 No subsequent marriage or remarriage will be provided for. Except for disabled children, the children's subsidy will cease at an age of 25 years.

3.14.1.10 The policy terms, including the amount and manner of discharge of the policy premium and the terms that will apply to any individual annuity policies that are issued, must be approved by Denel in writing prior to the Trust concluding the policy.

3.14.2 Despite any provision of clause 3.14.1:

3.14.2.1 Denel and the Trustees may agree in writing to any variation of or departure from any of the criteria in clause 3.14.1; and

3.14.2.2 once Denel gives the approval that is contemplated in clause 3.14.1.10, the policy that is acquired by the Trustees shall be deemed to comply with all of the criteria in clause 3.14.1.

3.15 "Group Annuity Policy Acquisition Date"

A date specified by Denel and notified to the Trustees as the date by which the Trust must have acquired the Group Annuity Policy and discharged the obligation to pay the premium to the insurer under the Group Annuity Policy. The date specified by Denel shall not be less than 10 calendar days from the date of Denel's notice to the Trustees and shall not be less than 30 calendar days after the amendment to the Trust deed to include this clause 3.15 takes effect. The date so specified may be extended from time to time by Denel by notice to the Trustees.

3.16 "Recognised Dependant"

In relation to a deceased Employee beneficiary, a dependant of that Employee beneficiary who is recognised by the Trust and Denel as a continuation and widow(er) member of the Trust.

3.17 "Scheme Active Participant"

An Employee beneficiary in the active employ of Denel or one of its subsidiaries who at any time has concluded an agreement with Denel (that has not been terminated) to be a Scheme Active Participant under the Trust deed..

3.1518 "Scheme Implementation Date"

A date specified by Denel and notified to the Trustees as the Scheme Implementation Date under clause 7.8 of the Trust deed. The date specified by Denel shall not be less than 5 calendar days after the Group Annuity Policy Acquisition Date. The date so specified may be extended from time to time by Denel by notice to the Trustees.

3.19 "Scheme Non-Participants"

An Employee beneficiary (including for the avoidance of doubt a Recognised Dependant) who at any relevant time is neither a Scheme Pensioner Participant nor a Scheme Active Participant.

3.20 "Scheme Pensioner Participant"

A retired Employee beneficiary (including for the avoidance of doubt a Recognised Dependant) who at any time has concluded an agreement with Denel (that has not been terminated) to be a Scheme Pensioner Participant under the Trust deed.

	<p><i>3.21 "Trust Excess Assets"</i></p> <p><i>At the relevant time, all of the assets of the Trust as at that time, including any income earned by the Trust on such assets, other than (i) the Group Annuity Policy (ii) sufficient cash or securities designated by the Trustees as being required to restore the balance of the Expense Fund to R20 million or such other amount as may be agreed in writing between Denel and the Trust and (iii) sufficient cash or securities designated by the Trustees acting on the advice of an actuary appointed by the Trust as being required to fund any liabilities of the Trust as at the relevant date other than any liabilities or obligations that are funded or insured under the Group Annuity Policy or to be discharged from the Expense Fund. For this purpose, the Group Annuity Policy will be regarded as fully funding any obligations of the Trust in respect of Scheme Active Participants and Scheme Non-Participants.</i></p>
<p>Clause 5. The addition of the following further paragraphs after the current paragraph:</p>	<p><i>The further main objectives of the Trust are:</i></p> <p><i>(i) to hold, as an asset of the Trust, a group annuity policy to give effect to the original main objective of the Trust (as set out in the first paragraph of clause 5 of the Trust deed) in respect of all of the Employee beneficiaries (including for the avoidance of doubt Recognised Dependents);</i></p>

	<p><i>(ii) to ensure the issue of an individual annuity policy to Employee beneficiaries (including for the avoidance of doubt Recognised Dependants) who choose to receive such a policy and, in so doing, to assist these Employee beneficiaries with post-retirement contributions payable to the Medical Scheme on the basis that once such an individual annuity policy has been issued, the individual annuitant will no longer be an Employee beneficiary of the Trust;</i></p> <p><i>(iii) to hold all of the excess assets of the Trust (other than the group annuity policy and an appropriate allowance for expenses) for the sole benefit of Denel and to distribute the excess assets to Denel.</i></p>
<p>Clause 7. The addition of the following new sub-clauses.</p>	<p><i>7.7 Despite any other provisions in this Trust deed, the Trustees shall have all of the powers required to give effect to the remaining provisions of this clause 7.</i></p> <p><i>7.8 The Trustees shall exercise these powers to give effect to the main objectives of the Trust. This shall include (but not be limited to):</i></p> <p style="padding-left: 40px;"><i>7.8.1 the Trustees shall ensure that they acquire the Group Annuity Policy and discharge the obligation to pay the premium to the insurer prior to the Group Annuity Policy Acquisition Date and that:</i></p> <p style="padding-left: 80px;"><i>7.8.1.1 the benefits and other terms of the</i></p>

	<p><i>Group Annuity Policy are consistent with the Group Annuity Policy Criteria, the main objectives of the Trust and the other provisions of this Trust deed; and</i></p> <p><i>7.8.1.2 the process to select the insurer under the Group Annuity Policy and to determine the amount of the premium payable by the Trust under the Group Annuity Policy is, as between the participants in the process, consistent with the principles of fairness, equitability, transparency, competitiveness and cost-effectiveness;</i></p> <p><i>7.8.2 in respect of each Scheme Pensioner Participant, the Trustees shall vest in Denel, on the Scheme Implementation Date, the rights under the Group Annuity Policy in respect of each Scheme Pensioner Participant and shall transfer those rights, by cession, to Denel with effect from the Scheme Implementation Date;</i></p> <p><i>7.8.3 in respect of each Scheme Active Participant, the Trustees shall vest in Denel, on the date on which a Scheme Active Participant retires or on any other date agreed to by Denel and the Scheme Active Participant and notified to the Trustees, the rights under the Group</i></p>
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	<p><i>Annuity Policy in respect of the Scheme Active Participant and shall transfer those rights, by cession, to Denel with effect from that date, provided that if Denel and the Scheme Active Participant agree that Denel will no longer have an obligation to pay or subsidise any medical aid costs in respect of the Scheme Active Participant, the Trustees will, if Denel requires this of the Trustees, surrender the Group Annuity Policy in respect of that Scheme Active Participant and vest in and distribute the surrender proceeds to Denel;</i></p> <p><i>7.8.4 in respect of any Scheme Non-Participant with whom Denel agrees after the Scheme Implementation Date that Denel will no longer have an obligation to pay or subsidise any medical aid costs in respect of the Scheme Non-Participant, the Trustees shall either, as Denel may require of the Trustees:</i></p> <p><i>7.8.4.1 surrender the Group Annuity Policy in respect of that Scheme Non-Participant and vest in and distribute the surrender proceeds to Denel; or</i></p> <p><i>7.8.4.2 vest in Denel, on a date specified by Denel, the rights under the Group Annuity</i></p>
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	<p><i>Policy in respect of that Scheme Non-Participant and shall transfer those rights, by cession, to Denel with effect from that date;</i></p> <p><i>7.8.5 identifying, prior to the Scheme Implementation Date, the Trust Excess Assets as at the Scheme Implementation Date; and</i></p> <p><i>7.8.6 on and from the Scheme Implementation Date holding the Trust Excess Assets for the sole benefit of Denel and, as may be required by Denel from time to time:</i></p> <p><i>7.8.6.1 liquidating all or any of the Trust Excess Assets in consultation with Denel; and</i></p> <p><i>7.8.6.2 applying the Trust Excess Assets for a purpose designated by Denel; or</i></p> <p><i>7.8.6.3 vesting in, and distributing to Denel, as a beneficiary of the Trust, all or any of the Trust Excess Assets on and with effect from the Scheme Implementation Date, provided that Denel may designate any one or more dates after the Scheme Implementation Date as the date on which any such vesting or distribution is to occur or take effect.</i></p> <p><i>7.9 The Trustees shall, in respect of all Employee beneficiaries of the Trust (including for the avoidance of doubt Recognised Dependants) that are Scheme</i></p>
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	<p><i>7.10.3 in addition to the obligations of the Trustees in clause 7.10.1 and clause 7.10.2, the Trustees shall have a discretion, acting on the advice of an actuary appointed by the Trust, to vest in and distribute to Denel all or any of the further Trust Excess Assets as at each financial year end of the Trust.</i></p> <p><i>7.11 On the winding up of the Trust following its termination, all of the assets remaining after discharging the Trust's liabilities and the expenses incurred in the winding-up of the Trust, including any balance in the Expense Fund, shall be paid to Denel.</i></p>
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IN THE HIGH COURT OF SOUTH AFRICA
(GAUTENG DIVISION, PRETORIA)

Case no.:

In the *ex parte* application of:

DENEL SOC LIMITED

Applicant

In re:

VARIATION OF THE TRUST DEED OF THE DENEL MEDICAL BENEFIT TRUST

FOUNDING AFFIDAVIT

J.C.W.
AT

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INTRODUCTION

I the undersigned

KHOHLONG WILLIAM HLAKOANE

do hereby make oath and say as follows:

- 1 I am the Interim Group Chief Executive Officer of the Applicant, Denel SOC Limited (“Denel”).
- 2 I am duly authorised to institute these proceedings and to depose to this founding affidavit on behalf of Denel.
- 3 The facts contained in this affidavit are both true and correct and, unless the context indicates otherwise, fall within my knowledge or are apparent from the documents under my control.
- 4 Some of the facts that I depose to for the sake of convenience are confirmed by Hendrick Potgieter, Paul Botha and Antony Lester whose supporting affidavits will accompany this affidavit.
- 5 Where I provide financial information or membership data, I do so with reference to the information or data as at 1 April 2021. This is the most recent date as at which the post-employment health care liabilities of Denel have been actuarially valued.

K.W.
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THE APPLICANT

- 6 The applicant is **DENEL SOC LIMITED**, a state-owned company incorporated under the laws of the Republic of South Africa, with its registered office at Nellmapius Drive, Irene, Gauteng, 0062.
- 7 Denel is the largest manufacturer of defence equipment in South Africa and operates in the military aerospace and landward defence environment.

OVERVIEW OF THIS APPLICATION

The problem that has given rise to this application

- 8 This application relates to the Denel Medical Benefit Trust (the "**Trust**"). I attach a copy of the Trust Deed as "**FA1**" (the "**Trust Deed**").
- 9 The Trust was established in 2002 for the purpose of enabling Denel to pay medical aid subsidy contributions on behalf of former employees who had taken up employment before 1 April 2000. Denel is contractually obliged to pay post-retirement medical aid subsidy contributions to those former employees and their dependants as specified in the former employees' contracts of employment with Denel. The Trust was established as a vehicle that discharges Denel's obligation to pay medical aid contributions on behalf of those former employees.
- 10 There are 626 retired employees of Denel or their surviving spouses and certain surviving dependent children who already qualify for benefits from Denel through the Trust. I shall refer to them as "continuation members". In addition, there are 32 people who were employed by Denel before 1 April 2000, who are still working for Denel, and who will qualify for benefits from Denel through the Trust when they retire from Denel in due course. I shall refer to them as "in-service members".

- 11 It follows that, in total, there are 657 persons to whom the Trust is already making payment, or will make payment in future, for medical scheme contributions. That number will decrease with the passage of time and will eventually dwindle to zero.
- 12 The Trust's assets significantly exceed the actuarial value of Denel's liabilities to pay medical aid subsidy contributions for former employees. In other words, the Trust's assets far exceed what the Trust is likely to require in order to pay medical scheme contributions for beneficiaries over their lifetimes. The Trust's excess assets are likely to become even larger with the passage of time.
- 13 The problem is that, as things stand, the Trust Deed does not permit the distribution of the excess assets to Denel or to the Trust's beneficiaries. Further, the Trust Deed does not permit the Trust to provide beneficiaries with benefits in excess of Denel's post-retirement medical aid obligation. Indeed the Trust Deed makes no provision for what should happen to the excess assets once it becomes apparent either that the assets of the Trust exceed the assets that are required by the Trust's object or that there are no former employees or dependants of former employees who can receive benefits from the Trust.

How Denel proposes to address the problem

- 14 The purpose of the present application is to address the problem described above. Denel proposes to do so by seeking the leave of this Court to amend the Trust Deed in terms of section 13 of the Trust Property Control Act 57 of 1988 (the "Act").
- 15 In broad terms, the proposed amendments are intended to achieve two objectives:
 - 15.1 First, the amendments will make it possible to issue a group annuity to the Trust and individual annuity policies to beneficiaries who elect to receive such a policy.

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15.2 Second, the amendments will authorise the Trustees to distribute the Trust's excess assets to Denel as capital distributions.

16 I elaborate on each of these objectives in turn.

17 As regards the group annuity policy and the individual annuity policies:

17.1 Denel proposes that the Trustees on behalf of the Trust will purchase a group life annuity policy from an appropriate insurer before any distribution of the excess assets is made to Denel. The group policy will insure Denel's post-retirement medical aid obligations to its former employees and will, accordingly, fund the benefits to the Employee beneficiaries under the Trust. The Trust will use the annuity it receives under the group policy to fund Denel's required contribution to each Employee beneficiary. In this way, the group annuity policy will fund the medical scheme contributions of all the Trust's beneficiaries for the rest of their lives.

17.2 Once the group life annuity policy is in place, the Trust's excess assets will not be required to meet Denel's liability in respect of post-retirement medical scheme contributions. The excess assets will not be needed because the Employee beneficiaries' post-retirement medical aid contributions will then be funded by annuity payments under the group life annuity policy held by the Trust. After purchasing the group life annuity policy, the Trust will continue to hold excess assets of approximately R800,000,000.00 (eight hundred million Rand).

17.3 Denel intends to make an offer to all the beneficiaries of the Trust to become annuitants under individual life annuity policies that will fund their medical aid contributions until they die. Each individual policy would then fund that

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beneficiary's medical aid contributions. If they were to accept this offer, the beneficiaries of the Trust would effectively move from the Trust's group life policy to their own individual life policies, which will be delivered through a part surrender of the group life annuity policy. The beneficiaries who do not choose the individual life annuity policies will continue to receive their benefits as before from the Trust. Those benefits will have been insured by the Trust under the group life annuity policy. The benefits under the group life annuity policy will be greater than the subsidy that will continue to be provided to the beneficiaries who do not choose the individual life annuity policies.

17.4 In its present form, the Trust Deed does not provide for the issuing of the group annuity policy or the individual annuity policies. The Trust Deed would therefore have to be varied in order for this to occur.

18 As regards the distribution of the Trust's excess assets:

18.1 Once the group annuity policy and the individual annuity policies have been issued, the financial commitments of the Trust will be locked-in. This will leave substantial excess assets in the Trust that will no longer be needed to achieve the objectives of the Trust, as those objectives are currently formulated in clause 5 of the Trust Deed.

18.2 The founder of the Trust (the "**Founder**") never contemplated the Trust amassing such substantial excess assets. As presently formulated, the sole purpose of the Trust is to fund Denel's obligation to contribute to the post-retirement medical aid premiums of its former employees. However, the Trust's excess assets will not be required for this purpose.

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18.3 It would make no sense for the excess assets—which currently amount to approximately R800,000,000.00 (eight hundred million Rand)—to be sterilised and to remain in the Trust indefinitely.

18.4 Denel accordingly proposes that the Trust Deed be varied so as to permit the excess assets to be distributed to it. As I shall explain below, this would not prejudice the beneficiaries of the Trust.

The two stages of this application

19 The application is brought in two stages:

19.1 In the first stage, Denel applies on an *ex parte* basis for:

19.1.1 a rule *nisi* calling on interested parties to show cause on the return day why the Trust Deed should not be varied as outlined in paragraph 15 above; and

19.1.2 an order granting Denel leave to serve the rule *nisi*, the notice of motion, and this founding affidavit (and annexures) on the Trustees and the beneficiaries of the Trust by substituted service in the manner outlined in paragraph 2 of the notice of motion.

19.2 The second stage will occur on the return day, when Denel will ask that the rule *nisi* be made final and that the proposed amendments to the Trust Deed effected in terms of section 13 of the Act. The Trustees, the beneficiaries of the Trust, and any other interested parties will have a full opportunity on the return day to oppose the relief if they were to be minded to do so.

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- 20 This affidavit serves as Denel's founding affidavit for both stages of this application. However, it will be unnecessary for this Court to fully engage with the merits of the proposed amendments at the first stage. That will be done at the second stage (i.e. on the return date of the rule *nisi*).
- 21 The Trustees have been made aware of this application and the fact that it will be brought in two stages. I attach as "FA2.1" to "FA2.5" a bundle of correspondence that has been addressed to the Trustees by Denel. The Trustees will not suffer any prejudice by virtue of the fact that they are not cited as respondents in the first stage. That is because the rule *nisi* will not have any interim effect and the Trustees will have a full opportunity to participate in the court hearing on the return day. As I shall explain below, this procedure has been adopted in order to expedite the matter and because of the practical difficulties involved in serving the founding papers on 657 members.

The structure of this affidavit

- 22 The remainder of my affidavit will be structured as follows:
- 22.1 I begin by explaining why this Court is vested with jurisdiction.
- 22.2 I summarise the facts that have given rise to this application.
- 22.3 I describe the problem that has arisen regarding excess assets in the Trust and Denel's proposed solution to the problem.
- 22.4 I deal with the requirements in section 13 of the Act and explain why those requirements are satisfied in the present circumstances.

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JURISDICTION

- 23 Denel's head office is located within the jurisdiction of this Court at Nellmapius Drive, Irene, Gauteng, 0062.
- 24 The Trust has its office located with the jurisdiction of this Court at Denel Building, Jochemus Street, Erasmuskloof, Pretoria.
- 25 Many of the Employee beneficiaries of the Trust are resident within the jurisdiction of this Court.
- 26 Accordingly, I submit that this Court has jurisdiction to determine the matter.

PROCEDURAL ISSUES

The ex parte application

- 27 As explained above, this application is brought in two stages. At the first stage, Denel applies on an *ex parte* basis for a rule *nisi* calling on interested parties to show cause on the return day why the Trust Deed should not be varied. The order will also regulate how interested parties should be informed of this application and how they should go about participating on the return day.
- 28 There are currently 657 beneficiaries of the Trust. They are made up of:
- 28.1 the 32 "in-service members" who were employed by Denel before 1 April 2000, who are still working for Denel, and who will qualify for benefits from the Trust when they retire from Denel; and

- 28.2 the 625 “continuation members” that I referred to above. I explain below that Denel and the Trust regard these so-called “continuation members” as the “Employee beneficiaries” within the meaning of the Trust Deed.
- 29 Denel accepts that these 657 people have an interest in the confirmation of the rule *nisi*.
- 30 However, it would not be practically feasible to serve this application on all 657 people in the manner required by Uniform Rule 4:
- 30.1 Serving this application on so many respondents in the ordinary way would be prohibitively expensive and would take an unreasonable amount of time.
- 30.2 The Employee beneficiaries are also disparately located throughout the country.
- 30.3 Service in the ordinary way would require complex coordination with various sheriff offices, adding to the expense and time of service in the ordinary manner. This is especially so given the unavoidable length of this affidavit and its annexures.
- 31 Denel accordingly seeks leave to serve the rule *nisi*, the notice of motion, and this affidavit (and annexures) through a combination of email, registered mail, SMS messages and publication on Denel’s website.
- 32 Denel proposes that service should take place in the following manner:
- 32.1 on the Trustees, by emailing a copy of the rule *nisi* and this application (including the founding affidavit, its annexures, and other supporting affidavits) to the email address of the Principal Officer of the Denel Medical Benefit Trust;

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32.2 on the Employee beneficiaries:

32.2.1 by email where Denel has an email address on record for an Employee beneficiary, which email must contain:

32.2.1.1 the rule *nisi*;

32.2.1.2 notice of motion;

32.2.1.3 an internet link where the rule *nisi*, the notice of motion, the founding affidavit, and the annexures to the founding affidavit can be accessed and downloaded;

32.2.1.4 the contact details of Denel's attorneys of record;

32.2.1.5 an invitation to the Employee beneficiary to contact the Applicant's attorneys of record if the Employee beneficiary wants a copy of the rule *nisi*, the notice of motion, and the founding affidavit and the annexures to the founding affidavit to be made available for collection free of charge; and

32.2.1.6 a written offer in respect of each Employee beneficiary that will:

32.2.1.6.1 record the amount of the subsidy that Denel is obliged to provide, as at a date specified in the offer, in respect of that Employee beneficiary;

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32.2.1.6.2 describe the benefits and other terms of an individual annuity policy that will be issued to the Employee beneficiary if the Employee beneficiary accepts the offer of the individual annuity policy; and

32.2.1.6.3 set out all of the other terms and conditions of the offer (the “**Individual Annuity Policy Offer**”);

32.2.2 where Denel has a postal address on record for an Employee beneficiary but no email address by registered mail, which registered mail correspondence must include:

32.2.2.1 the rule *nisi*;

32.2.2.2 the notice of motion;

32.2.2.3 an internet link where the rule *nisi*, the notice of motion, the founding affidavit, and the annexures to the founding affidavit can be accessed and downloaded;

32.2.2.4 the contact details of Denel’s attorneys of record;

32.2.2.5 an invitation to the Employee beneficiary to contact Denel’s attorneys of record if the Employee beneficiary wants a copy of the rule *nisi*, the notice of motion, and the founding affidavit and the annexures to the founding affidavit to be made available for collection free of charge; and

32.2.2.6 the Individual Annuity Policy Offer for that Employee beneficiary.

32.2.3 In addition to service by email and registered mail stated in 32.1 and 32.2, Denel will:

32.2.3.1 send the following SMS to each Employee beneficiary for whom Denel has a mobile phone number on record:

“Denel SOC Limited has applied to the High Court of South Africa, Gauteng Division, Pretoria, for an Order amending the trust deed of the Denel Medical Benefits Trust.

The Court has ordered Denel to send this message to you to notify you of the proceedings and its Order. Further documentation is available at an internet link where the rule nisi, the notice of motion, the founding affidavit, and the annexures to the founding affidavit can be accessed and downloaded or by calling Denel’s attorneys of record on 021 410 2500 between the hours of 09:00 to 16:00 on any day other than a Saturday or Sunday or public holiday.”

32.2.3.2 post on Denel’s website:

32.2.3.2.1 the rule nisi;

32.2.3.2.2 the notice of motion and the founding affidavit and the annexures to the founding

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affidavit or an internet link where they can be accessed and downloaded;

32.2.3.2.3 the contact details of Denel's attorneys of record; and

32.2.3.2.4 an invitation to contact Denel's attorneys of record if an Employee beneficiary or any other interested party wants a copy of the rule *nisi*, the notice of motion, and the founding affidavit and the annexures to the founding affidavit to be made available for collection free of charge.

32.2.3.3 cause the following notice to be published in the legal notices section of three consecutive editions of two newspapers with national circulation:

"Denel SOC Limited has applied to the High Court of South Africa, Gauteng Division, Pretoria, for an Order amending the trust deed of the Denel Medical Benefits Trust. Further documentation is available at an internet link where the rule nisi, the notice of motion, the founding affidavit, and the annexures to the founding affidavit can be accessed and downloaded or by calling Denel's attorneys of record on 021 410 2500 between the hours of 09:00 to 16:00 on any day other than a Saturday or Sunday or public holiday."

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- 33 With regard to the telephone number and website post:
- 33.1 Denel will appoint an employee who will telephone the Employee beneficiaries for whom Denel has a telephone number on record to confirm receipt of the rule *nisi*, notice of motion, founding affidavit and annexures.
- 33.2 In addition, Denel will set up a dedicated call centre that Employee beneficiaries can contact on a toll-free number to obtain more information about this application and where to access the relevant documents.
- 33.3 Denel will also prepare and place on its website, a link to where a summary of potential questions and answers about this application and where to access the relevant documents.
- 34 I am informed that a similar form of substituted service has been adopted in circumstances where approval has been sought of settlements of a class actions. The use of this kind of substituted service has, accordingly, been approved by this Court.
- 35 As I have mentioned above, the Trustees will be served with a full copy of the founding papers and the rule *nisi*. I understand that it is unusual for the Trustees not to be heard at the first stage, but the Trustees have been made aware of this application and the fact that it will be brought in two stages:
- 35.1 I have already attached as "FA2.1" to "FA2.5" a bundle of correspondence that has been addressed to the Trustees by Denel. .
- 35.2 As stated earlier, the Trustees will not suffer any prejudice by virtue of the fact that they are not cited as respondents in the first stage. That is because the rule *nisi* will not have any interim effect and the Trustees will have a full opportunity to participate on the return day.

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The return day

36 On the return day, Denel will move for an amendment to the Trust Deed on the basis described in the schedule to the notice of motion. All interested parties, including the Trustees and the Employee beneficiaries, will have an opportunity to oppose that relief if they were to be minded to do so.

37 With this in mind, the indicative timetable that Denel proposes for the further conduct of this matter is as follows:

37.1 The rule *nisi* will be communicated to Employee beneficiaries within 7 days of its granting.

37.2 Any Trustee, Employee Beneficiary or other interested party who wishes to oppose confirmation of the rule *nisi* or otherwise to participate in the hearing on the Return Day, must take the following steps in order to do so:

37.2.1 Give notice of his or her intention to oppose to the Applicant's attorneys of record within 5 days upon receipt of the rule *nisi* and, in the notice, appoint an address within 15 kilometres of the office of the Registrar of this court at which he or she will accept notice and service of all documents in these proceedings; and

37.2.2 Deliver an answering affidavit 20 days after delivery of the notice of intention to oppose.

37.3 Denel, will file its replying affidavits 15 days upon receipt of the aforementioned answering affidavits.

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37.4 Denel will file an affidavit setting out its compliance with paragraph 32 above which affidavit will be filed at least five days before the return date.

Urgency

38 I am advised that because the application for a rule *nisi* is *ex parte*, it will be set down on this Court's unopposed roll (or on an expedited date to be arranged with the Deputy Judge President). Since it will not be set down on the urgent roll, it is unnecessary for Denel to make out a case for urgency.

39 Nonetheless, I submit that it would be in the interests of justice for this application to be heard on an expedited basis (that is, both the application for a rule *nisi* and the return date). I elaborate on the reasons for this below.

40 If Denel is to obtain access to the Trust's excess assets, then it is in the best interests of Denel and its employees that this application be determined as expeditiously as possible. Given Denel's role as a state-owned entity, the short term strain under which it is currently operating has knock-on systemic effects on other industries and the economy as a whole. Being able to access the Trust's excess assets would go some way towards assisting Denel's financial position in the short term.

41 Denel is working closely with the shareholder to restructure the organisation to profitability but short term funding is important to assist Denel with execution of operations, payment of suppliers and employee obligations and the protection of capabilities considered of strategic and sovereign importance for national security.

42 The National Defence Industry Council has identified the financial liquidity challenges Denel is facing as having the potential impact of:

42.1 compromising South Africa's national security;

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- 42.2 collapsing the entire defence industry irretrievably;
- 42.3 exposing South Africa to a mass exodus of skilled personnel in sensitive defence domains to countries that are not necessarily aligned to South Africa's national interests; and
- 42.4 loss of critical defence capabilities, including sovereign and strategic capabilities.
- 43 Denel appreciates that it has no entitlement to the Trust's excess assets unless this application were to succeed. Given Denel's straitened financial position—and, in particular, its need for liquidity—it is in the interests of justice for a determination to be made on Denel's entitlement to the excess assets on an expedited basis.
- 44 Were this application to wait for a hearing in the ordinary course (that is, a hearing in the ordinary course for either the rule *nisi* or its return date), Denel would likely suffer irreparable harm, with systemic knock-on effects across the industry and on the economy as a whole.
- 45 The relief sought in this application will also improve the financial position of the Employee Beneficiaries. For this reason as well, I respectfully submit that it should be determined on an expedited basis.

Statutory approval

- 46 Under section 54(2)(f) of the Public Finance Management Act 1 of 1999 (the "**PFMA**"), before Denel concludes "*a significant change in the nature or extent of its interest in a significant ... trust*", it must notify National Treasury and obtain the approval of the Department of Public Enterprises (the "**Department**").

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47 Denel accepts that section 54(2)(f) of the PFMA applies to the proposed arrangements regarding the Trust outlined in this affidavit. As such, Denel is in the process of notifying National Treasury and seeking the Department's approval. Denel will update this Court in due course on its progress in these regards.

THE FACTUAL BACKGROUND

48 I now turn to describe the events that have given rise to this application and the need to vary the Trust Deed. What is set out below is primarily relevant to the second stage of this application.

The incorporation of Denel

49 Denel was incorporated as a company on 1 April 1992 in terms of the Companies Act 62 of 1973. It was formed out of the industrial part of the Armaments Corporation of South Africa ("**ARMSCOR**").

50 Prior to 1 April 1992, ARMSCOR together with its subsidiaries performed all of its manufacturing, development and procurement functions itself. However, following the formation of Denel, the procurement function was kept separate. Parliament approved the split of the manufacturing and development part from the acquisition function and ARMSCOR retained only the procurement function.

The establishment of the Medical Benefit Fund

51 During 1992, Denel undertook a due diligence exercise. Hendrick Potgieter ("**Mr Potgieter**") was in charge of the financial work stream as part of this process and he confirms what is stated in the paragraphs below.

52 One of the issues that arose during the due diligence was the risk of the future funding of employee and pensioners' medical aid. Various options were investigated, discussions were held with SARS, and Coopers Du Toit (now part of PwC) worked on the tax issues. The final recommendation was that the money should be put into the vehicle that ultimately became the Denel Medical Benefit Fund ("**Medical Benefit Fund**").

53 I attach as "**FA3**" the Reglement of the Medical Benefit Fund.

54 Denel historically operated an in-house medical scheme called UMED. As clause 5 of the Reglement explains, the purpose of the Medical Benefit Fund was to provide financial assistance to employees and former employees who were members of UMED, in circumstances where UMED did not fully cover their medical expenses.

55 In essence, UMED would regularly claim from the Medical Benefit Fund the difference between the claims that members would make on UMED for their medical expenses and the contributions that members would make to UMED. After making an initial lump sum contribution to the Medical Benefit Fund, Denel continued to fund the Medical Benefit Fund at the rate of 25% of two thirds of the active member's medical contributions.

56 Mr Potgieter confirms that at the time when Medical Benefit Fund was established, there were no discussions as to what would happen should there be excess assets in the Medical Benefit Fund. The Medical Benefit Fund was substantially under-funded and it was not anticipated that the Medical Benefit Fund would ever have substantial excess assets.

The establishment of the Trust

57 Before 31 December 1999, the Medical Benefit Fund was exempt from paying income tax. However, the Medical Benefit Fund lost its tax-exempt status on 1 January 2000

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due to changes to the tax legislation. This prompted Denel to consider an alternative structure.

58 By this time, it had become clear to Denel that it would be impossible for it to continue providing post-retirement medical aid contributions to new employees. A proposal was made to change the service conditions so that new employees of Denel would not qualify for post-retirement medical benefit subsidies.

59 I attach as "FA4" a memorandum prepared for a meeting of the Denel Personnel and Remuneration Committee held on 16 February 2000:

59.1 The memorandum highlights the very substantial deficit that had arisen between the assets in the Medical Benefit Fund and Denel's post-retirement healthcare liability. It also highlights that this liability was expected to increase and it summarises the various options open to Denel in relation to the funding of its healthcare liability.

59.2 As foreshadowed in paragraph 6.1.2 of the memorandum, the conditions of employment were in due course changed so that with effect from 1 April 2000 new employees of Denel would no longer qualify for post-retirement medical aid benefits.

60 What this means is that employees of Denel who were employed before 1 April 2000 are contractually entitled to receive subsidies in respect of their medical scheme contributions after they retire. This benefit was a condition of service when Denel was formed in 1992. However, employees of Denel who were employed after 1 April 2000 have no such contractual entitlement to post-retirement medical aid subsidies. This has the effect of fixing the maximum number of employees who are owed the post-retirement medical aid obligation. This in turn ensures that over time the liability of Denel reduces

as its employees and their dependants reduce in number, whether by resignation, retrenchment, death, early retirement or being bought out of the liability.

61 In addition, the memorandum contemplates that some of the surplus in the Denel Pension Fund (a defined benefit pension fund) would be used to compensate the members of the Medical Benefit Fund who were also members of the Denel Pension Fund for a reduction in Denel's contribution to their medical expenses.

62 I pause to observe that the post-retirement medical aid subsidy that existed at the time, was that the employer's liability would be for a set percentage of the monthly contribution to UMED, which was the in-house medical scheme of Denel. In 2010, UMED amalgamated with Discovery Health Medical Scheme. The subsidy now takes the form of a set percentage of the monthly contribution to a maximum of the Essential Comprehensive benefit option that is offered by the Discovery Health Medical Scheme.

63 Approval for the new strategy was obtained in or around April 2000.

64 Thereafter, Denel obtained an actuarial valuation of its healthcare liability as at 1 August 2000. That valuation was reported on to Denel's "EXCOM MEMBERS" in a memorandum dated 19 February 2001, which I attach as "FA5". That memorandum highlighted that Denel had, through its new strategy, reduced its healthcare liability but that even with the new strategy, the Medical Benefit Fund was required to fund UMED at a level that could not be afforded by the Medical Benefit Fund. Denel was, accordingly, considering various ways to manage the deficit, including reducing the subsidy level, making an *ex gratia* contribution to the Medical Benefit Fund or reducing the tax burden of the Medical Benefit Fund.

65 The actuarial valuation as at 1 August 2000 was done on the basis that Denel had changed its liabilities in respect of medical costs of retirees so that:

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- 65.1 Denel would no longer meet the difference between the member's total medical costs and the contributions paid by members;
- 65.2 Denel's liability in respect of each member would be limited to 2/3rds of that member's medical aid costs;
- 65.3 Members of the Denel Pension Fund would receive 85% of their medical aid costs from the Denel Pension Fund and Denel's liability would be limited to 15% of the future medical aid contributions.
- 66 The Trust was founded in October 2002 in order to enable Denel to discharge its post-retirement medical aid funding obligation towards employees who had commenced employment prior to 1 April 2000.
- 67 In essence, the assets of the Medical Benefit Fund were transferred to the Trust. That is why the Trust Deed describes the Medical Benefit Fund as being the Founder of the Trust. In simple terms, the Trust replaced the Medical Benefit Fund as the vehicle through which Denel's post-retirement medical aid obligation was to be funded.
- 68 Denel obtained a valuation of its liability for medical scheme costs as at 1 April 2003, by which time the Trust had been established. That valuation is attached as "FA6". It shows the values of the assets and liabilities as at 1 April 2002 and 1 April 2003. The following is the summary of the funding level in the report:

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	01/04/2003 (R'000's) (3% real)	01/04/2002 (R'000's) (2% real)
Market Value of Assets	748,720	805,649
Trust's Liability (Past and Future Service)	791,320	794,280
Surplus (Deficit)	(42,600)	11,369
Funding Level	94.62%	101.40%

69 This table shows that at the time the Trust was established, it had a small surplus which by the next year was a deficit. (I pause to note that the small deficit for the period 1 April 2002 to 31 March 2003 arose because investments return was negative. This reversed itself quickly.)

70 Mr Potgieter confirms that no consideration was given to the Trust having excess assets. As a result of the focus on the historical under-funded position, there was no regard given to the possibility of there being meaningful excess assets.

71 The funding of the Trust and the strategy approved in 2000 were based on members who retired at the age of 65. In the case of members retiring prior to the age of 65, annual actuarial valuations were done to calculate what would be needed if someone retired, for example, at 55 to cover the funding between 55 and 65 years. The actuarial valuation determined what Denel's contribution would be to make good for the early retirement. Denel was, until 2007, responsible for putting this money into the Trust. Mr Potgieter confirms that this was the only capital contribution made by Denel to the Trust. These amounts were relatively small, as the large obligation was funding from retirement until death.

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Relevant provisions of the Trust Deed

- 72 The following provisions of the Trust Deed are of particular relevance to this application.
- 73 Clause 5 records that the main objective of the Trust is “to make post-retirement medical aid subsidy contributions to the Medical Scheme as employer on behalf of the Employee beneficiaries, in order to assist such Employee beneficiaries with post-retirement contributions payable to the Medical Scheme”.
- 74 Clause 3.2 defines “Beneficiary” as meaning “capital and income beneficiaries”.
- 75 Clause 3.3 defines “Capital beneficiaries” as meaning (i) the Employee beneficiaries as well as (ii) Denel in its capacity as employer but subject to the provisions of clause 7.
- 76 Clause 3.6 defines “Employee beneficiaries” as meaning “the class of persons consisting of employees and retired employees of Denel ... in respect of whom Denel as employer has an obligation to make post-retirement medical aid subsidy contributions”. As I have explained above, this class is limited to employees who commenced employment before 1 April 2000. I explain the position in respect of the dependants of these employees below.
- 77 Clause 3.8 defines “Income beneficiary” as meaning “Denel as Income beneficiary in order to make post-retirement medical aid subsidy contributions in its capacity as employer of Employee beneficiaries, subject to the prerequisites stipulated in clause 7”.
- 78 Clause 7 regulates the distribution of income and capital by the Trustees:
- 78.1 Clause 7.4 makes it plain that the Trust is a discretionary trust as regards both income and capital. It provides that the Trustees may allocate income and

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capital "in their absolute discretion to Beneficiaries", but subject to the restrictions in clause 7.

78.2 Clause 7.3 provides that "capital may only be distributed to Denel by the Trustees in order to enable Denel to create a fund, trust or entity with objectives substantially similar to the objectives of this Trust stipulated in clause 5".

78.3 Clause 7.1 provides that income shall only accrue to Denel after the Trustees have exercised their discretion to distribute income, and may be used solely for purposes of making post-retirement medical aid subsidy contributions.

79 Clause 11 of the Trust Deed deals with amendments. Clause 11.1 allows the Trustees, with the consent of Denel, to amend any "administrative provision" in the Trust Deed to enable the Trustees to administer the Trust more effectively to achieve the objectives of the Trust provided for in clause 5. Clause 11 goes on to state that the Trustees may not amend the Trust Deed in respect of:

79.1 the objective of the Trust as provided for in clause 5;

79.2 the provisions relating to the pre-requisites subject to which income and capital are to be distributed to Denel as provided for in clause 7; and

79.3 the provisions of clause 11.

The class of Employee beneficiaries

80 I have explained above that the class of "Employee beneficiaries" became a closed class when Denel changed its conditions of service so that only employees who were employed before 1 April 2000 are owed the post-retirement medical aid obligation.

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81 The definition of "Employee beneficiaries" refers to the persons comprising this class as "employees" and "retired employees":

81.1 The definition could be read and applied so as to exclude widows or widowers of deceased employees or orphaned dependent children from the class of "Employee beneficiaries".

81.2 However, such an interpretation would be at odds with the practice of Denel and the Trust since the inception of the Trust. Since the inception of the Trust, Denel and the Trust have recognised a class of "continuation members" of the Trust. This class includes retired employees and, where a retired employee has died, his or her surviving spouse.

82 In short, Denel continues to recognise a post-retirement medical aid obligation in relation to certain dependants of a retired employee who survive the death of that employee. These dependants are regarded by Denel and the Trust as falling within the definition of "Employee beneficiaries".

83 It follows that the beneficiaries of the Trust fall into the two groups I have described above, namely:

83.1 "continuation members", being retired employees (employed before 1 April 2000) or the surviving spouses of deceased retired employees ; and

83.2 "in-service members" or "active members", who were employed before 1 April 2000 and who are currently working at Denel.

84 The actuarial valuation prepared as at 1 April 2003 gives the following membership data in respect of these two groups as at 1 April 2002 and 1 April 2003:

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2.1 Continuation Members

	01/04/2003	01/04/2002
<i>Number</i>	2557	2674
<i>Total Annual Umed Contribution</i>	52,497,300	R 46,458,288
<i>Average Annual Umed Contribution</i>	R 20,531	R 17,374
<i>Benefit Weighted Average Age</i>	58 years 10 months	60 years 0 months

In-Service members who were over the age of 60 were valued as if they have retired on the particular valuation date.

2.2 In-Service Members

	01/04/2003	01/04/2002
<i>Number</i>	4689	5017
<i>Total Annual Umed Contribution</i>	R 108,882,582	R 97,084,548
<i>Average Annual Umed Contribution</i>	R 23,221	R 19,351
<i>Benefit Weighted Average Age</i>	48 years 0 months	47 years 0 months
<i>Benefit Weighted Average Past Service</i>	17 years 6 months	16 years 5 months

85 The most recently prepared actuarial valuation was prepared as at 1 April 2021. It is attached as "FA7". That report gives the following data about membership (the reference to "CAWMs" is to "continuation and widow(er) members"):

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<i>Status</i>	<i>Number of Members</i>	<i>Subsidy weighted average age</i>	<i>Average past service</i>	<i>Proportion married</i>	<i>Average monthly subsidy 2021</i>
<i>Actives</i>	32	60.7	33.6	59%	R4 781
<i>CAWMs</i>	625	71.5	-	52%	R4 032
<i>Total</i>	657	70.9	-	53%	R4 069

86 These tables show a decline in the aggregate number of Employee beneficiaries from 7246 as at 1 April 2003 to 657 as at 1 April 2021. The decline is as a result of a variety of factors. They include:

86.1 the fact that the employee group is closed;

86.2 the number of resignations;

86.3 the death of retired employees and their spouses and dependants;

86.4 retrenchments and early retirements of employees; and

86.5 a number of transactions (“buy-outs”) that have been implemented since the 2011 financial year in terms of which Denel effectively discharged its post-retirement medical aid liability in respect of an active or retired employee. These transactions all resulted in the relevant Employee beneficiary no longer being a beneficiary of the Trust.

87 Over time, the number of Employee beneficiaries will decrease. When the last Employee beneficiary dies, the only remaining beneficiary will be Denel.

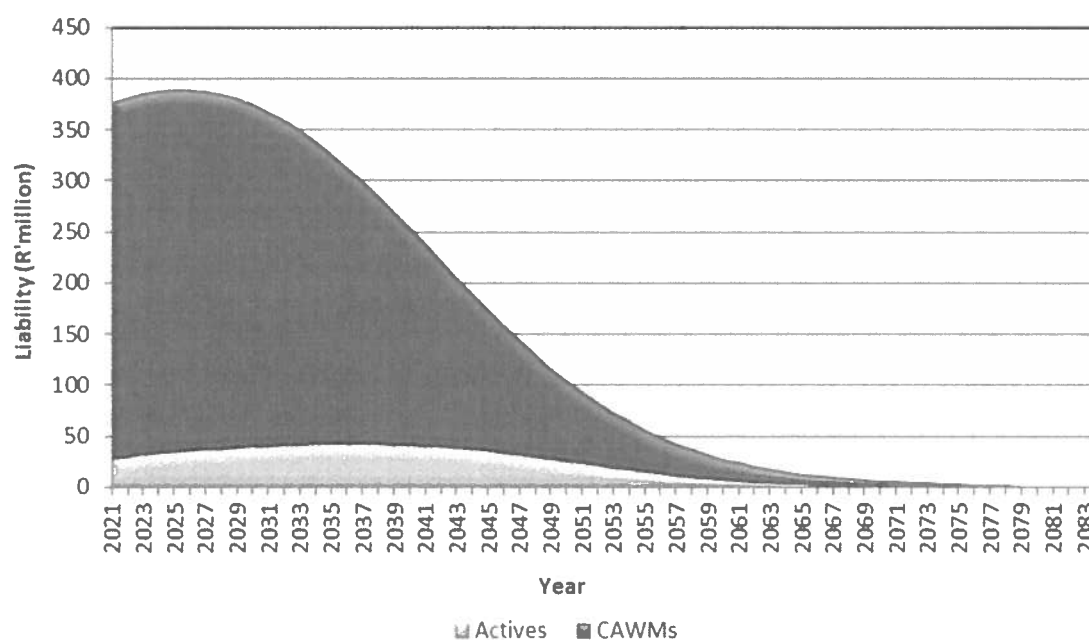
88 It is not possible to say exactly when that will occur. Since Denel recognises certain dependent children of active and retired employees as “Employee beneficiaries”, it is

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possible that this could be a very long time in the future, and probably at least not until the late 2070's.

- 89 In their most recent actuarial valuation (attached as "FA7"), the actuaries include the following graph that shows the actuaries' assessment of the future amount of Denel's liability to the Employee beneficiaries:

Accrued liability projection



- 90 This graph reflects the actuaries' projection that it will take until the year 2079 for Denel's liability to dwindle to zero. In other words, the actuaries estimate that Denel will be the only remaining beneficiary of the Trust in around 2079.

The current financial position of the Trust

- 91 I attach as "FA8" the annual financial statements of the Trust for the year ending 29 February 2020. These are the Trust's most recently available financial statements.

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92 The actuarial valuation of Denel's post-retirement healthcare liabilities also reflects the funding level of the Trust. The following is the summary extracted from the actuarial valuation as at 1 April 2021 that is referred to above and attached as "FA7":

Net Liability/(assets)

	1 April 2021 R'000	1 April 2020 R'000	1 April 2019 R'000
Liability	374 996	374 556	388 570
Assets	(1 645 114)	(1 485 729)	(1 393 868)
Net liability/(assets)	(1 270 118)	(1 111 173)	(1 005 298)
Unrecognised due to asset ceiling	1 269 250	1 110 145	1 003 803
Recognised Liability/(assets)	(868)	(1 028)	(1 495)
<i>Funding level</i>	<i>438.70%</i>	<i>396.66%</i>	<i>358.72%</i>

93 I should note that the actuarial valuation was prepared to assist Denel to comply with the requirements of the relevant accounting standard, namely IAS 19. I emphasise this because IAS 19 does not require the future service liability and the past service liability to be valued – only the past service liability is valued. The actuarial valuations that were obtained, for example, as at 1 April 2003 included the "future service liability" in the liabilities used in determining the funding levels referred to in paragraph 68. The "future service liability" is simply that portion of the member's future medical aid contribution that arises from service between the valuation date and the member's expected exit from the Trust. Given the relatively small number of active employees (32) and their average age (a subsidy weighted average age of 61), the future service liability is not a significant number.

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94 The annual financial statements and this report show that the Trust is in an extremely healthy financial position since its assets exceed the actuarially-valued liabilities of Denel (which the Trust is responsible for paying) by a very significant amount. In other words, the Trust has assets that are way in excess of what is needed to fund the medical scheme contributions of Employee beneficiaries as at 1 April 2021. As at 1 April 2021, these “excess assets” had a value of R1.2 billion, using the amounts reflected in the 1 April 2021 actuarial valuation as referred to in paragraph 92 above.

95 I shall explain below that Denel proposes that the Trustees will purchase a group annuity policy (“**Group Annuity Policy**”) that will lock-in the Trust’s financial position. As the Group Annuity Policy would effectively fully fund Denel’s post-retirement medical aid liability, all of the assets of the Trust, other than the Group Annuity Policy, would then become “excess assets”. Both the value of the assets of the Trust and the anticipated cost to the Trust of the Group Annuity Policy depend in part on future market conditions. Based on Denel’s estimates of the likely cost of the Group Annuity Policy and the amount that Denel estimates that the Trust will realise for its assets, Denel estimates that the excess assets will be approximately R800 million. This is also after providing an amount of R20 million which it is proposed be earmarked for future expenses.

The reason for the Trust having substantial excess assets

96 At the time of the Trust’s formation, it did not have significant excess assets. In fact, the first actuarial valuation of the Trust after its formation shows that as at 1 April 2003 the Trust was in a deficit (i.e. the value of its assets were not sufficient to meet Denel’s actuarially-valued liabilities).

97 By 2021, the assets of the Trust exceeded its requirements by a very substantial sum. A number of factors have contributed to this. They include the following:

97.1 First, the Trust has achieved much better returns on investments than were anticipated.

97.2 Second, those returns exceeded medical aid inflation.

97.3 Third, the actual experience of the rate at which members withdrew from the Trust (by resigning from Denel or being bought out by Denel or being retrenched) was better than what the actuaries anticipated in valuing the liabilities.

98 Denel has asked Mr Antony Lester ("**Mr Lester**") of Willis Towers Watson to explain the reason for the excess assets being so substantial and to quantify the extent to which each factor contributed to the amount of the excess. Mr Lester's report will be delivered separately. Mr Lester is the Managing Director of Towers Watson Proprietary Limited. Mr Lester will depose to an affidavit in which he elaborates on his expertise in relation to the subject matter of his report.

99 As more fully described below, Denel concluded negotiations with "the DREMS Forum" (the representative forum of Denel's pensioners referred to below). Mr Lester acted as the adviser to the forum in those negotiations. As agreed with the forum at the time, Denel paid Mr Lester's professional fees for that work.

THE TRUST DEED MUST BE VARIED TO AVOID STERILISING THE EXCESS ASSETS

100 I have explained above that the assets of the Trust exceed by a significant amount the actuarially-valued liabilities of Denel to the Employee beneficiaries. The excess assets will almost certainly continue to grow since the capital of the Trust is likely to increase

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while the number of Employee beneficiaries will continue to decline and eventually become zero.

101 Once purchased, the Group Annuity Policy will insure the liabilities that are owed to Employee beneficiaries and will provide adequate protection against future medical aid inflation. As a result, the excess assets will not be required to protect the Employee beneficiaries against fluctuations in the value of the Trust's assets. The excess assets will be superfluous to the requirements of the Trust.

102 The Trust Deed fails to provide for what is to happen with the excess assets – whether at the present time or in the future when there are no Employee beneficiaries left. Denel cannot receive the excess assets since this is not provided for in clause 7 of the Trust Deed. The Employee beneficiaries cannot receive the excess assets since the purpose of the Trust is merely to ensure that their medical scheme contributions are subsidised.

103 The Trust Deed does not deal with the situation that has arisen because the Founder never anticipated that the Trust would end up with such substantial excess assets.

104 It would make no economic sense for the excess assets to be sterilised in perpetuity. In order to avoid such an outcome, it will be necessary for the Court to vary the Trust Deed so as to regulate the distribution of the excess assets. That is the purpose of the present application.

DENEL'S PROPOSALS REGARDING USE OF THE EXCESS ASSETS

105 I turn now to describe the proposals made by Denel in order to deal with the excess assets.

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Purchase of the Group Annuity Policy

106 Denel proposes that, as a first step, the Trust will purchase the Group Annuity Policy. Denel's proposals as to how the Trustees should go about doing so are set out below.

107 In terms of the Group Annuity Policy, the insurer would have to pay the policyholder (i.e. the Trust) an annuity that is calculated in respect of each Employee beneficiary. The amount of the annuity would be calculated so as to cover Denel's post-retirement medical aid obligation in respect of each Employee beneficiary as if they were on the Discovery Essential Comprehensive Plan, even if they choose a lower cost plan, plus a buffer of 20%. The annuity (including the 20% buffer) would increase annually at the same rate as the Consumer Price Index (CPI) plus 4%.

108 The Group Annuity Policy would insure the benefits to which the Employee beneficiaries are entitled under the Trust. The Trust would use the annuity it receives under the Policy to fund the Trust's contributions to each Employee beneficiary's medical scheme premium. In this way, the Group Annuity Policy would fund the medical scheme contributions of all the Trust's beneficiaries until they die.

109 The effect of the Group Annuity Policy would be that the insurer assumes all of the mortality risks associated with each of the Employee beneficiaries and all of the investment risks associated with the Trust's assets. The insurer would be required to meet its obligations to the Trust for as long as each of the Employee beneficiaries are alive. Moreover, the insurer would be required to meet its obligations to pay the annuity regardless of the performance of the Trust's assets against its liabilities.

110 The benefits under the Group Annuity Policy would increase by CPI plus 4%. The benefits would not increase by the actual future medical aid inflation and policyholder

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would retain some of the risks of medical aid inflation. The Group Annuity Policy would provide some protection against future medical aid inflation, as I explain below.

The Individual Annuity Policies

111 Denel proposes to offer the Employee beneficiaries the option of receiving an annuity from an insurance company that will pay the amount of their medical scheme contributions as if they were on the Discovery Essential Comprehensive Plan, even if they choose a lower cost plan plus a 20% enhancement (guaranteed to increase by 4% above CPI). I shall refer to it as the “**Individual Annuity Policy**” in order to distinguish it from the Group Annuity Policy described above.

112 In essence, Denel will offer Employee beneficiaries the option to become annuitants under an individual life annuity policy that will fund their medical scheme contributions, and most likely more than this, until they die. If they accept this offer, the issue of the Individual Annuity Policy will discharge Denel’s obligation to make medical scheme contributions in respect of that Employee beneficiary and that Employee beneficiary will, as a result, no longer be a beneficiary of the Trust.

113 Employee beneficiaries of the Trust that elect this option would effectively move from being owed a medical scheme contribution by Denel (that is funded by the Trust via the Group Annuity Policy) to their own individual policy. The Individual Annuity Policy will be issued to that Employee beneficiary through the Group Annuity Policy, as explained further below.

114 The Individual Annuity Policies will operate as follows:

114.1 In terms of the Group Annuity Policy, the insurer will issue an Individual Annuity Policy in respect of each Employee beneficiary that elects to receive such a policy. Doing so will terminate the insurer’s obligations under the Group Annuity

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Policy in respect of that Employee beneficiary. The Individual Annuity Policy will in effect take the place of the benefits under the Group Annuity Policy in respect of that particular Employee beneficiary.

114.2 The amount of the life annuity contract will be determined so as to provide for the following monthly payments by the insurer to the Employee beneficiary:

- a subsidy of post-retirement medical scheme contributions in line with the maximum limit based on the relevant percentage of the current Discovery Health Essential Comprehensive benefit option; plus
- an enhancement of 20% on these contributions; and
- guaranteed annual medical scheme contribution increases of 4% above CPI applied to the medical scheme contribution and the 20% enhancement.

114.3 The monthly life annuity contract payment from the insurer will be paid directly to Discovery Health Medical Scheme (or any other approved medical scheme) for so long as the Employee beneficiary remains a member of that scheme. If the annuity payment exceeds the amount due to the medical scheme, the excess will be paid directly to the annuitant.

114.4 In terms of the current tax legislation, Employee beneficiaries will not be liable for any tax on the payments from the insurance contract as long as they are directed towards the medical scheme to meet the annuitant's medical aid contributions in full.

114.5 Spouses and dependants currently subsidised through the Trust will be covered. New spouses and dependants after the transaction will not be provided for. The child subsidy amount will cease at the age of 25 except for disabled children for

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whom this will continue for life. This is consistent with the manner in which Denel and the Trust currently deal with spouses and dependants.

114.6 On the issuing of the Individual Annuity Policy in the name of an Employee beneficiary, Denel will have discharged its post-retirement medical scheme contribution obligations towards that employee. The employee will at that stage also cease to be a beneficiary of the Trust.

115 I must emphasise that no Employee beneficiary will be compelled to accept an Individual Annuity Policy. All Employee beneficiaries will be offered an election whether they wish to retain the status *quo* or switch to an Individual Annuity Policy.

116 I anticipate that the overwhelming majority of Employee beneficiaries will elect to switch to the Individual Annuity Policy because it will put them in an improved financial position. The advantages include the following:

116.1 The subsidy amount will be based on the Discovery Essential Comprehensive benefit option, even in the case of employees who are currently on lower-priced Discovery Health options.

116.2 The subsidy amount will be independent of the medical scheme option chosen. Employee beneficiaries will be able to opt for a less expensive medical scheme option and will still receive the same subsidy amount regardless of their choice. Many Employee beneficiaries may value this option.

116.3 The Employee beneficiaries will receive a higher subsidy amount than they are currently receiving, as a result of the 20% enhancement provided by the insurance company.

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116.4 Employee beneficiaries will be protected against future inflation as the Individual Annuity Policy will guarantee increases of CPI plus 4% to provide protection for medical inflation which may be higher than CPI.

116.5 Employee beneficiaries will no longer be exposed to the risks associated with their benefits being owed by Denel and administered by the Trust. Many Employee beneficiaries may value this aspect since Denel's current financial position is poor.

117 In fairness, I must make it plain that the Individual Annuity Policies are not without some risk to Employee beneficiaries. The main risks are the following:

117.1 It is possible that the guaranteed increases in the benefits payable under the Individual Annuity Policy will not keep track with the increases in medical scheme costs. However, annuitants will have a 20% buffer plus a guaranteed increase of CPI plus 4% to protect them against this risk. Annuitants will also have the flexibility to reduce their costs by electing a less expensive medical scheme option.

117.2 It is notionally possible that the insurer may run into financial difficulty.

117.3 Changes in tax laws may adversely affect the Employee beneficiaries.

118 Denel has asked Mr Lester to also analyse the fairness of the offer to Employee beneficiaries. Mr Lester's report is will be delivered separately.

119 I explain below that the key terms of the Individual Annuity Policy are the result of an extended negotiation between Denel, on the one hand, and a representative forum of Denel's pensioners, known as the Denel Retired Employees Medical Scheme Forum (the "DREMS Forum").

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120 I must emphasise that the switch to the Individual Annuity Policy will be conditional on the grant of the relief sought in the present application. That is because the Individual Annuity Policies cannot be implemented unless the Trust Deed were to be varied. I explain the reasons for this below.

The proposed use of the Trust's excess assets

121 The Employee beneficiaries who elect to switch to the Individual Annuity Policies will no longer be beneficiaries of the Trust and Denel will have no further obligations towards them. In effect, the insurance company will pay the medical scheme contributions (after a 20% enhancement) that were formerly paid by the Trust, guaranteed to increase by 4% above inflation.

122 In respect of those beneficiaries who do not accept the offer of the Individual Annuity Policy, their medical scheme contributions will continue to be paid by the Trust as before and will be covered through the Group Annuity Policy held by the Trust. The amount paid under the Group Annuity Policy is expected to exceed the amount required by the subsidy under almost all circumstances.

123 As mentioned earlier, the Trust's excess assets are not required to meet the liability in respect of post-retirement medical contributions. That is because the Employee beneficiaries who decline the Individual Annuity Policy offer will have their post-retirement medical contributions funded by annuity payments under the Group Annuity Policy.

124 Once the Group Annuity Policy has been purchased, the excess assets will constitute all the assets of the Trust other than:

- the Group Annuity Policy; and

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- sufficient cash or securities to fund the expenses and any liabilities of the Trust.

125 It is proposed that Denel will receive the excess assets that are identified following the issue of the Individual Annuity Policies. This will require an amendment to the Trust Deed, as I explain in the next section.

126 In addition, it is proposed that the Trust distribute 50% of any future excess assets to Denel every three years with the remaining balance being paid to Denel on termination of the Trust.

127 If Denel were to receive the excess assets, those assets will no longer be available to the Trust to fund the remaining Employee beneficiaries' medical scheme contributions. Only the Group Annuity Policy will be available for this purpose. Importantly, if the Group Annuity Policy were to be insufficient, the remaining Employee beneficiaries would still be owed Denel's post-retirement medical scheme contribution obligation.

128 Denel has asked Mr Lester to comment on the risk to Employee beneficiaries that the assets of the Trust will not, in the future, be sufficient to meet Denel's obligations. Mr Lester's analysis and conclusions on this aspect are dealt with in the report which will be delivered separately.

The proposal regarding current Denel employees who are Employee beneficiaries

129 As explained above, a relatively small proportion of the Employee beneficiaries are currently employed by Denel.

130 As Denel's obligation is only to make medical scheme contributions after retirement, the Trust does not currently pay any amounts in respect of this category of Employee beneficiaries.

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- 131 The terms of the Group Annuity Policy will be that the insurer will nevertheless pay an annuity to the Trust in respect of these Employee beneficiaries. Pending their retirement, the Trust will receive that amount.
- 132 Active employees that are Employee beneficiaries will be offered an election to receive an Individual Annuity Policy on retirement. This offer will be made by Denel at around the same time as the offer to the continuation Employee beneficiaries. However, the Individual Annuity Policies will only be issued upon retirement.
- 133 It is possible that Denel and one of these employees may reach an agreement voluntarily severing employment with Denel before the employee retires. That agreement may terminate Denel's obligation to contribute to the employee's medical scheme on retirement. In those circumstances, it is proposed that the Trustees surrender the Group Annuity Policy benefits that relate to the relevant employee and distribute the proceeds to Denel.

The proposal regarding Trust expenses

- 134 The Trust will continue to incur expenses in administering the assets of the Trust and ultimately terminating and winding-up the Trust.
- 135 The following is a summary, drawn from the most recent annual financial statements of the Trust (as at 29 February 2020), of the Trust's annual expenses: R6 109 997 comprising of Audit Fees at R139 995; Bank Charges at R10 217; Administration Fees at R262 918; Principal Officer remuneration at R298 319; Consultancy Fees at R581 015; Fidelity Insurance at R30 780; Postage at R971; Trustee Expenses at Nil; Other fees paid at Nil; Legal Fees at R6 400 and Investment Management Fees at R4 779 422. These financial statements are attached as "FA8".

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136 Following the Trust's investment in the Group Annuity Policy, the amendments to the Trust Deed taking effect and the issuing of the Individual Annuity Policies, Denel envisages that the Trust would no longer incur significant asset management fees as the Trust would hold only the Group Annuity Policy and cash. The asset management fees are allowed for in the cost of the Group Annuity Policy paid to the insurer and it is only the investment of the cash that might incur asset management fees.

137 Accordingly Denel envisages that R1 100 000 would be an adequate annual budget for expenses. As asset management fees would be deducted from the return on the invested cash, asset management fees are not included in this amount.

138 Nevertheless, the actual amount of expenses that the Trust will in future incur is uncertain. Denel accordingly proposes that the funding of Trust expenses be dealt with as follows:

138.1 The Trustees will maintain an expense fund (the "**Expense Fund**").

138.2 The Expense Fund will initially be funded with an amount of R20 million, which will be deducted from the excess assets of the Trust that would otherwise be distributed to Denel.

138.3 The Trustees will disburse trust expenses from the Expense Fund.

138.4 The Expense Fund will be topped up before any future distributions of excess assets are made to Denel. This should happen at least every three years.

138.5 On the termination of the Trust, Denel will receive the balance in the Expense Fund.

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138.6 The amount of R20 million may be adjusted by agreement between Denel and the Trustees.

139 Given the likely budgeted expenses of R1 100 000 per annum, the amount of R20 million is likely to be more than adequate.

Interactions with the DREMS Forum regarding the proposals

140 The DREMS Forum represents a substantial number of the Employee beneficiaries. Denel has been negotiating with the DREMS Forum regarding the Individual Annuity Policies. To this end, Mr Paul Botha (“**Mr Botha**”) has prepared a substantive affidavit which pertains to the engagements between Denel and the DREMS forum.

141 To avoid burdening with the papers with the history of the engagements, I wish to rely on the history of the aforementioned engagements in Mr Botha’s affidavit as if specifically incorporated hereunder.

142 By the end of June 2020, the DREMS Forum was supportive of the Individual Annuity Policies (comprising a subsidy based on the premium payable for the Discovery Health Essential Comprehensive plan plus an enhancement of 20% and a guaranteed annual increase of 4% above CPI).

THE PROPOSED AMENDMENTS TO THE TRUST DEED

143 I have summarised in the preceding section the mechanisms proposed by Denel in order to deal with the excess assets. However, those mechanisms could not be implemented unless the Trust Deed were to be varied. In the section that follows, I describe the amendments that would have to be made to the Trust Deed in order to give effect to Denel’s proposals.

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144 The amendments to the Trust Deed would have to cover all the topics canvassed in the previous section. In other words, the amendments would have to deal with:

144.1 the purchase by the Trust of the Group Annuity Policy;

144.2 the issuing of the Individual Annuity Policies;

144.3 the identification of the excess assets to be distributed to Denel after the issuing of the Individual Annuity Policies;

144.4 provision for the payment of the expenses of the Trust;

144.5 the administration by the Trustees of the Group Annuity Policy for the benefit of Employee beneficiaries who do not agree to receive an Individual Annuity Policy and for the benefit of Employee beneficiaries that have not retired; and

144.6 the quantification and identification of future amounts of excess assets and their distribution to Denel on termination of the Trust and periodically before then.

145 The amendments sought by Denel are set out in the table that annexed to the notice of motion. For the sake of convenience, I have reproduced the table below:

Trust Deed Amendments	
Deletions.	Clause 7.3 and Clause 11.2.2 of the Trust deed are deleted without any consequential changes in the clause numbering.
Clause 3.1. The addition of the following new definitions:	<p>3.12 "Expense Fund"</p> <p><i>Assets of the Trust that are earmarked by the Trustees to meet the expenses of the Trust after the Scheme Implementation Date.</i></p> <p>3.13 "Group Annuity Policy"</p>

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The Group Annuity Policy to be acquired and held by the Trust.

3.14.1 Subject to clause 3.14.2, each of the following:

3.14.1.1 The insurer will be an insurer that is identified by the Trustees and approved in writing by Denel, provided that Denel's approval of the insurer will not be required if the insurer is one of Old Mutual Life Assurance Company (South Africa) Limited, Momentum Metropolitan Life Limited and Sanlam Life Insurance Limited.

3.14.1.2 The benefits under the policy will be paid in respect of all of the Employee beneficiaries (including Recognised Dependants) that are named in the policy.

3.14.1.3 The benefits under the policy will be an annuity equal to 120% of the benefits that are required to be paid in terms of Denel's current subsidy policy on the basis that all beneficiaries are on the Discovery Health Essential Comprehensive option even if they do not belong to the Discovery Health Medical Scheme or have not opted for the Essential Comprehensive option (determined on the basis of the cost, as at the date of the issue of the policy or such earlier date that Denel may specify).

3.14.1.4 The annuity will increase in January every year by CPI + 4% using the CPI published in respect of October in the preceding year, subject to a minimum inflation rate of 0%. In the event of deflation, the increase will be 4%, but the cumulative increases since date of the issue of the policy will

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not exceed CPI + 4% p.a. This means that the insurer will "clawback" the impact of setting inflation at a minimum of 0% where there has been deflation.

3.14.1.5 The annuity and the annual increases are to be guaranteed by the insurer.

3.14.1.6 The policy must confer on the policyholder (the Trust or, pursuant to a transfer of these rights by the Trust, Denel) a right to surrender the entire policy or part of the policy insofar as it relates to an Employee beneficiary.

3.14.1.7 The rights of the policyholder under the policy in respect of each Employee beneficiary will be capable of transfer by the Trust to Denel in one or more transfers from time to time, without any requirement that the insurer consents or agrees to that transfer.

3.14.1.8 The policy will provide for an individual annuity policy to be issued to the relevant Employee beneficiary if this is required by the policyholder (the Trust or, pursuant to a transfer of these rights by the Trust, Denel). The individual annuity policy will not include a right to surrender the individual annuity policy.

3.14.1.9 No subsequent marriage or remarriage will be provided for. Except for disabled children, the children's subsidy will cease at an age of 25 years.

3.14.1.10 The policy terms, including the amount and manner of discharge of the policy premium and the terms that will apply to any individual annuity policies that are issued,

must be approved by Denel in writing prior to the Trust concluding the policy.

3.14.2 Despite any provision of clause 3.14.1:

3.14.2.1 Denel and the Trustees may agree in writing to any variation of or departure from any of the criteria in clause 3.14.1; and

3.14.2.2 once Denel gives the approval that is contemplated in clause 3.14.1.10, the policy that is acquired by the Trustees shall be deemed to comply with all of the criteria in clause 3.14.1.

3.15 "Group Annuity Policy Acquisition Date"

A date specified by Denel and notified to the Trustees as the date by which the Trust must have acquired the Group Annuity Policy and discharged the obligation to pay the premium to the insurer under the Group Annuity Policy. The date specified by Denel shall not be less than 10 calendar days from the date of Denel's notice to the Trustees and shall not be less than 30 calendar days after the amendment to the Trust deed to include this clause 3.15 takes effect. The date so specified may be extended from time to time by Denel by notice to the Trustees.

3.16 "Recognised Dependant"

In relation to a deceased Employee beneficiary, a dependant of that Employee beneficiary who is recognised by the Trust and Denel as a continuation and widow(er) member of the Trust.

3.17 "Scheme Active Participant"

An Employee beneficiary in the active employ of Denel or one of its subsidiaries who at any time has concluded an agreement with Denel (that has not been terminated) to be a Scheme Active Participant under the Trust deed..

3.1518 "Scheme Implementation Date"

A date specified by Denel and notified to the Trustees as the Scheme Implementation Date under clause 7.8 of the Trust deed. The date specified by Denel shall not be less than 5 calendar days after the Group Annuity Policy Acquisition Date. The date so specified may be extended from time to time by Denel by notice to the Trustees.

3.19 "Scheme Non-Participants"

An Employee beneficiary (including for the avoidance of doubt a Recognised Dependant) who at any relevant time is neither a Scheme Pensioner Participant nor a Scheme Active Participant.

3.20 "Scheme Pensioner Participant"

A retired Employee beneficiary (including for the avoidance of doubt a Recognised Dependant) who at any time has concluded an agreement with Denel (that has not been terminated) to be a Scheme Pensioner Participant under the Trust deed.

3.21 "Trust Excess Assets"

At the relevant time, all of the assets of the Trust as at that time, including any income earned by the Trust on such

	<p><i>assets, other than (i) the Group Annuity Policy (ii) sufficient cash or securities designated by the Trustees as being required to restore the balance of the Expense Fund to R20 million or such other amount as may be agreed in writing between Denel and the Trust and (iii) sufficient cash or securities designated by the Trustees acting on the advice of an actuary appointed by the Trust as being required to fund any liabilities of the Trust as at the relevant date other than any liabilities or obligations that are funded or insured under the Group Annuity Policy or to be discharged from the Expense Fund. For this purpose, the Group Annuity Policy will be regarded as fully funding any obligations of the Trust in respect of Scheme Active Participants and Scheme Non-Participants.</i></p>
<p>Clause 5. The addition of the following further paragraphs after the current paragraph:</p>	<p><i>The further main objectives of the Trust are:</i></p> <p><i>(i) to hold, as an asset of the Trust, a group annuity policy to give effect to the original main objective of the Trust (as set out in the first paragraph of clause 5 of the Trust deed) in respect of all of the Employee beneficiaries (including for the avoidance of doubt Recognised Dependants);</i></p> <p><i>(ii) to ensure the issue of an individual annuity policy to Employee beneficiaries (including for the avoidance of doubt Recognised Dependants) who choose to receive such a policy and, in so doing, to assist these Employee beneficiaries with post-retirement contributions payable to the Medical Scheme on the basis that once such an individual annuity policy has been issued, the individual</i></p>

	<p><i>annuitant will no longer be an Employee beneficiary of the Trust;</i></p> <p><i>(iii) to hold all of the excess assets of the Trust (other than the group annuity policy and an appropriate allowance for expenses) for the sole benefit of Denel and to distribute the excess assets to Denel.</i></p>
<p>Clause 7. The addition of the following new sub-clauses.</p>	<p><i>7.7 Despite any other provisions in this Trust deed, the Trustees shall have all of the powers required to give effect to the remaining provisions of this clause 7.</i></p> <p><i>7.8 The Trustees shall exercise these powers to give effect to the main objectives of the Trust. This shall include (but not be limited to):</i></p> <p style="padding-left: 40px;"><i>7.8.1 the Trustees shall ensure that they acquire the Group Annuity Policy and discharge the obligation to pay the premium to the insurer prior to the Group Annuity Policy Acquisition Date and that:</i></p> <p style="padding-left: 80px;"><i>7.8.1.1 the benefits and other terms of the Group Annuity Policy are consistent with the Group Annuity Policy Criteria, the main objectives of the Trust and the other provisions of this Trust deed; and</i></p> <p style="padding-left: 80px;"><i>7.8.1.2 the process to select the insurer under the Group Annuity Policy and to determine the amount of the premium payable by the Trust under the Group Annuity Policy is, as between the participants in the process, consistent with the principles of fairness, equitability, transparency, competitiveness and cost-effectiveness;</i></p>

7.8.2 in respect of each Scheme Pensioner Participant, the Trustees shall vest in Denel, on the Scheme Implementation Date, the rights under the Group Annuity Policy in respect of each Scheme Pensioner Participant and shall transfer those rights, by cession, to Denel with effect from the Scheme Implementation Date;

7.8.3 in respect of each Scheme Active Participant, the Trustees shall vest in Denel, on the date on which a Scheme Active Participant retires or on any other date agreed to by Denel and the Scheme Active Participant and notified to the Trustees, the rights under the Group Annuity Policy in respect of the Scheme Active Participant and shall transfer those rights, by cession, to Denel with effect from that date, provided that if Denel and the Scheme Active Participant agree that Denel will no longer have an obligation to pay or subsidise any medical aid costs in respect of the Scheme Active Participant, the Trustees will, if Denel requires this of the Trustees, surrender the Group Annuity Policy in respect of that Scheme Active Participant and vest in and distribute the surrender proceeds to Denel;

7.8.4 in respect of any Scheme Non-Participant with whom Denel agrees after the Scheme Implementation Date that Denel will no longer have an obligation to pay or subsidise any medical aid

costs in respect of the Scheme Non-Participant, the Trustees shall either, as Denel may require of the Trustees:

7.8.4.1 surrender the Group Annuity Policy in respect of that Scheme Non-Participant and vest in and distribute the surrender proceeds to Denel; or

7.8.4.2 vest in Denel, on a date specified by Denel, the rights under the Group Annuity Policy in respect of that Scheme Non- Participant and shall transfer those rights, by cession, to Denel with effect from that date;

7.8.5 identifying, prior to the Scheme Implementation Date, the Trust Excess Assets as at the Scheme Implementation Date; and

7.8.6 on and from the Scheme Implementation Date holding the Trust Excess Assets for the sole benefit of Denel and, as may be required by Denel from time to time:

7.8.6.1 liquidating all or any of the Trust Excess Assets in consultation with Denel; and

7.8.6.2 applying the Trust Excess Assets for a purpose designated by Denel; or

7.8.6.3 vesting in, and distributing to Denel, as a beneficiary of the Trust, all or any of the Trust Excess Assets on and with effect from the Scheme Implementation Date, provided that Denel may designate any one or more dates after the Scheme

Implementation Date as the date on which any such vesting or distribution is to occur or take effect.

7.9 The Trustees shall, in respect of all Employee beneficiaries of the Trust (including for the avoidance of doubt Recognised Dependants) that are Scheme Non-Participants, continue to administer the Group Annuity Policy in respect of all Scheme Non-Participants in accordance with the original main objective of the Trust as set out in the first paragraph of clause 5 of the Trust deed and in accordance with the other provisions of this Trust deed. The Trust shall terminate once there are no longer any Scheme Non-Participants that are beneficiaries of the Trust.

7.10. As at each financial year end of the Trust following the Scheme Implementation Date and on the termination of the Trust, the Trustees shall identify any further Trust Excess Assets as at that date. The provisions of clause 7.8.6 of this Trust deed shall apply to such further Trust Excess Assets, provided that:

7.10.1 the Trustees shall be obliged to vest in and distribute to Denel one half of the further Trust Excess Assets:

7.10.1.1 as at the date of the third financial year end of the Trust following the Scheme Implementation Date; and

7.10.1.2 thereafter every three years as at the relevant financial year end of the Trust; and

7.10.2 once the Trust terminates, the Trustees shall be obliged to vest in and distribute to Denel all of the remaining Trust Excess Assets; and

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	<p>7.10.3 in addition to the obligations of the Trustees in clause 7.10.1 and clause 7.10.2, the Trustees shall have a discretion, acting on the advice of an actuary appointed by the Trust, to vest in and distribute to Denel all or any of the further Trust Excess Assets as at each financial year end of the Trust.</p> <p>7.11 On the winding up of the Trust following its termination, all of the assets remaining after discharging the Trust's liabilities and the expenses incurred in the winding-up of the Trust, including any balance in the Expense Fund, shall be paid to Denel.</p>
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146 I now explain the proposed amendments in more detail.

The proposed amendment regarding the main objectives of the Trust

147 In its present form, clause 5 of the Trust Deed provides as follows:

“5. OBJECTIVE OF THE TRUST

The main objective of the Trust is to establish separate funds and assets to be administered by the Trustees, subject to the provisions of this Trust Deed, in order to enable Denel to make post-retirement medical aid subsidy contributions to the Medical Scheme as employer on behalf of the Employee beneficiaries, in order to assist such Employee beneficiaries with post-retirement contributions payable to the Medical Scheme.”

148 Denel proposes to include the following paragraphs immediately thereafter:

“The further main objectives of the Trust are:

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(i) to hold, as an asset of the Trust, a group annuity policy to give effect to the original main objective of the Trust (as set out in the first paragraph of clause 5 of the Trust deed) in respect of all of the Employee beneficiaries (including for the avoidance of doubt Recognised Dependants);

(ii) to ensure the issue of an individual annuity policy to Employee beneficiaries (including for the avoidance of doubt Recognised Dependants) who choose to receive such a policy and, in so doing, to assist these Employee beneficiaries with post-retirement contributions payable to the Medical Scheme on the basis that once such an individual annuity policy has been issued, the individual annuitant will no longer be an Employee beneficiary of the Trust;

(iii) to hold all of the excess assets of the Trust (other than the group annuity policy and an appropriate allowance for expenses) for the sole benefit of Denel and to distribute the excess assets to Denel."

149 I elaborate below on the proposed amendments with reference to the further main objectives to be included in (i), (ii) and (iii) of clause 5.

Further main objective (i) and proposed clause 7.8.1 and proposed clause 7.9

150 Denel proposes that the Trust deed provide for a further main objective of the Trust, namely to acquire and hold the Group Annuity Policy. This new main objective will require the Trustees to purchase a group annuity policy on appropriate terms with an appropriate insurer and to hold the policy thereafter.

151 The main amendments to give effect to the purchase of the policy are the new clause 7.8.1 and the definitions of "Group Annuity Policy Acquisition Date" (clause 3.15) and "Group Annuity Policy Criteria" (clause 3.14).

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- 152 Clause 7.8.1 of the Trust Deed will require the Trustees to purchase the Group Annuity Policy by following a process that is consistent with the principles of fairness, equitability, transparency, competitiveness and cost-effectiveness. These standards are drawn from the provisions of section 217(1) of the Constitution.
- 153 Denel has a clear interest in the terms of the Group Annuity Policy and in the identity of the insurer that will provide the policy. Denel's proposal contemplates that the Trust will acquire the Group Annuity Policy. Accordingly, the proposed clause 3.14.1.10 provides that Denel must approve all of the policy terms, including the amount and manner of discharge of the policy premium and the terms that apply to any individual annuity policies that are to be issued, prior to the trust's investment in the Group Annuity Policy.
- 154 The key benefits and other terms of the Group Annuity Policy are described in proposed clauses 3.14.1.2 to clause 3.14.1.8. The terms are consistent with the features of the Group Annuity Policy described in this affidavit.
- 155 The amendments envisage that Denel will approve the final terms prior to the conclusion of the policy and that if the final terms are approved by Denel that the "Group Annuity Policy Criteria" will have been complied with.
- 156 The amendments contemplate that the Trustees will identify the insurer and that Denel must approve the insurer. The three named insurers (Old Mutual Life Assurance Company (South Africa) Limited, Momentum Metropolitan Life Limited and Sanlam Life Insurance Limited) would be acceptable to Denel and, accordingly, Denel's proposed clause does not require that it approve the identity of the insurer if the insurer is one of those three.
- 157 Proposed clause 7.9 will require the Trustees to continue to administer the Group Annuity Policy for the benefit of Scheme Non-Participants. This provision will be required

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because the Group Annuity Policy will be held, and should be administered, after all of the Individual Annuity Policies have been issued to those beneficiaries that accept an Individual Annuity Policy Offer.

158 In addition, proposed clause 7.9 will specify that the Trust will terminate once there are no longer any Scheme Non-Participants that are beneficiaries of the Trust.

Further main objective (ii) and proposed clause 7.8.2, clause 7.8.3 and clause 7.8.4

159 The addition of the second proposed new main objective to clause 5 of the Trust Deed will make it clear that it is an objective of the Trust to ensure the issuing of Individual Annuity Policies to Employee beneficiaries who choose to receive such a policy.

160 I have explained Denel's proposal in relation to the issue of Individual Annuity Policies to Employee beneficiaries, in paragraphs 100 to 104 above.

161 This should be read together with proposed clause 7.8.2 and proposed clause 7.8.3.

162 These provisions should be considered against the following background:

162.1 I have explained above that the Trust will hold a Group Annuity Policy. The benefits under the Group Annuity Policy will be described with reference to each of the Employee beneficiaries.

162.2 The Group Annuity Policy will confer on the policyholder (i.e. the Trust) an additional benefit: if the policyholder requires this of the insurer, the insurer is required to issue an individual annuity policy to an Employee beneficiary. Once an individual annuity policy is issued, the corresponding obligations under the group annuity policy will terminate. The rights of the policyholder under the

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group annuity policy in respect of each Employee beneficiary are capable of cession by the Trust to Denel.

162.3 An Employee beneficiary who wishes to receive an individual annuity policy will be required to agree with Denel that upon becoming an annuitant under such a policy, all of Denel's post-retirement medical aid obligations in respect of that Employee beneficiary and his/her dependants will have been discharged. The effect will also be that from that moment the relevant Employee beneficiary will no longer be an Employee beneficiary of the Trust.

163 The effect of the proposed amendment to clause 7.8.2 would be that on a date specified by Denel (i.e. the "Scheme Implementation Date"), the following will occur in respect of all Employee beneficiaries who wish to receive an individual annuity policy (i.e. the "Scheme Pensioner Participants contemplated by the proposed amendments):

163.1 Denel will take cession, pursuant to clause 7.8.2, of all the rights under the Group Annuity policy in respect of the Scheme Pensioner Participants and will immediately require the issue of an Individual Annuity Policy to the Scheme Pensioner Participants.

163.2 The insurer will issue the Individual Annuity Policies with the result that Denel would have discharged its post-retirement medical aid obligation in respect of the Scheme Pensioner Participants and the Scheme Pensioner Participants would no longer have any interest in the Trust.

164 Proposed clause 7.8.3 deals with the position in respect of active employees who wish to receive an individual annuity policy on their retirement (i.e. the "Scheme Active Participants" contemplated by the proposed amendments). Essentially, the amendments provide that they will receive an individual annuity policy on their retirement

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pursuant to the same mechanism that is proposed in respect of Scheme Pensioner Participants.

165 Proposed clause 7.8.3 also deals with the situation that arises if an employee leaves Denel's employ before retirement in circumstances where Denel and the employee agree that Denel will not have any post-retirement medical aid obligation in respect to that employee. In those circumstances, the Trust does not require the benefits under the group annuity policy in respect of that employee and the proposal is that the trustee would surrender the group annuity policy in respect of that employee and distribute the proceeds to Denel.

166 The purpose of proposed clause 7.8.4 is to allow Denel and Scheme Non-Participants the flexibility to agree and implement a similar transaction to the envisaged transactions with Scheme Pensioner Participants. Denel currently has no intention to pursue such transactions. In the future, however, this might change.

Further main objective (iii) and the proposed clause 7.8.5, clause 7.8.6, clause 7.10 and clause 7.11

167 The addition of the third new main objective to clause 5 of the Trust Deed will provide that it is an objective of Trust that all the excess assets of the Trust should be held for the sole benefit of Denel and should be distributed to Denel.

168 This should be read together with the proposed new definitions of "Trust Excess Assets" and "Expense Fund" and the provisions of clause 7.8.5, clause 7.8.6, clause 7.10 and clause 7.11.

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169 In essence, the proposed arrangement will operate as follows:

169.1 The Group Annuity Policy is the asset that will insure the medical scheme contributions in respect of Employee beneficiaries who do not wish to receive an individual annuity policy (i.e. the Scheme Non-Participants).

169.2 The provisions require the Trustees to, at the Scheme Implementation Date:

169.2.1 establish an Expense Fund of R20 million; and

169.2.2 provide from the assets of the Trust for any liabilities of the Medical Benefit Fund at that time that have not been discharged (other than those that are covered by the Group Annuity Policy).

169.3 All the assets of the Trust other than those earmarked in this way by the Trustees will constitute the Trust Excess Assets contemplated by the proposed amendments. On the Scheme Implementation Date, all the Trust Excess Assets will be liquidated and the proceeds distributed to Denel.

169.4 Since Denel will receive the proceeds of the liquidation, Denel has an interest in the Trustees' liquidation of these assets. The amendments accordingly provide for this asset liquidation to take place in consultation with Denel.

169.5 This will leave the Trust with the Group Annuity Policy in respect of Scheme Non-Participants, sufficient assets to discharge its liabilities and a fund of R20 million earmarked for future expenses.

170 Since it is expected that the assets that remain in the Trust (including the Group Annuity Policy) will exceed the value of the assets that it requires to fund the medical scheme contributions of the Scheme Non-Participants, it is anticipated that a further surplus will

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build up in the Trust. This further surplus will provide an additional buffer against future medical aid inflation, and will be used to top-up the Expense Fund. Every three years, one half of the surplus will be distributed to Denel as a capital distribution. Such distributions may also take place more frequently.

171 If at the termination and winding-up of the Trust there are any assets left in the Trust, including in the Expense Fund, the assets will be paid to Denel. This will only occur once there are no more Employee beneficiaries.

“Recognised Dependants”

172 The proposed amendments include a definition of “Recognised Dependants” and provide that, when reference is made to an Employee beneficiary, this includes Recognised Dependants.

173 The Recognised Dependants will be defined as follows:

“3.16 “Recognised Dependant”

In relation to a deceased Employee beneficiary, a dependant of that Employee beneficiary who is recognised by the Trust and Denel as a continuation and widow(er) member of the Trust.”

174 These dependants will be recognized as “Employee beneficiaries” and will receive an offer to become annuitants under an Individual Annuity Policy.

Miscellaneous proposed amendments

175 Clause 7.3 of the Trust Deed currently provides as follows:

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“7.3 Capital may only be distributed to Denel by the Trustees in order to enable Denel to create a fund, trust or entity with objectives substantially similar to the objectives of this Trust stipulated in clause 5.”

176 It is proposed that this clause be deleted as it would be inconsistent with the amended main objectives of the Trust and the other provisions that have been described above.

177 Clause 11 currently provides as follows:

“11. AMENDMENT TO THE TRUST DEED

11.1 The Trustees shall be entitled with the consent of Denel, to amend any administrative provision set out in the Trust Deed in order to enable the Trustees to administer the Trust more effectively in order to achieve the objectives of the Trust provided for in clause 5 above.

11.2 The Trust Deed may not be amended in any way whatsoever in respect of:

11.2.1 the objectives of the Trust as provided for in clause 5.

11.2.2 the provisions relating to the pre-requisites subject to which income and capital are to be distributed to Denel as provided for in clause 7.

11.2.3 the provisions of this clause 11.”

178 If clause 7.3 were to be deleted (see above), then clause 11.2.2 would also have to be deleted.

179 Finally, it is proposed that clause 7.7 be added in order to ensure that any inconsistencies between the proposed new clauses and remaining provisions of the Trust Deed are resolved in favour of the proposed new clauses. It will provide as follows:

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“7.7 Despite any other provisions in this Trust deed, the Trustees shall have all of the powers required to give effect to the remaining provisions of this clause 7.”

THE TRUST DEED SHOULD BE VARIED IN TERMS OF SECTION 13 OF THE ACT

180 Section 13 of the Act provides as follows:

“If a trust instrument contains any provision which brings about consequences which in the opinion of the court the founder of a trust did not contemplate or foresee and which—

(a) hampers the achievement of the objects of the founder; or

(b) prejudices the interests of beneficiaries; or

(c) is in conflict with the public interest,

the court may, on application of the trustee or any person who in the opinion of the court has a sufficient interest in the trust property, delete or vary any such provision or make in respect thereof any order which such court deems just, including an order whereby particular trust property is substituted for particular other property, or an order terminating the trust.”

181 For the reasons explained above, Denel is a person with an interest in the property of the Trust (within the meaning of section 13).

182 The Trust Deed brings about consequences that the Founder did not contemplate or foresee. I say so for the following reasons:

182.1 The Founder simply did not envisage a situation in which the Trust would find itself sitting on a massive pile of excess assets. Had the Founder envisaged this, the Trust Deed would have provided for how the excess assets would be distributed and dealt with.

182.2 The stated objective of the Trust is to “enable Denel to make post-retirement medical aid subsidy contributions” for Employee beneficiaries. The objective of the Trust was never to generate income for beneficiaries beyond that narrow

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purpose – the Trust was a vehicle for medical scheme contributions, not a general investment vehicle. It follows that it was never contemplated by the Founder that the Trust would generate excess assets well above what was necessary for the Trust to fund its obligations to Employee beneficiaries. For similar reasons, it was never contemplated by the Founder that Employee beneficiaries would be entitled to a windfall in the form of the excess assets.

182.3 The unforeseen consequence of sterilised excess assets is brought about by clause 7 of the Trust Deed, which restricts the Trustees' discretion to make distributions to Denel. These restrictions were intended to ring-fence and protect funds so as to ensure the Trust's ability to pay medical scheme contributions. The Founder did not intend the restrictions to operate in perpetuity and even when the Trust's assets far exceed what is required to meet the Trust's object.

182.4 Contemporaneous evidence shows that the Founder did not contemplate the Trust maintaining any excess assets at all, let alone in significant amounts. In February 2000, the Founder prepared a joint memorandum to Denel's Personnel & Remuneration Committee (a copy of the memorandum has already been attached as "FA4"). I draw attention to the following parts of this memorandum:

182.4.1 Paragraph 6.1.3 of the memorandum recommended that Denel "manage the post-retirement healthcare liability of the current 8566 members [Medical Benefit Fund] on a 'dying-fund' basis, i.e. run out of money one day after the death of the last members (+/- 45 years from now)."

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182.4.2 Paragraph 6.3 of the memorandum recommended ways to fund a “deficit in the future” in the Medical Benefit Fund.

182.5 This provides contemporaneous evidence that it was never intended that the Medical Benefit Fund would accumulate excess assets. To the contrary, the Medical Benefit Fund was always intended to be managed so that it would “run out of money one day after the death of the last member.” The Medical Benefit Fund was the Founder of the Trust, and there is no reason to believe that the Medical Benefit Fund contemplated anything different in respect of the Trust.

182.6 Mr Potgieter confirms that the possibility of excess assets arising in the Trust was not considered at the time the Trust was established.

183 I submit that, in its present form, the Trust Deed brings about consequences that fall within the ambit of sections 13(a), (b) or (c) of the Act. I make this submission for the following reasons:

183.1 The sterilisation of the excess assets of the Trust hampers the achievement of the objects of the Founder as envisaged in section 13(a) of the Act. The Trust was created for the sole purpose of enabling Denel to pay post-retirement medical scheme contributions. Implicit in that objective is that Trust funds would be managed efficiently and in a commercially sensible manner. Sterilising Trust assets that are significantly more than the actuarial liabilities is inefficient and commercially insensible.

183.2 Sterilising the excess assets conflicts with the public interest as envisaged in section 13(c) of the Act. It would make no commercial sense to sterilise substantial amounts of money. The public interest favours the productive use of resources. Denel is the only beneficiary with a sensible entitlement to the excess

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assets. The Trustees should be allowed to distribute the excess assets to Denel so that the funds can be put to productive use.

183.3 I have explained above that Employee beneficiaries are very likely to be better off if they were to accept the Individual Annuity Policies, and that the Individual Annuity Policies cannot be implemented unless the Trust Deed were to be varied. The present situation therefore prejudices the interests of beneficiaries, within the meaning of section 13(b) of the Act.

184 For all the reasons set out above, I submit that it would be just to vary the Trust Deed in the manner set out in the schedule to the notice of motion.

PRAYER

185 Denel asks for order in terms of the notice of motion.

186 On the return day, Denel intends to ask that the rule *nisi* be confirmed.



KHOHLONG WILLIAM HLAKOANE

I certify that the deponent acknowledged that s/he knows and understands the contents of this affidavit, which was signed and sworn to before me at Bryanston on this the 21st day of **MAY 2021**, in accordance with Regulation No. R1258 dated 21 July 1972 as amended by Government Report R1648 dated 19 August 1977, as further amended by Government Report R1428 dated 11 July 1980, and by Government Report R774 of 23 April 1982.



Andre Ferreira
Commissioner of Oaths
Practising Attorney RSA
52 Katherine Street
Wierda Valley, Sandton
Johannesburg 2196



COMMISSIONER OF OATHS

Designation and Area:

Full Names:

Street Address

WILLENHOUTS VAN DER MERWE

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**DENEL MEDICAL
BENEFIT TRUST**

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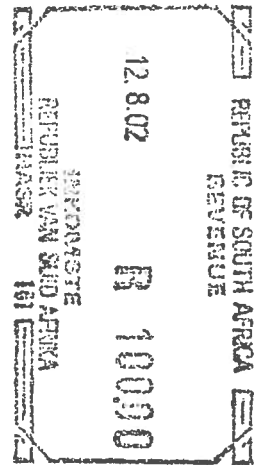
1. NAME

The name of the Trust is the **DENEL MEDICAL BENEFIT TRUST** (hereinafter referred to as the Trust) which is to be administered in accordance with the provisions set out in this Trust deed.

2. OFFICE

The office of the Trust is situated at:

Denel Building
Jochemus Street
Erasmuskloof
Pretoria



or at such other place as the Trustees may determine from time to time.

3. DEFINITION OF TERMS

Words have the same meaning as attached to them, and unless this conflicts with the context, all words and expressions which refer to the male gender include the female gender and the words in the singular also include the plural, and vice versa, and the following expressions have the following meanings:

3.1 "Auditor"

The External Auditors of Denel (Proprietary) Limited.

3.2 "Beneficiary"

Capital and income Beneficiaries

3.3 "Capital beneficiaries"

The Employee beneficiaries as well as Denel in its capacity as employer subject to the provisions of clause 7.

3.4 "Contribution"

Any amount which the Trust may received by way of donation, gift, bequest or otherwise.

3.5 "Denel"

Denel (Proprietary) Limited, a company incorporated in terms of the Companies Act, 1973, as amended, and all of its subsidiary companies.

3.6 "Employee beneficiaries"

The class of persons consisting of employees and retired employees of Denel, including employees of participating employers,, in respect of whom Denel as employer has an obligation to make post-retirement medical aid subsidy contributions.

3.7 "the Founder"

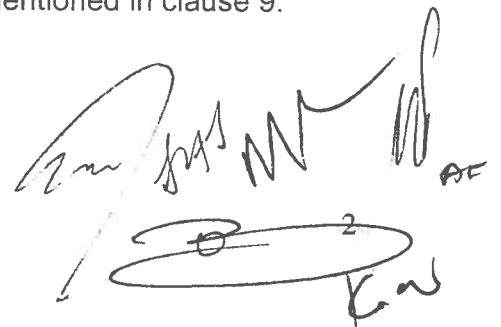
The Denel Medical Benefit Fund

3.8 "Income beneficiary"

Denel as Income beneficiary in order to make post-retirement medical aid subsidy contributions in its capacity as employer of Employee beneficiaries, subject to the prerequisites stipulated in clause 7.

3.9 "Trustee"

The Trustees appointed from time to time subject to the provisions of this Trust deed, the first Trustees being the trustees mentioned in clause 9.



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3.10 "Medical Scheme"

Umed or a substitute medical scheme registered in terms of the Medical Schemes Act, Act no. 131 of 1998, which Denel may establish or appoint for Employee Beneficiaries.

3.11 "Participating Employers"

Employers who previously formed part of Denel or subsidiary companies of Denel and in respect of which employers Denel undertook to make post-retirement medical aid subsidy contributions to their employees.

4. NAME OF TRUST

4.1 The name of the Trust shall be the Denel Medical Benefit Trust.

4.2 Notwithstanding the provisions of clause 4.1, the Trustees may, by way of unanimous resolution, change the name of the Trust from time to time to such other name as they may deem appropriate in the circumstances.

5. OBJECTIVE OF THE TRUST

The main objective of the Trust is to establish separate funds and assets to be administered by the Trustees, subject to the provisions of this Trust Deed, in order to enable Denel to make post-retirement medical aid subsidy contributions to the Medical Scheme as employer on behalf of Employee beneficiaries, in order to assist such Employee beneficiaries with post-retirement contributions payable to the Medical Scheme.

6. CONTRIBUTION TO THE TRUST

Anyone can voluntarily make a donation, gift or contribute in another way to the Trust. The fact that someone makes a donation or gift or contributes in any other

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way, shall under no circumstances be interpreted that such "contributor" should obtain a right to any benefit.

7. PRE-REQUISITES IN RESPECT OF INCOME AND CAPITAL DISTRIBUTED TO DENEL

7.1 Income of the Trust shall only accrue to Denel –

7.1.1 after the Trustees have exercised their discretion to distribute income to Denel as provided for in clause 7.4;

7.1.2 the income so distributed is used, exclusively for purposes as set out in clause 5 above by Denel.

7.2 No income that accrued to Denel as stipulated in clause 7.1 above, shall be paid by the Trustees to Denel, but shall be paid to the relevant medical schemes on behalf of Denel by the Trustees and to the extent that the amount accrued to Denel as stipulated herein exceeds the contributions payable to Medical Schemes, such excess shall be deposited in an account created by the Trustees on behalf of Denel to be utilized in another year of assessment for purposes of clause 5 on behalf of Denel.

7.3 Capital may only be distributed to Denel by the Trustees in order to enable Denel to create a fund, trust or entity with objectives substantially similar to the objectives of this Trust stipulated in clause 5.

7.4 The Trust is a discretionary trust as far as the allocation, distribution and use of income of the Trust and capital of the Trust are concerned and the Trustees can allocate the income of the Trust and the capital, subject to the provisions of this clause 7 in their absolute discretion to Beneficiaries.

7.5 Any allocation of Trust capital can be made partially in cash and partially in specie.



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7.6 The Trustees shall be entitled to determine in such manner as they may consider fit, whether any money is to be considered as income or capital and the decision of the Trustees shall be final and binding and there shall be no appeal therefrom.

8. **MANAGEMENT**

The affairs of the Trust are managed in terms of these Rules by a Board of Trustees of at least 3 (three) and not more than 8 (eight) persons as determined and appointed from time to time by Denel.

9. **TRUSTEES**

9.1 **Appointment of Trustees**

9.1.1 The following Trustees shall serve as the First Trustees of the Trust:

Mr MC Jita (Chairperson)

Mr HD du P Potgieter

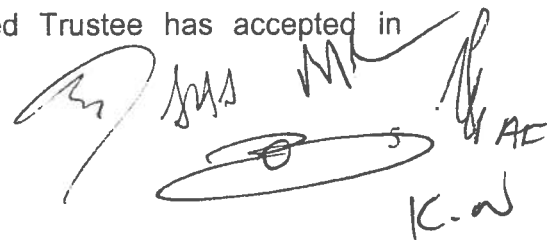
Mr Z Makhaye

Ms TA Tulwana

Mr NC Bianco

9.1.2 At all times there shall be at least 3 (three) Trustees in office and if the number of Trustees, for whichever reason falls below the minimum, the number shall be supplemented within 60 (sixty) days by the remaining Trustees, provided that only persons who are approved by the board of directors of Denel may be nominated and appointed as Trustees. Until such time as the vacancy is filled, the remaining Trustees shall be authorized to exercise all the powers of the Trustees for the preservation of the Trust assets.

9.1.3 No appointment or nomination of a Trustee shall be effective before the appointed or nominated Trustee has accepted in writing.



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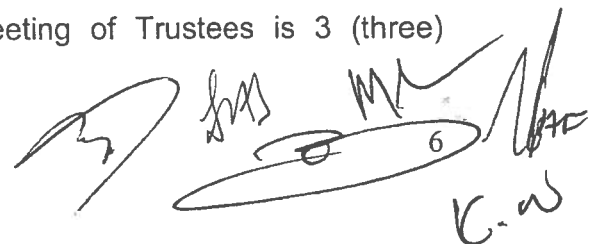
9.2 Termination of Office of Trustee

The office of a trustee shall be terminated immediately and without any further notice or intervention of the Court and the Trust assets cease to be vested in a Trustee, if –

- 9.2.1 the Trustees resigns by giving his fellow Trustees written notice to that effect; or
- 9.2.2 he becomes mentally disturbed or mentally ill; or
- 9.2.3 he is incompetent or incapable for any reason to act as Trustee; or
- 9.2.4 his estate becomes sequestrated, whether provisionally or finally, or if he enters into a compromise with his creditors or commits an act of insolvency; or
- 9.2.5 he is disqualified under the Companies Act as amended from time to time to act as director of a company.

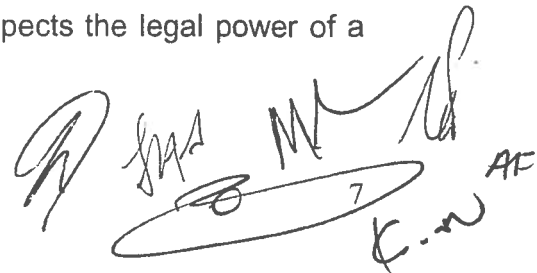
9.3 Functions of the Trustees

- 9.3.1 Provided that the Trustees constantly heed the objectives of the Trust and subject to the Trustees' duties of trust, the Trustees shall be entitled in the managing and administration of the affairs of the Trust to follow such administrative procedures as the Trustees may determine from time to time.
- 9.3.2 Any Trustee shall be entitled to convene a meeting of the Trustees with 7 (seven) days' written notice to the other Trustees.
- 9.3.3 The required quorum for a meeting of Trustees is 3 (three) trustees.



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- 9.3.4** If 10 (ten) minutes after a meeting has commenced the required quorum of Trustees is not present, the meeting of the Trustees is adjourned for a period of at least 3 (three) days and shall meet at a date, time and place as fixed by the Trustees at the adjourned meeting and of which all Trustees shall be notified in writing. The quorum requirement for the adjourned meeting is 3 (three) Trustees.
- 9.3.5** Subject to any express provisions of the agreement to the contrary all resolutions and actions of the Trustees shall be taken and made by means of an unanimous resolution.
- 9.3.6** A resolution which is placed in writing and signed by all the Trustees has the same legal power as a resolution taken at a properly constituted meeting.
- 9.3.7** The Trustees are obliged to record all resolutions relating to the Trust in a minute book and in this regard the same procedures shall be followed that companies are required to follow in terms of Section 204 of the Companies Act, 1973 (Act 61 of 1973) (as amended from time to time).
- 9.3.8** The Trustees shall meet as often as the Trustees decide, but at least once a year.
- 9.3.9** The Trustees shall be entitled to authorize one or more of the Trustees to sign on behalf of the Trustees all documents for official purposes which are necessary in the administration of the Trust and for the execution of any transaction relating to the Trust's affairs, and any resolutions which are certified by a Trustee as a true extract from the minutes of a special resolution of all the Trustees shall have in all respects the legal power of a resolution signed by all the Trustees.



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9.4 Security

9.4.1 Every Trustee, whether a First or subsequent Trustee, is exempt from any obligation to provide security relating to his appointment or for the proper administration of the Trust to the Master of the Supreme Court of South Africa or any other official as provided in any Act which is in force or which may hereafter become in force relating to the protection of the Trust assets, and the Master and any other such official shall hereby be requested to dispense with any such security.

9.4.2 If the Master at his discretion requires that a Trustee grants security, the cost relating to the granting of such security shall be paid by the Trust and the Trustees are hereby authorized to allow such payment to be made out of the Trust's funds.

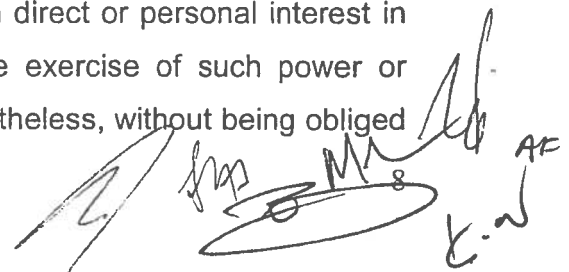
9.5 Discretionary Powers of Trustees

9.5.1 The discretionary powers which have been granted in terms of this agreement to the Trustees, unless expressly provided to the contrary in this agreement, shall be absolute and unimpeded.

9.5.2 No discretion or power which is granted to the Trustees in terms of this agreement shall be exercised or applied in a manner which shall result in any portion of the Trust assets or the income of the Trust being allocated or applied directly or indirectly to a Trustee other than in his capacity as Trustee.

9.6 Interests of the Trustees

9.6.1 Any trustee may exercise the powers and discretions granted to him hereunder or lawfully, or agree with the exercise thereof despite the fact that he may have a direct or personal interest in the manner or consequence of the exercise of such power or discretion, but a Trustee may, nevertheless, without being obliged

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thereto and should he prefer, refrain from any action or exercise of a power in any affair in which he may have a personal interest and may permit his fellow Trustee(s) to act alone in the exercise of the powers and discretions mentioned with respect to such matter.

9.6.2 Every Trustee who has such an interest in any action concerning the Trust shall be obliged to disclose the nature and extent of his interest beforehand in writing to his fellow Trustee(s).

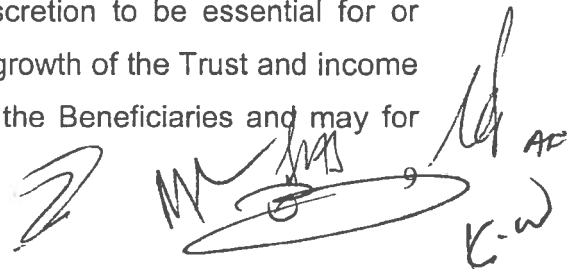
9.6.3 If any benefit, regardless of the nature thereof, should accrue to a Trustee which is related directly or indirectly to any transaction in which the Trust is involved or if a Trustee neglects to comply with the disclosure duty in clause 9.6.1, he shall receive such benefit on behalf of the Trust and shall be obliged to make it over to the Trust at the request of the other Trustee(s) in the manner and at such a time as determined by the remaining Trustee(s).

9.7 Powers and Competencies of the Trustees

9.7.1 The Trust assets and income vests in the Trustees in their capacity as such and such assets and income shall not form part of the Trustees' personal estates.

9.7.2 The Trust assets and income and all powers which are granted to the Trustees in accordance with this agreement vest, in the Trustees in their capacity as Trustees in order to enable them to deal with the Trust assets and income of the Trust on behalf of the beneficiaries to the advantage of the beneficiaries and not to the personal advantage of the Trustees.

9.7.3 The Trustees shall be entitled to perform any action whatsoever which they deem at their sole discretion to be essential for or conducive to the preservation and growth of the Trust and income of the Trust and in the interest of the Beneficiaries and may for



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that purpose perform any function on behalf of the Trust which a fully contractually competent natural person may perform in respect of his own affairs.

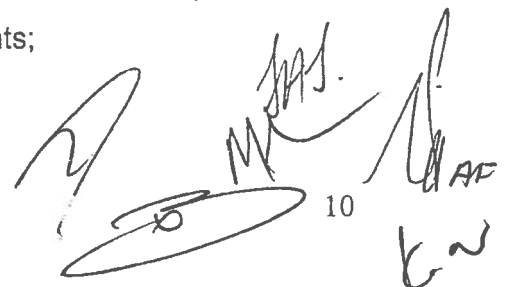
9.7.4 Without restricting the generality of the powers of the Trustees in any way, the Trustees shall be empowered to -

9.7.4.1 open a bank account in the name of the Trust; draw cheques from and deposit monies into such account, allow bills of exchange and guarantees to be issued against such account and hand over bills of exchange in favour of the Trust for collection.

For the purposes of this subparagraph the signature of any of the Trustees shall suffice for any transaction with regard to the bank account, provided that the power granted to a single Trustee is supported by a proper resolution of the Trustees. "Bank account" also includes accounts at or any credit arrangements with banks and recognized financial institutions.

9.7.4.2 buy, sell or exchange goods of any nature, movable or immovable, material or not material and wherever they may be situated, including shares, stocks, funds, letters of credit and securities, and enter into any credit agreements and contracts of any nature such conditions as provided by the Trustees;

9.7.4.3 sell, lease, improve, change and maintain any fixed property which comprises part of the Trust capital, and if necessary, to demolish fixed improvements and erect new improvements;

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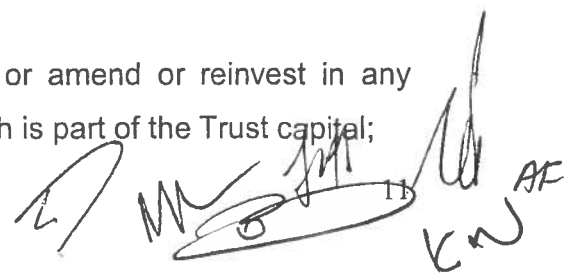
9.7.4.4 effect any sale of assets which are part of the Trust capital and at their own unrestricted discretion conduct such sale by private auction, public tender or privately and at their own unrestricted discretion to grant credit in respect of the whole purchase price or a part thereof, with or without security or interest;

9.7.4.5 draw up any documents or deed with regard to disposal, distribution, exchange, transfer, mortgaging, hypothecation or otherwise in any Deeds Office, Mining Title Office or other public office dealing with servitudes, usufructs, restricted interests or otherwise, and to make any applications, grant permission and agree to any amendment, change, annulment, cession, discharge, reduction, substitution or anything which in general pertains to any deed, bond or document, and for any purposes to obtain copies of deeds, bonds or documents, and in general to do any action whatsoever, or allow any action whatsoever to be done, in any such office;

9.7.4.6 enter into lease contracts as tenant or lessor and if a lessor, to collect rental and cancel lease contracts and take the necessary steps to remove a tenant from a leased property and undertake township development and sectional title development on such property;

9.7.4.7 invest monies which are part of the Trust capital or income whether with interest or interest free in such securities, policies or instruments and in such a manner and according to such conditions as the Trustees may determine;

9.7.4.8 at their discretion retain or amend or reinvest in any form any investment which is part of the Trust capital;



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- 9.7.4.9 enter into loans for the purposes of the Trust, with or without interest and with or without security, and according to such conditions as may be agreed upon with the person or institution which makes the loan to the Trustees;
- 9.7.4.10 mortgage any asset of the Trust, hypothecate it or give a retention thereon;
- 9.7.4.11 institute, defend or settle legal proceedings;
- 9.7.4.12 attend meetings of creditors of a private individual, company or body which is a debtor of the Trust, irrespective of whether the meeting pertains to insolvency, liquidation or judicial management, to vote about any matters which are submitted to the meeting, and, in general to exercise any rights which are afforded to a creditor in such circumstances;
- 9.7.4.13 guarantee the compliance of the contracts or commitments of any person or company against remuneration or free of charge as guarantor and as co-principal debtor and to mortgage assets of the Trust as security for that purpose;
- 9.7.4.14 give receipts, exemptions or indemnities in respect of any amount or claim which is received or which has been complied with;
- 9.7.4.15 make use of the services of professional advisors and of artisans for the affairs of the Trust and to pay for such services out of the Trust;



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9.7.5.5 not possess any assets of the Trust for their own benefit or for the advantage of their estates, except as expressly stipulated to the contrary in this deed, and the estate, assets, accounts and affairs of the Trust shall be held, controlled and administered separately from those of the Trustees. All movable, immovable and negotiable assets, documents, investments, business transactions and business must be registered and take place in the name of the Trust or in the name of the Trustees, but then indicating that it is on behalf of and in their capacity as Trustees of the Trust.

9.8 Personal Liability of Trustees

A Trustee shall not be personally liable for any loss which the Trust may suffer, irrespective of the reason therefore, unless such loss arises out of a deliberate unlawful action or the gross negligence of a Trustee. A Trustee shall not be liable for a fraudulent act of a fellow Trustee unless there was collaboration between such a Trustee and the fellow Trustee.

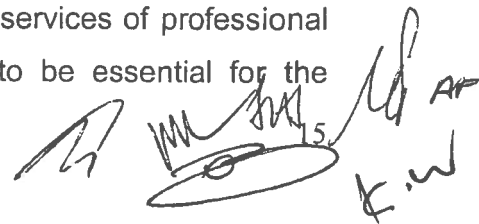
9.9 Remuneration of Trustees

The remuneration which the Trustees may claim for their services shall be fixed annually by means of a resolution by the Trustees as near as possible to the end of the Trust's financial year.

10. PROFESSIONAL SERVICES

10.1 The Trustees must, from time to time, appoint a chartered accountant (referred to in this deed as the auditor of the Trust) to act as auditor of the Trust. At the end of each financial year the Trustees shall instruct the auditors to draw up audited financial statements of the Trust.

10.2 The Trustees shall be entitled to make use of the services of professional persons in so far as they deem such services to be essential for the



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purposes of the Trust and shall pay for such services out of the Trust's fund.

10.3 The fact that a Trustee exercises a profession or business shall not be an impediment to him or his firm to receive and execute mandates in professional or other capacity from the Trust and to be remunerated therefore just as if he was not a Trustee.

11. **AMENDMENT OF TRUST DEED**

11.1 The Trustees shall be entitled with the consent of Denel, to amend any administrative provision set out in the Trust deed in order to enable the Trustees to administer the Trust more effectively in order to achieve the objectives of the Trust provided for in clause 5 above.

11.2 The Trust Deed may not be amended in any way whatsoever in respect of –

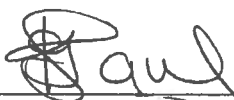
11.2.1 the objective of the Trust as provided for in clause 5;


11.2.2 the provisions relating to the pre-requisites subject to which income and capital are to be distributed to Denel as provided for in clause 7;

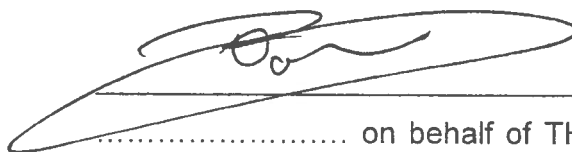
11.2.3 the provisions of this clause 11.

SIGNED on this 30 day of OCTOBER.....2002

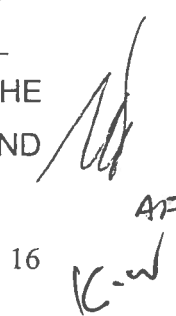
AS WITNESSES

1. 

2. 



..... on behalf of THE
DENEL MEDICAL BENEFIT FUND
duly authorized thereto



SIGNED on this 31 day of OCTOBER 2002

AS WITNESSES

- 1. Ms Grobler
- 2. [Signature]

X [Signature]
 TRUSTEE

SIGNED on this 31 day of OCTOBER 2002

AS WITNESSES

- 1. Ms Grobler
- 2. [Signature]

[Signature]
 TRUSTEE

SIGNED on this 1st day of NOVEMBER 2002

AS WITNESSES

- 1. Ms Grobler
- 2. [Signature]

[Signature]
 TRUSTEE

SIGNED on this 4th day of NOVEMBER 2002

AS WITNESSES

- 1. [Signature]
- 2. [Signature]

[Signature]
 TRUSTEE

TO BE KEPT IN THE ATTORNEY GENERAL'S OFFICE FOR THE ORIGINAL DOCUMENT
ENTRUSTED A TRUE COPY OF THE ORIGINAL DOCUMENT. THERE IS NO
OBLIGATION TO RETURN THE ORIGINAL DOCUMENT TO THE
OFFICE OF THE ATTORNEY GENERAL. THE ORIGINAL DOCUMENT IS
TO BE KEPT IN THE OFFICE OF THE ATTORNEY GENERAL.
UNLESS OTHERWISE ORDERED BY THE COURT.
[Signature]
MEESTER VAN DIE NOORD GAUTENG HOOGGEREGSHOF, PRETORIA
MASTER OF THE NORTH GAUTENG HIGH COURT, PRETORIA

MASTER OF THE NORTH GAUTENG
HIGH COURT PRETORIA

RECEIVED
TIRHANI SHIPHAMELE

2020 -09- 01

Time:
PRETORIA

MEESTER VAN DIE NOORD GAUTENG
HOOGGEREGSHOF PRETORIA

AT
K.W



DENEL GROUP

Office of the Interim GCEO

Tel: +27 12 671 2758

talibs@denel.co.za

marietjies@denel.co.za

Ref 082 1911 Post-Retirement Medical Aid Obligation of Denel SOC Ltd

The Trustees of the Denel Medical Benefit Trust

Dear Trustees

POST-RETIREMENT MEDICAL AID OBLIGATION OF DENEL SOC LIMITED: ALTERNATIVE OFFER TO CURRENT AND FORMER EMPLOYEES

1. We refer to your letter of 20 August 2020.
2. We attach:
 - 2.1 a note by Ant Lester of Willis Towers Watson outlining Denel's proposal in relation to the change in the investment strategy of the Denel Medical Benefit Trust ("DMBT");
 - 2.2 draft of the amendments that Denel envisages being made to the trust deed of the DMBT; and
 - 2.3 a note by Ant Lester of Willis Towers Watson that assesses the impact on DMBT members of the envisaged transaction.

Change to investment strategy

3. You will note from the first mentioned memorandum that Denel proposes:
 - 3.1 DMBT liquidates its current investments;
 - 3.2 as soon as possible, the DMBT invest in a portfolio of inflation-linked bonds;
 - 3.3 thereafter, DMBT uses the bonds to discharge the premium for an appropriate group annuity policy to be issued by an insurer; and
 - 3.4 DMBT invests the balance of its assets in the money market.
4. We are available to discuss this proposal with a view to ensuring that the investment strategy secures a good outcome for all stakeholders. We look forward to a response.

Denel SOC Ltd, Reg No 1992/001337/30, Nellmapius Drive, Irene

P O Box 8322, Centurion, 0046, South Africa. Tel: +27 (0)12 671 2700, Fax: +27 (0)12 671 2751

Directors: Ms M W Hlahla (Chairperson), Ms M K Lehloenyane, Mr T H Magazi, Lt Gen. (Ret) T T Matanzima, Mr M M Mnisi, Dr H Nel, Gen. (Ret) S Nyanda, Ms S R Rabkin, Mrs G T Serobe, Dr S P Sibisi, Ms N Siyotula, Mr M T Sadik¹ (Interim Group Chief Executive Officer), Ms C le Grange¹ (Group Chief Financial Officer)

¹ Ex-Officio Director

Group Company Secretary: FluidRock Co Sec (Pty) Ltd

AF

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Trust Deed Amendments

5. As previously conveyed, Denel intends to apply to the High Court for an order (in terms of section 13 of the Trust Property Control Act) amending the trust deed of the DMBT.
6. You will note from the current draft of the amendments that:
 - 6.1 Denel envisages that the group annuity policy referred to above will be in place before the trust deed amendments take effect. We are advised that it would be better for the group annuity policy to be in place before Denel launches its application.
 - 6.2 A number of transactions will take effect on "the Scheme Implementation Date". It is envisaged that this date will follow:
 - 6.2.1 the group annuity policy being in place;
 - 6.2.2 Denel having obtained the relevant court order amending the trust deed;
 - 6.2.3 the completion of the member communication and offer process to be undertaken by Denel in respect of active and continuation members of the DMBT; and
 - 6.2.4 the completion of the various other steps required to implement the scheme.
 - 6.3 Denel envisages proceeding with the trust deed amendments regardless of whether all of the DMBT members accept Denel's offer. As a result, the draft trust deed amendments include new provisions that will apply to the manner in which the trustees will be required to administer the remaining assets of the DMBT for the benefit of DMBT members who do not accept Denel's offer and for the benefit of Denel. You will note, in particular, that the amendments contemplate that the DMBT will include an expense fund that will be sufficient to ensure that the DMBT's expenses are adequately covered. We have proposed an amount of R10 000 000 for this expense fund on the basis that investment management fees will be recovered directly from the assets and the administration costs will be allowed for in the consideration paid to the insurer, thus reducing the operating costs of DMBT. In addition, it is possible that there may be a substantial reduction in the number of trust beneficiaries which should reduce costs. Please would you consider whether this amount is appropriate.
7. We would be pleased to receive comments from the trustees on the draft amendments and for an opportunity to discuss these matters.
8. We look forward to hearing from you.

Yours sincerely,



Talib Sadik
**INTERIM GROUP CHIEF EXECUTIVE OFFICER
DENEL SOC LTD**

Date: 19 November 2022

INVESTMENT STRATEGY NOTE BY A LESTER

AF
K.W

Investment strategy – Denel Medical Benefit Trust

Introduction

We have prepared a separate report setting out the reasons why we consider that the proposed offers to members of the Denel Medical Benefit Trust (“DMBT”) may be described as generous. However, to give effect to this offer Denel SOC Limited (“Denel”) needs certainty that the assets of the DMBT include a group annuity policy that will lock-in the benefits to be received by members (both those who elect to exit the current arrangement and those who don’t). In addition, Denel would request that the other assets of the DMBT are invested on a basis that provides much greater certainty of the amount which will be distributed to company if the envisaged scheme is implemented.

We highlight that the proposed scheme, including the distribution to Denel, does not require the approval of the Trustees of the DMBT (“the Trustees”). Rather the scheme will be effected in accordance with the DMBT Trust Deed once it has been amended in terms of an order of the High Court. The High Court will decide whether to make that order. Accordingly, what is being requested of the Trustees is that they amend the investment strategy of the DMBT so that it is possible to implement the scheme as planned should the Court so approve. In our view, the Trustees may be able to conclude that the implementation of the proposed investment strategy is appropriate regardless of whether the distribution to Denel is implemented. Naturally, the Trustees may wish to seek advice from their appointed investment consultant before doing so.

Investment strategy for the Trust

The proposed transaction involves the purchase of a life annuity policy from an Insurer which guarantees the members’ post-retirement medical aid subsidy but based on the Discovery Essential Comprehensive option for all members, enhanced by 20% together with future pension increases of inflation plus 4% p.a. on each 1 January with the first such increase being on 1 January 2021.

A process needs to be followed to select the final insurer, but until this is done the DMBT should implement a strategy that will hedge the pricing of such a policy against interest rate movements. This will require the Trust to buy the following portfolio of inflation linked bonds:

Inflation-linked Government Bond	Rand million exposure
I2050	168.75
I2046	75.00
I2038	120.00
I2033 or R202	112.50
I2029 or R210	112.50
I2025	75.00
R197	37.50
R212	48.75
Total	750.00

We understand that the inflation linked bond market is narrow and it may not be possible to buy the above portfolio quickly without a material market impact cost. Accordingly, we are comfortable for the Trust to deviate from this schedule provided that the Rand Per Point of the actual portfolio is within 5% of that of the above schedule. We would be pleased to engage with the Party that would be executing the strategy on behalf of the Trust to agree a more specific mandate.

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We believe that the Trustees can reasonably take the view that the proposed insurance policy for members which secures a lifelong pension for the member and his or her dependents, together with guaranteed future pension increases of inflation plus 4% p.a. on each 1 January is an appropriate investment strategy. We say this because such a policy will eliminate investment and longevity risk and is expected to meet Denel SOC's post-retirement medical aid obligation with a very high degree of certainty.

In addition, Denel requests that the balance of the assets be sold and held in a money market portfolio. In this way, the Court papers can provide a degree of certainty about how much money Denel is likely to receive should the High Court indeed approve the arrangement.

Investment vehicle

We understand that the DMBTs current investments are held in a "with profit" annuity with Momentum Metropolitan Life Limited.

We believe it would be beneficial to continue with this arrangement as long as possible and accordingly:

1. It would be beneficial to hold the inflation-linked bonds and money market portfolio in the Momentum policy pending the investment in the group annuity policy. When the premium becomes payable for the group annuity policy this should be discharged by partially surrendering the policy for the inflation-linked bonds that will be required to be transferred under the group annuity policy. We highlight that settling the policy consideration in this manner will reduce its cost because it materially reduces the insurer's implementation risk.
2. Thereafter, once the group annuity policy is acquired, it would be beneficial to continue to hold the remaining balance of the DMBTs assets, including the money market portfolio, in the Momentum policy. The Momentum policy would finally be surrendered if the scheme is implemented following the amendment of the Trust Deed.

As the terms of the Momentum policy envisage only a single surrender, we suggest that it be agreed with the insurer that the policy may partially be surrendered. We expect that the insurer would agree.

We would be pleased to engage with the Trustees further on this matter.



Ant Lester

19 November 2020

AF
K.W

DMBT TRUST DEED AMENDMENTS AS AT 2020.11.19

AP
K. W.

Trust Deed Amendments	
Deletions.	Clause 7.3 and Clause 11.2.2 of the Trust deed are deleted without any consequential changes in the clause numbering.
Clause 3.1. The addition of the following new definitions:	<p>3.12 "Expense Fund"</p> <p><i>Assets of the Trust that are earmarked by the Trustees to meet future expenses of the Trust.</i></p> <p>3.13 "Group Annuity Policy"</p> <p><i>The Group Annuity Policy held by the Trust.</i></p> <p>3.14 "Scheme Active Participant"</p> <p><i>An Employee beneficiary in the active employ of Denel or one of its subsidiaries who has agreed with Denel to be a Scheme Active Participant under the Trust deed.</i></p> <p>3.15 "Scheme Implementation Date"</p> <p><i>A date specified by Denel and notified to the Trustees as the Scheme Implementation Date under the Trust deed.</i></p> <p>3.16 "Scheme Non-Participants"</p> <p><i>An Employee beneficiary who is neither a Scheme Pensioner Participant nor a Scheme Active Participant.</i></p> <p>3.17 "Scheme Pensioner Participant"</p> <p><i>A retired Employee beneficiary who has agreed with Denel to be a Scheme Pensioner Participant under the Trust deed.</i></p> <p>3.18 "Trust Excess Assets"</p> <p><i>At the relevant time, all of the assets of the Trust as at that time, including any income earned by the Trust on such assets, other than (i) the Group Annuity Policy (ii) sufficient cash or securities designated by the Trustees as being required to restore the balance of the Expense Fund to R[insert] or such other amount as may be agreed in writing between Denel and the Trust and (iii) sufficient cash or securities designated by</i></p>

AF
K.W

	<p><i>the Trustees as being required to fund any liabilities of the Trust as at the relevant date other than any liabilities or obligations that are funded or insured under the Group Annuity Policy or to be discharged from the Expense Fund. For this purpose, the Group Annuity Policy will be regarded as fully funding any obligations of the Trust in respect of Scheme Active Participants and Scheme Non-Participants.</i></p>
<p>Clause 5. The addition of the following further paragraphs after the current paragraph:</p>	<p><i>The further main objectives of the Trust are:</i></p> <p><i>(i) to ensure the issue of an individual annuity policy to Employee beneficiaries who choose to receive such a policy and, in so doing, to assist these Employee beneficiaries with post-retirement contributions payable to the Medical Scheme</i></p> <p><i>(ii) to continue to hold, as an asset of the Trust, a group annuity policy to give effect to the original main objective of the Trust (as set out in the first paragraph of clause 5 of the Trust deed) in respect of all of the Employee beneficiaries that do not choose to receive such an individual annuity policy</i></p> <p><i>(iii) to hold all of the excess assets of the Trust (other than the group annuity policy) for the sole benefit of Denel and to distribute the excess assets to Denel.</i></p>
<p>Clause 7. The addition of the following new sub-clauses.</p>	<p><i>7.7 Despite any other provisions in this Trust deed, the Trustees shall have all of the powers required to give effect to the remaining provisions of this clause 7.</i></p> <p><i>7.8 The Trustees shall exercise these powers to give effect to the main objectives of the Trust. This shall include (but not be limited to):</i></p> <p><i>7.8.1 in respect of each Scheme Pensioner Participant, the Trustees shall vest in Denel, on the Scheme Implementation Date, the rights under the Group Annuity Policy in respect of each Scheme Pensioner Participant and shall transfer those rights, by cession, to Denel with effect from the Scheme Implementation Date;</i></p> <p><i>7.8.2 in respect of each Scheme Active Participant, the Trustees shall vest in Denel, on the date on which a Scheme Active Participant retires or on any other date agreed to by Denel and the Scheme Active Participant and notified to the Trustees, the</i></p>

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rights under the Group Annuity Policy in respect of the Scheme Active Participant and shall transfer those rights, by cession, to Denel with effect from that date, provided that if Denel and the Scheme Active Participant agree that Denel will no longer have an obligation to pay or subsidise any medical aid costs in respect of the Scheme Active Participant, the Trustees will, if Denel requires this of the Trustees, surrender the Group Annuity Policy in respect of that Scheme Active Participant and vest in and distribute the surrender proceeds to Denel;

7.8.3 identifying, prior to the Scheme Implementation Date, the Trust Excess Assets as at the Scheme Implementation Date; and

7.8.4 on and from the Scheme Implementation Date holding the Trust Excess Assets for the sole benefit of Denel and, as may be required by Denel from time to time:

7.8.4.1 liquidating all or any of the Trust Excess Assets; and

7.8.4.2 applying the Trust Excess Assets for a purpose designated by Denel; or

7.8.4.3 vesting in, and distributing to Denel, as a beneficiary of the Trust, all or any of the Trust Excess Assets on and with effect from the Scheme Implementation Date, provided that Denel may designate any one or more dates after the Scheme Implementation Date as the date on which any such vesting or distribution is to occur or take effect.

7.9 The Trustees shall, in respect of all Employee beneficiaries of the Trust that are Scheme Non-Participants, continue to administer the Group Annuity Policy in respect of all Scheme Non-Participants in accordance with the original main objective of the Trust as set out in the first paragraph of clause 5 of the Trust deed and in accordance with the other provisions of this Trust deed. The Trust shall terminate once there are no longer any Scheme Non-Participants that are beneficiaries of the Trust.

7.10. As at each financial year end of the Trust following the Scheme Implementation Date and on the termination of the Trust, the Trustees shall identify any further Trust Excess Assets as at that date. The

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	<p><i>provisions of clause [7.8.4] of this Trust deed shall apply to such further Trust Excess Assets, provided that:</i></p> <p><i>7.10.1 the Trustees shall be obliged to vest in and distribute to Denel one half of the further Trust Excess Assets:</i></p> <p><i>7.10.1.1 as at the date of the third financial year end of the Trust following the Scheme Implementation Date; and</i></p> <p><i>7.10.1.2 thereafter every three years as at the relevant financial year end of the Trust; and</i></p> <p><i>7.10.2 once the Trust terminates, the Trustees shall be obliged to vest in and distribute to Denel all of the remaining Trust Excess Assets; and</i></p> <p><i>7.10.3 in addition to the obligations of the Trustees in clause 7.10.1 and clause 7.10.2, the Trustees shall have a discretion, acting on the advice of an actuary appointed by the Trust, to vest in and distribute to Denel all or any of the further Trust Excess Assets as at each financial year end of the Trust.</i></p> <p><i>7.11 On the winding up of the Trust following its termination, all of the assets remaining after discharging the Trust's liabilities and the expenses incurred in the winding-up of the Trust, including any balance in the Expense Fund, shall be paid to Denel.</i></p>
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ASSESSMENT OF BUYOUT OFFER NOTE BY A LESTER

AF
K.W

Assessment of the proposed transaction in respect of the Denel Medical Benefit Trust

Introduction

I have acted as the advisor to the Denel Retired Employees Medical Scheme ("DREMS") Forum in negotiating the proposed transaction to discharge Denel's post-retirement medical aid ("PRMA") obligations.

My initial understanding was that all members of the Denel Medical Benefit Trust ("DMBT") would need to accept the offer if it were to be implemented. However, Denel has now amended the approach so that the transaction may be implemented if not all of the members of the DMBT choose to accept Denel's offer. Denel will retain its PRMA obligations in respect of those members. Those members will also retain their membership of the DMBT.

As part of the transaction, Denel will be approaching the High Court seeking an amendment to the Trust Deed which will provide that the excess assets of the Trust are to be paid out to Denel and that DMBT members that accept the offer will be provided with benefits that exceed the amount of Denel's current PRMA obligations. The assets that are left in the DMBT (mainly a group annuity policy) will continue to be administered by its trustees to meet Denel's PRMA obligations to those who have not accepted Denel's offer.

Consequently, the two aspects we need to deal with in this report are:

- Is the proposed offer fair to members of the DMBT?; and
- Will sufficient assets be left in the DMBT so that the reasonable benefit expectations of the members that remain in the Trust will be met?

The current benefit

At present, Denel owes the DMBT members a PRMA obligation. This obligation is to subsidise a portion of each member's medical aid contribution obligations. The DMBT funds and secures these obligations. At present, the benefit that Denel provides each year increases in line with the increase in the Discovery Health contribution rates. However, it remains possible that Denel will, in the future, seek to change manner in which the benefit increases. This could, for example, occur by agreement with the members of the DMBT .

The offer

The offer to members is as follows:

1. The benefit that will be secured for members is the current PRMA subsidy as at 1 December 2020 but assuming that all members are on the Discovery Health Essential Comprehensive Plan. This means an increase in the benefit for members that have elected a lower cost medical option than the Discovery Essential Comprehensive Plan.
2. The amount in 1 above will then be increased by 20%.
3. The total benefit (i.e. including the 20% enhancement) will then be secured via a life annuity policy issued by an Insurer in the name of the individual member for those members that elect the option .
4. The terms of the individual annuity policy will guarantee a lifelong annuity to the member and his or her dependants increasing on each 1 January by 100% of the annual inflation rate to the preceding 30 September plus 4% p.a.
5. The individual annuity policies will only provide benefits in respect of spouses and children as at the date of the relevant employee's retirement.

6. Once the insurer has issued the member with the policy in the individual's name, the member would look only to the insurer for payment. Denel will have discharged its PRMA obligation to the member and the member would no longer have any interest in the Trust.

The current plan is to backdate the benefits under the group annuity policy and the implementation date of the above to 1 December 2020, irrespective of when the offer is made to members. In this way members that choose the offer can benefit from the increased benefits with effect from an earlier date. In the balance of this note we explain the benefit enhancements as though all of the arrangements were implemented, and the benefit enhancements were paid from 1 December 2020. It must be emphasised that the benefit increases are conditional on the implementation of the entire arrangement. As this can only occur sometime after 1 December 2020, the enhanced benefits will need to be provided as a catch-up payment in the future.

It is always easier to explain by way of example: let us assume that a member has chosen a lower cost option than the Discovery Essential Comprehensive Plan and his or her current PRMA subsidy is R5 000 per month. However, had the member been on the Discovery Essential Comprehensive Plan the subsidy would have been R6 500 per month. A member that accepts the offer will receive a benefit of R7 800 per month (i.e. R6 500 increased by 20%) plus insurer guaranteed annual future increases on 1 January each year of CPI + 4% p.a.

Importantly, for members that elect to remain with the DMBT, the assets of the Trust will be an insurance policy which provides the identical benefit, but with the benefit being paid to the Trust. However, the members' current subsidy will be unchanged. Using the above example, the DMBT will receive R7 800 per month increasing on each 1 January by inflation plus 4% p.a. Nevertheless, the Trust will only pay R5 000 p.m. increasing by the actual increase in the medical aid contribution rate to Discovery Health. In this way the DMBT will continue to build-up a surplus, at least initially, to the extent that the amount received from the Insurer exceeds the amount that is paid to Discovery Health for the remaining members. The proposed amendment to the Trust Deed provides that 50% of any surplus built-up in this way should be paid to Denel every three years, noting that such repatriation can be done more frequently should Trustees exercise a discretion to do so.

Assessment – risks and opportunity for members that elect the buy-out option

Maybe it is best to start with the opportunity that the offer provides for a member that elects the option. From 1 December 2020 onwards he or she will receive a monthly annuity that is at least 20% higher than their current PRMA subsidy. For members that have elected a lower cost option than the Discovery Essential Comprehensive Plan, the additional amount received will be higher.

Furthermore, this pension will increase by 7.0% on 1 January 2020, this being the year-on-year inflation rate to 30 September 2020 (3.0%) plus the 4.0% guaranteed increase. Usefully, Discovery Health has communicated that it will freeze its current contribution rates until 30 June 2021, after which the rates for the balance of 2021 will increase by a maximum of CPI plus 2%. Discovery has indicated that this increase is unlikely to exceed 5.9%. This known information means that the enhancement to a member that chooses the offer is at least 24% from 1 January 2021 calculated as the initial 20% enhancement plus the guaranteed 7% increase on 1 January 2021 less the current subsidy increased 5.9% from 1 July 2021, which when averaged over the year, is rounded to 3%.

Based on the current tax regime, the member will not pay any tax on that part of his/her annuity that is contributed to Discovery Health. However, the part of the annuity that is not paid to the medical scheme, will be taxable income in the member's hands. A member could reduce his or her taxable income by electing a more expensive plan that secures better benefits.

Accordingly, the benefits accruing to a member that chooses to accept the offer are:

1. Additional income of at least 20% for December 2020 and 24% for 2021 which is taxable unless the member elects to apply this amount to secure better medical aid benefits. To give this context, for a member that has one adult dependant, who is on the Discovery Essential Comprehensive Plan and receiving a 67% subsidy, the aggregate of the annuity and subsidy that is to be paid for the 13 months to 31 December 2021 is R108 313.72. If the member elects to remain with the DMBT the aggregate subsidy over the same 13 months will be R87 091.85 (i.e. some R21 221.87 less). Naturally the additional amount for a single member will be lower at R10 907.44 for the 13 months and higher for members with more than one adult dependant.

For members that are on a lower cost option than the Discovery Essential Comprehensive Plan and elect to remain on this option, the additional amount will be higher as will be the amount that is included in taxable income.

2. Certainty of future annuity increase of CPI (year on year to the preceding 30 September) + 4% p.a. on each 1 January on the total lifelong annuity including lives of their dependants. The insurer guarantees the increase in the annuity every year. Future increases to the benefit are no longer subject to Denel's policies and discretion and the possible renegotiation of the PRMA liability.
3. The flexibility to choose what they do with their annuity. If the member elects a lower cost medical aid option, he or she will still receive the same annuity, noting that as per the above any annuity not applied to the medical scheme will be taxable. Similarly, a member may elect a more expensive option, securing better benefits and reducing that member's taxable income. Such flexibility may be valuable to some members.

Naturally, the buy-out offer is not risk-free and the most important risks we have identified are:

- Future medical aid increases exceed inflation plus 4% p.a. However, the 20% enhancement to the current subsidy and the known lower Discovery Health increase for 2021 provides a buffer against much higher medical aid inflation. The table below estimates how many years it would be before the offered annuity is exceeded by medical aid increases above inflation by scenario

Table 1: Years to exceed medical aid increases scenario

Medical aid increase from 2022 onwards	CPI + 4.5%	CPI +5.0%	CPI + 5.5%	CPI + 6% p.a.
Cross-over year	2069	2045	2038	2034

For example, it would take an estimated 25 years for the subsidy to exceed the offered annuity if medical aid inflation exceeds CPI by 5.0% p.a. from 2022 onwards. The reality is that period is longer because the member could invest the difference between the annuity received and the amount paid to the medical scheme and this would provide an additional buffer. It follows from the above that the risk of medical aid inflation exceeding inflation plus 4% p.a. is more acute for younger members (or members that have young adult dependants).

Over the ten year period from 2011 to 2020 the Discovery Essential Comprehensive contribution rate exceeded general inflation by 4.6% p.a. The industry view is that medical aid inflation is expected to exceed inflation by 2% to 3% p.a. in the future. Presumably this estimate is derived from the data which shows that for the 20 years covering the period 2000 to 2009 medical aid inflation across all medical schemes averaged 7.8% p.a. whereas inflation averaged 5.6% p.a.

AF
K.W

Our judgement is that at the boundary of the range of plausible outcomes, medical aid inflation could exceed inflation by 5.5% p.a. i.e. there is a low probability that medical aid inflation will indeed exceed general inflation by more than 5.5% p.a. over the long term. In addition, in the rare event that medical aid inflation is much higher than general inflation we would expect many members to choose a lower medical aid benefit option or for the medical scheme to reduce their benefits so that they remain affordable. We say this because there is a constraint on how much members can, firstly afford to pay and, secondly would be willing to pay, for medical aid benefits. To give context, we estimate that if medical aid inflation exceeds inflation by 5.5% p.a. a member that is currently contributing 15% of his or her total income for medical aid contributions would need to allocate 30% (i.e. double) of his or her money for this purpose in fifteen years' time. If the member were currently allocating 20% of income for medical aid, this would increase to 40% after 15 years i.e. the allocation of income doubles after 15 years.

Naturally, there are scenarios (the outer reaches which are low probability outcomes) where medical aid inflation exceeds general inflation by such a margin that members that opt-out are worse off. This risk is more acute for younger members and members with young adult dependants. However, members can reduce this risk by saving the excess annuity above their medical aid contribution, although we expect that few will do so.

- The insurance company paying the annuity gets into financial difficulty and reduces annuity significantly. This risk is mitigated by the choice of Insurer which will be one of Old Mutual, Sanlam or Momentum Metropolitan who are large insurers with reserves that are currently more than twice the Statutory Capital Requirements. Old Mutual is 175 years old, Sanlam is 102 years old and Momentum has been in business for more than 40 years.

Furthermore, the policy would fall under the class of business known as "non-profit". If an Insurer gets into financial difficulty the first loss is borne by the shareholders, then by policyholders whose policies absorb some of the insurer's financial risks, including to an extent the with-profit policyholders and then only the non-profit policyholders. In our opinion it would take an extreme event for an insurer like Old Mutual, Sanlam or Momentum to burn through so much capital and adaptive buffers that they would need to reduce the benefits of non-profit policyholders.

- The last risk we would identify is a legislative change which adversely affects policyholders, with the same legislation not being applicable to the DMBT. Again, we would assess this to be a very low probability event. If anything, the risk of legislative changes adversely affecting benefits of the DMBT are higher as the tax status of Trusts are routinely under review. Furthermore, it is not straightforward to change the Trust Deed to mitigate the impact of any legislation change and it is most likely that the High Court would need to approve any such changes.

Our sense is that the best way to consider the buy-option is to answer the question: "If my parents were provided with this buy-out offer, would I recommend that they accepted it?" Our answer is that we would counsel our parents to accept the buy-out offer as we assess that there is a high chance that they will better off. Of course, there are scenarios where they can be worse off, but in our view this falls into the outer reaches of potential outcomes which have a low probability. We suspect that the main reason for members not to accept the offer is that they are anxious about change and are concerned that they don't understand all the issues fully.

The position of members that elect to stay with the DMBT

As explained previously, the proposed transaction for members that remain in the DMBT is for the DMBT continue to hold a group annuity policy that provides for exactly the same benefits as for members that elect the buy-out offer. However, the key difference is that the DMBT will only pay across to Discovery Health the member's current PRMA subsidy (unless Denel renegotiates this provision), with any subsequent increases thereon. This means that the member does not receive any part of the enhancement.

AF
X-J

For this reason, at least in the early years, the DMBT will receive more income than what it needs to pay away to Discovery. This surplus will be invested by the DMBT and 50% of the amount so accumulated has to be returned to Denel every three years. The three year period was chosen to correspond to the statutory period for the actuarial valuation of defined benefit arrangements, which is the nature of the PMRA liability. In addition, the Trust Deed will be amended to allow for more regular repatriation of surplus if the Trustees resolve to do so, which we assume would only happen if the DMBT's actuary certifies that it is prudent to do so.

Members that elect to remain in the DMBT face the same risks as members that choose the buy-out option, albeit that these risks are lower. We say this for the following reasons:

1. The Trust will build-up a reserve equal to 50% of the excess benefits received from the policy compared to the actual subsidies it pays. Such excess assets can be invested thus earning a return, but at the end of each three years 50% of the reserve will be paid-out to Denel.. Effectively this means that the reserve the DMBT will build-up over time is 50% of the aggregate excess amount accumulated with investment returns.

Should the subsidy exceed the policy proceeds, the reserve can be used to finance the shortfall to the extent that the Trust is able to do so. As highlighted above, in theory a member that accepts Denel's offer could invest the entire excess, but very few are likely to opt to do so and unlike the Trust, the investment return will not be tax-free.

2. The terms of the life annuity policy that the Trust holds will provide for termination on favourable terms for specified breaches including if the Insurer's solvency reserve margin drops below an agreed level. Thus, in the unlikely event that the Insurer starts moving towards a situation where their financial soundness may come under pressure, the Trust will be able to exit the investment. The same right to terminate will not apply to members that opt out of the Trust.
3. Finally, for members that elect to remain with the Trust, the Denel PRMA obligation is unchanged. Accordingly, Denel would need to negotiate in good faith any reduction in the subsidy should the Trust have insufficient assets to meet the subsidy requirement in future. Naturally, for members that have opted-out of the DMBT no such negotiation is required and the member's benefit is the amount paid by the Insurer.

It is obvious that the higher assets the Trust has, the less likely it is that it will have insufficient money to pay the PRMA subsidy in future. By returning some R750 million of the Trust's assets to the Company, the security of benefits for members is reduced, albeit in our opinion, only slightly.

What the term "reasonable benefit expectation" means has never been defined by the Courts. However, most agree that a reasonable expectation means more than a 50% chance of the outcome and some have suggested that to be "reasonable" the chance of the targeted outcome must be at least 80%. Our analysis suggests that the chances of the Trust being able to finance the Denel PRMA liability from the insurance policy only on the terms described above comfortably meets this threshold.

Summary and conclusion

In our opinion, the proposed offer to the members of the DMBT falls into the category of generous. Naturally there are circumstances in which the member that elects this option is worse off than if they remained in the Trust, but we assess this to be a low probability outcome. On the other hand, there is better than a 50% chance that the member that elects this option will be better off, particularly if one takes the view that medical aid inflation is unlikely to exceed general inflation by more than 5.5% p.a. over the long term and if this happens members, in any way, would move to lower cost benefit options simply on the basis of affordability or medical aid providers will reduce benefits to keep their product options affordable.

It follows that we are also of the opinion that the Trust will be able to meet the reasonable benefit expectations of members that remain in the Trust with a high probability.



Ant Lester

19 November 2020



**MEDICAL BENEFIT TRUST**

Mr T Sadik
Acting Chief Executive Officer: Denel SOC Limited
Nellmapius Drive
P O Box 8322
CENTURION
0046

25 November 2020

Dear Mr Sadik

ALTERNATIVE OFFER TO BENEFICIARIES CURRENTLY ENTITLED TO RECEIVING A POST-RETIREMENT MEDICAL AID SUBSIDY ON RETIREMENT

We refer to your documentation recently received regarding the above and wish to comment as follows on the following items.

Change to investment strategy

It is opportune for the Trustees to review the Trust investment Strategy in consultation with the Trust's Investment Consultant, Actuary and current Policy Holder (MMI) and may consider your proposal after discussion with the said Consultants, who assist the Trustees with key investment decisions.

Trust Deed Amendments

We cannot comment to the request because we are not a party to this exercise. Furthermore, we can also not comment on the R 10 million expense budget as requested because we are in no position and cannot envisage how many beneficiaries will decide to remain in the Trust by not accepting the said offer.

We can also not comment to the content of the draft DREMS Forum letter.

Your faithfully

On behalf of HM IVY
CHAIRPERSON

U:\Lubbe\RIA\Denel Med Benefit Trust\Letter to Forum 2020 11 25

Matthew Scorgie

From: Jacques Van der Merwe <Jacquesvdm@retfunds.co.za>
Sent: 15 March 2021 06:38 AM
To: Gawie Van Zyl; William Hlakoane
Cc: Hugo Ivy; twelibanzi1@gmail.com
Subject: FW: DENEL MEDICAL BENEFIT TRUST: PROPOSAL TO AMEND THE TRUST'S INVESTMENT STRATEGY
Attachments: doc00021920210312172820.pdf

Hi Gawie

We refer to your enquiry below and *attached* herewith the Trustees' response in this respect.

Regards

P J VAN DER MERWE
PRINCIPAL OFFICER

Tel: 010 549 1101
 E-mail: jacquesvdm@retfunds.co.za
 3CX Video Conference Facility: <https://retfunds-za.3cx.net/webrtc/join/jacquesvandermerwe>
<https://meet.dachserwarehouse.co.za/JVD>

From: Gawie Van Zyl <Gawiev@denel.co.za>
Sent: Thursday, 11 March 2021 14:27
To: Jacques Van der Merwe <Jacquesvdm@retfunds.co.za>
Cc: Themba B. Zwelibanzi <thembaz@denel.co.za>; William Hlakoane <Williamh@denel.co.za>; Gawie Van Zyl <Gawiev@denel.co.za>
Subject: RE: DENEL MEDICAL BENEFIT TRUST: PROPOSAL TO AMEND THE TRUST'S INVESTMENT STRATEGY

Dear Jacques

Our various discussions and correspondence refer

As Denel (Gawie and William) we would like to engage with the Trustees on the matter of support from you on the buying of policy once the courts have made their decision on the proposed amendments.

We do respect the Trustee's view on this matter and our intention is not to put undue pressure or be prescriptive to the trustees in this meeting.

Our conundrum is however that the court will not provide guidance or issue a ruling on the investment strategy, but will require assurance that the benefits promised to the beneficiaries will realise once the ruling is made.

Hope that we can find some way forward on this matter, as our legal advice is that without this assurance our probability of success is decreased significantly.

From: Gawie Van Zyl <Gawiev@denel.co.za>
Sent: Thursday, 25 February 2021 16:31
To: Carmen Le Grange <CarmenL@denel.co.za>; William Hlakoane <Williamh@denel.co.za>; Jacques Van der Merwe <Jacquesvdm@retfunds.co.za>; paultjie@gmail.com; potties@iafrica.com

Cc: Gawie Van Zyl <Gawiev@denel.co.za>

Subject: RE: DENEL MEDICAL BENEFIT TRUST: PROPOSAL TO AMEND THE TRUST'S INVESTMENT STRATEGY

Dear Jacques

Thank you for the response

We do respect the position of the Trustees on this matter, however it does negatively impact on our chances of success with the court, which we believe is in the interest of Denel and all the beneficiaries.

We request an opportunity to engage with the Trustees and the advisor NMG to firstly understand the reason behind the decision and also communicate why we believe the proposed action will be to the benefit of all.

Our availability is as below and we will appreciate if you can avail yourselves and call on NMG to be available accordingly

Monday between 11.30 and 1.30pm

Monday between 3pm and 4pm

Tuesday all day until 2.45pm

Wednesday all day until 3.45pm

From: Jacques Van der Merwe [<mailto:Jacquesvdm@retfunds.co.za>]

Sent: 22 February 2021 03:07 PM

To: Marietjie Strydom

Cc: Themba B. Zwelibanzi

Subject: DENEL MEDICAL BENEFIT TRUST: PROPOSAL TO AMEND THE TRUST'S INVESTMENT STRATEGY

Dear Ms Strydom

Please refer to the *attached* document which relates to the above-mentioned issue at hand.

Regards

P J VAN DER MERWE

PRINCIPAL OFFICER/TRUSTEE: DENEL MEDICAL BENEFIT TRUST

Tel: 010 549 1101

E-mail: jacquesvdm@retfunds.co.za

3CX Video Conference Facility: <https://retfunds-za.3cx.net/webrtc/join/jacquesvandermerwe>

<https://meet.dachserwarehouse.co.za/JVD>

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MEDICAL BENEFIT TRUST

Mr W Hlakoane
Acting Chief Executive Officer: Denel SOC Limited
Nellmapius Drive
P O Box 8322
CENTURION
0046

12 March 2021

For Attention: Mr G Van Zyl

Dear Mr Hlakoane

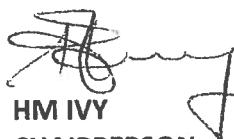
AMENDMENT TO INVESTMENT STRATEGY OF THE TRUST PROPOSED BY DENEL

We refer to the request of your Mr Van Zyl for a special meeting to further discuss the proposed amendment to the Trust's current investment strategy to be in principle approved by the Trustees.

We have also noted your so-called "conundrum" that the Court will not provide guidance or issue a ruling on the investment strategy, but will require assurance that the benefits promised to the beneficiaries will realise once the ruling is made.

In light of the above, we kindly refer you to our letter dated 18 February 2021 in which we have confirmed that we will honour and implement the implications of the final ruling of the Court, and as result, wish to confirm that we do not have anything more to add and cannot envisage that a meeting will change our initial collective decision in this respect.

Your faithfully



HM IVY
CHAIRPERSON

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MEDICAL BENEFIT TRUST

Mr W Hlakoane
Acting Chief Executive Officer: Denel SOC Limited
Nellmapius Drive
P O Box 8322
CENTURION
0046

18 February 2021

Dear Mr Hlakoane

AMENDMENT TO INVESTMENT STRATEGY OF THE TRUST PROPOSED BY DENEL

We refer to your documentation recently received regarding the proposed amendment to the Trust's current investment strategy.

We wish to confirm that the Investment Consultant and Actuary of the Trust were tasked to review the proposed amendment of the Trust's investment strategy compiled by Willis Towers Watson and to advise the Trustees on the feasibility and impact thereof on the future direction of the Trust.

Within the context of the advice received from our Consultants, we are of the opinion that the implementation of the proposed strategy is premature at this stage and should not be considered before a final ruling is issued by the Court in respect of Denel's envisaged course of action regarding the future of the post-retirement medical subsidies funded through the Denel Medical Benefit Trust.

Your faithfully



HM IVY
CHAIRPERSON

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DENEL GROUP

Office of the Group CEO

Tel: +27 12 671 2758

williamh@denel.co.zamarietjies@denel.co.za

Ref 19 2804 DMBT Letter to Trustees

The Trustees

Denel Medical Benefit Trust

Dear Trustees

POST-RETIREMENT MEDICAL AID OBLIGATION OF DENEL SOC LIMITED: ALTERNATIVE OFFER TO CURRENT AND FORMER EMPLOYEES

1. We refer to our ongoing correspondence in relation to this matter and, in particular, to the application that Denel will make to the High Court to amend the trust deed of the Denel Medical Benefit Trust ("DMBT").
2. We write to inform you of the following:
 - 2.1 Denel's application will be brought to court in two parts:
 - 2.1.1 In the first stage, Denel will apply on an *ex parte* basis for a rule *nisi* calling on interested parties to show cause on the return day why the DMBT trust deed should not be varied (the *rule nisi* will not have interim effect) and an order granting Denel leave to serve the *rule nisi*, the notice of motion and the founding affidavit on the trustees and the members of the trust by substituted service.
 - 2.1.2 The second stage will occur on the return day, when Denel will ask that the rule *nisi* be made final and the proposed amendments to the trust deed effected in terms of section 13 of the Trust Property Control Act. Any interested party will have a full opportunity on the return day to oppose the order that Denel will seek if they are minded to do so.
 - 2.2 The amendments that Denel will seek are no longer the same as those communicated in our letter of 19 November 2020. We attach the current draft of the envisaged amendments to this letter. The changes to those provided to the Trustees with our 19 November 2020 letter are tracked. You will note that the changes to the amendments include a number of provisions

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 P O Box 8322, Centurion, 0046, South Africa. Tel: +27 (0)12 671 2700, Fax: +27 (0)12 671 2751
 Directors: Mrs G T Serobe (Acting Chairperson), Mr T H Magazi, Lt Gen. (Ret) T T Matanzima, Mr M M Mnisi,
 Mr K W Hlakoane¹ (Interim Group Chief Executive Officer), Ms T Sabela¹ (Interim Group Chief Financial Officer)

¹ Ex-Officio Director
 Group Company Secretary: FluidRock Co Sec (Pty) Ltd

Handwritten initials: E.W.
 AF

requiring the Trustees to acquire a group annuity policy once the amendments to the trust deed have taken effect.

- 2.3 The final draft amendments must be included in Denel's court papers when Denel launches its application. Denel proposes to launch its application once its papers are ready, which will not be before 4 May 2021.
3. We remain available to discuss any aspect that you wish to discuss in relation to the proposed amendments.
4. Denel has been advised that it will be necessary to serve Denel's application on the Trustees. Denel proposes to do so by email to the Principal Officer of the DMBT and would be grateful for your confirmation that this is in order and for this confirmation to be received by close of business on 3 May 2021.

We look forward to hearing from you.

Yours sincerely



William Hlakoane
INTERIM GROUP CHIEF EXECUTIVE OFFICER
DENEL SOC LTD

Date 28 April 2021

ATTACHMENT 2.2

DMBT TRUST DEED AMENDMENTS (TRACKS OF VERSIONS TO TRUSTEES) AS AT 2021.04.23

AK
AK

Trust Deed Amendments	<u>Draft of 23 April 2021 to Trustees</u>
Deletions.	Clause 7.3 and Clause 11.2.2 of the Trust deed are deleted without any consequential changes in the clause numbering.
Clause 3.1. The addition of the following new definitions:	<p>3.12 "Expense Fund"</p> <p><u>Assets of the Trust that are earmarked by the Trustees to meet futurethe expenses of the Trust after the Scheme Implementation Date.</u></p> <p>3.13 "Group Annuity Policy"</p> <p><u>The Group Annuity Policy to be acquired and held by the Trust.</u></p> <p>3.14 3.14 "Group Annuity Policy Criteria"</p> <p><u>3.14.1 Subject to clause 3.14.2, each of the following.</u></p> <p><u>3.14.1.1 The insurer will be an insurer that is identified by the Trustees and approved in writing by Denel, provided that Denel's approval of the insurer will not be required if the insurer is one of Old Mutual Life Assurance Company (South Africa) Limited, Momentum Metropolitan Life Limited and Sanlam Life Insurance Limited.</u></p> <p><u>3.14.1.2 The benefits under the policy will be paid in respect of all of the Employee beneficiaries (including Recognised Dependants) that are named in the policy.</u></p> <p><u>3.14.1.3 The benefits under the policy will be an annuity equal to 120% of the benefits that are required to be paid in terms of Denel's current subsidy policy on the basis that all beneficiaries are on the Discovery Health Essential Comprehensive option even if they do not belong to the Discovery Health Medical Scheme or have not opted for the Essential Comprehensive option (determined on the basis of the cost as at the date of the issue of the policy or such earlier date that Denel may specify)</u></p> <p><u>3.14.1.4 The annuity will increase in January every year by CPI + 4% using the CPI published in respect of October in the preceding year, subject to a minimum inflation rate of 0%. In the event of deflation, the</u></p>

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increase will be 4%, but the cumulative increases since date of the issue of the policy will not exceed CPI + 4% p.a. This means that the insurer will "clawback" the impact of setting inflation at a minimum of 0% where there has been deflation.

3 14.1.5 The annuity and the annual increases are to be guaranteed by the insurer.

3 14.1.6 The policy must confer on the policyholder (the Trust or, pursuant to a transfer of these rights by the Trust, Denel) a right to surrender the entire policy or part of the policy insofar as it relates to an Employee beneficiary.

3 14.1.7 The rights of the policyholder under the policy in respect of each Employee beneficiary will be capable of transfer by the Trust to Denel in one or more transfers from time to time, without any requirement that the insurer consents or agrees to that transfer.

3 14.1.8 The policy will provide for an individual annuity policy to be issued to the relevant Employee beneficiary if this is required by the policyholder (the Trust or, pursuant to a transfer of these rights by the Trust, Denel). The individual annuity policy will not include a right to surrender the individual annuity policy.

3 14.1.9 No subsequent marriage or remarriage will be provided for. Except for disabled children the children's subsidy will cease at an age of 25 years.

3 14.1.10 The policy terms, including the amount and manner of discharge of the policy premium and the terms that will apply to any individual annuity policies that are issued, must be approved by Denel in writing prior to the Trust concluding the policy.

3 14.2 Despite any provision of clause 3 14.1

3 14.2.1 Denel and the Trustees may agree in writing to any variation of or departure from any of the criteria in clause 3 14.1 and

3 14.2.2 once Denel gives the approval that is contemplated in clause 3 14.1.10, the policy that is acquired by the Trustees shall be deemed to comply with all of the criteria in clause 3 14.1

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3.15 "Group Annuity Policy Acquisition Date"

A date specified by Denel and notified to the Trustees as the date by which the Trust must have acquired the Group Annuity Policy and discharged the obligation to pay the premium to the insurer under the Group Annuity Policy. The date specified by Denel shall not be less than 10 calendar days from the date of Denel's notice to the Trustees and shall not be less than 30 calendar days after the amendment to the Trust deed to include this clause 3.15 takes effect. The date so specified may be extended from time to time by Denel by notice to the Trustees.

3.16 "Recognised Dependant"

In relation to a deceased Employee beneficiary, a dependant of that Employee beneficiary who is recognised by the Trust and Denel as a continuation and widow(er) member of the Trust.

3.17 "Scheme Active Participant"

An Employee beneficiary in the active employ of Denel or one of its subsidiaries who at any time has agreed concluded an agreement with Denel (that has not been terminated) to be a Scheme Active Participant under the Trust deed.

3.18 "Scheme Implementation Date"

A date specified by Denel and notified to the Trustees as the Scheme Implementation Date under clause 7.8 of the Trust deed. The date specified by Denel shall not be less than 5 calendar days after the Group Annuity Policy Acquisition Date. The date so specified may be extended from time to time by Denel by notice to the Trustees.

3.19 "Scheme Non-Participants"

An Employee beneficiary who (including for the avoidance of doubt a Recognised Dependant) who at any relevant time is neither a Scheme Pensioner Participant nor a Scheme Active Participant.

3.20 "Scheme Pensioner Participant"

A retired Employee beneficiary (including for the avoidance of doubt a Recognised Dependant) who at any time has agreed concluded an

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	<p><u>agreement with Denel (that has not been terminated) to be a Scheme Pensioner Participant under the Trust deed.</u></p> <p>3.4821 "Trust Excess Assets"</p> <p><i>At the relevant time, all of the assets of the Trust as at that time, including any income earned by the Trust on such assets, other than (i) the Group Annuity Policy (ii) sufficient cash or securities designated by the Trustees as being required to restore the balance of the Expense Fund to R100 million <u>R20 million</u> or such other amount as may be agreed in writing between Denel and the Trust and (iii) sufficient cash or securities designated by the Trustees <u>acting on the advice of an actuary appointed by the Trust</u> as being required to fund any liabilities of the Trust as at the relevant date other than any liabilities or obligations that are funded or insured under the Group Annuity Policy or to be discharged from the Expense Fund. For this purpose, the Group Annuity Policy will be regarded as fully funding any obligations of the Trust in respect of Scheme Active Participants and Scheme Non-Participants.</i></p>
<p>Clause 5. The addition of the following further paragraphs after the current paragraph:</p>	<p><i>The further main objectives of the Trust are:</i></p> <p>(i) to ensure the issue of an individual annuity policy to Employee beneficiaries who choose to receive such a policy and in so doing to assist these Employee beneficiaries with post-retirement contributions payable to the Medical Scheme</p> <p>(ii) to continue (i) to hold, as an asset of the Trust, a group annuity policy to give effect to the original main objective of the Trust (as set out in the first paragraph of clause 5 of the Trust deed) in respect of all of the Employee beneficiaries that do not choose to receive such an individual annuity policy (including for the avoidance of doubt Recognised Dependants).</p> <p><u>(ii) to ensure the issue of an individual annuity policy to Employee beneficiaries (including for the avoidance of doubt Recognised Dependants) who choose to receive such a policy and in so doing to assist these Employee beneficiaries with post-retirement contributions payable to the Medical Scheme on the basis that once such an individual annuity policy has been issued, the individual annuitant will no longer be an Employee beneficiary of the Trust.</u></p>

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	<p><i>(iii) to hold all of the excess assets of the Trust (other than the group annuity policy and an appropriate allowance for expenses) for the sole benefit of Denel and to distribute the excess assets to Denel.</i></p>
<p>Clause 7. The addition of the following new sub-clauses.</p>	<p><i>7.7 Despite any other provisions in this Trust deed, the Trustees shall have all of the powers required to give effect to the remaining provisions of this clause 7.</i></p> <p><i>7.8 The Trustees shall exercise these powers to give effect to the main objectives of the Trust. This shall include (but not be limited to):</i></p> <p><i><u>7.8.1 the Trustees shall ensure that they acquire the Group Annuity Policy and discharge the obligation to pay the premium to the insurer prior to the Group Annuity Policy Acquisition Date and that</u></i></p> <p><i><u>7.8.1.1 the benefits and other terms of the Group Annuity Policy are consistent with the Group Annuity Policy Criteria, the main objectives of the Trust and the other provisions of this Trust deed, and</u></i></p> <p><i><u>7.8.1.2 the process to select the insurer under the Group Annuity Policy and to determine the amount of the premium payable by the Trust under the Group Annuity Policy is, as between the participants in the process, consistent with the principles of fairness, equitability, transparency, competitiveness and cost-effectiveness.</u></i></p> <p><i>7.8.2 in respect of each Scheme Pensioner Participant, the Trustees shall vest in Denel, on the Scheme Implementation Date, the rights under the Group Annuity Policy in respect of each Scheme Pensioner Participant and shall transfer those rights, by cession, to Denel with effect from the Scheme Implementation Date;</i></p> <p><i>7.8.23 in respect of each Scheme Active Participant, the Trustees shall vest in Denel, on the date on which a Scheme Active Participant retires or on any other date agreed to by Denel and the Scheme Active Participant and notified to the Trustees, the rights under the Group Annuity Policy in respect of the Scheme Active Participant and shall transfer those rights, by cession, to Denel with effect from that date, provided that if</i></p>

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Denel and the Scheme Active Participant agree that Denel will no longer have an obligation to pay or subsidise any medical aid costs in respect of the Scheme Active Participant, the Trustees will, if Denel requires this of the Trustees, surrender the Group Annuity Policy in respect of that Scheme Active Participant and vest in and distribute the surrender proceeds to Denel;

~~*7.8.4*~~ *7.8.4 in respect of any Scheme Non-Participant with whom Denel agrees after the Scheme Implementation Date that Denel will no longer have an obligation to pay or subsidise any medical aid costs in respect of the Scheme Non-Participant the Trustees shall either as Denel may require of the Trustees*

~~*7.8.4.1*~~ *surrender the Group Annuity Policy in respect of that Scheme Non-Participant and vest in and distribute the surrender proceeds to Denel, or*

~~*7.8.4.2*~~ *vest in Denel, on a date specified by Denel, the rights under the Group Annuity Policy in respect of that Scheme Non-Participant and shall transfer those rights, by cession, to Denel with effect from that date.*

~~*7.8.5*~~ *identifying, prior to the Scheme Implementation Date, the Trust Excess Assets as at the Scheme Implementation Date; and*

~~*7.8.46*~~ *on and from the Scheme Implementation Date holding the Trust Excess Assets for the sole benefit of Denel and, as may be required by Denel from time to time.*

~~*7.8.46.1*~~ *liquidating all or any of the Trust Excess Assets in consultation with Denel, and*

~~*7.8.46.2*~~ *applying the Trust Excess Assets for a purpose designated by Denel; or*

~~*7.8.46.3*~~ *vesting in, and distributing to Denel, as a beneficiary of the Trust, all or any of the Trust Excess Assets on and with effect from the Scheme Implementation Date, provided that Denel may designate any one or more dates after the Scheme*

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Implementation Date as the date on which any such vesting or distribution is to occur or take effect.

7.9 The Trustees shall, in respect of all Employee beneficiaries of the Trust (including for the avoidance of doubt Recognised Dependants) that are Scheme Non-Participants, continue to administer the Group Annuity Policy in respect of all Scheme Non-Participants in accordance with the original main objective of the Trust as set out in the first paragraph of clause 5 of the Trust deed and in accordance with the other provisions of this Trust deed. The Trust shall terminate once there are no longer any Scheme Non-Participants that are beneficiaries of the Trust.

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7.10. As at each financial year end of the Trust following the Scheme Implementation Date and on the termination of the Trust, the Trustees shall identify any further Trust Excess Assets as at that date. The provisions of clause [7.8.4] of this Trust deed shall apply to such further Trust Excess Assets, provided that:

7.10.1 the Trustees shall be obliged to vest in and distribute to Denel one half of the further Trust Excess Assets:

7.10.1.1 as at the date of the third financial year end of the Trust following the Scheme Implementation Date; and

7.10.1.2 thereafter every three years as at the relevant financial year end of the Trust; and

7.10.2 once the Trust terminates, the Trustees shall be obliged to vest in and distribute to Denel all of the remaining Trust Excess Assets; and

7.10.3 in addition to the obligations of the Trustees in clause 7.10.1 and clause 7.10.2, the Trustees shall have a discretion, acting on the advice of an actuary appointed by the Trust, to vest in and distribute to Denel all or any of the further Trust Excess Assets as at each financial year end of the Trust.

7.11 On the winding up of the Trust following its termination, all of the assets remaining after discharging the Trust's liabilities and the expenses incurred in the winding-up of the Trust, including any balance in the Expense Fund, shall be paid to Denel.

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REGLEMENT

VAN

DENEL MEDIESE BYSTANDSFONDS

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1. *NAAM*

Die naam van die Fonds is die *DENEL MEDIESE BYSTANDSFONDS* (hierina die Fonds genoem) wat geadministreer te word ooreenkomstig die bepalings van die reëls.

2. *REGSPERSOONLIKHEID*

Die Fonds is bevoeg om in sy eie naam eisend en verwerend op te tree en om roerende en onroerende eiendom te bekom, te besit en te vervreem.

3. *KANTOOR*

Die kantoor van die Fonds is geleë te

Denelgebou
 Jochemusstraat
 ERASMUSKLOOF
 PRETORIA

of op sodanige ander plek as wat die Trustee van tyd tot tyd kan bepaal.

4. *WOORDOMSKRYWINGS*

Woorde dra die normale betekenis wat daaraan geheg word, en tensy dit strydig is met die samehang, sluit alle woorde en uitdrukkings wat op die manlike geslag betrekking het, die vroulike geslag in en sluit die woorde in die enkelvoud ook die meervoud in, en omgekeerd, en het die volgende uitdrukkings die volgende betekenis :

4.1 *Aanvangsdatum*

1 April 1992.

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4.2 "Bydrae"

Enige bedrag wat die Fonds mag ontvang by wyse van donasie, skenk-
ing, bemaking of andersins.

4.3 "Denel"

Denel (Edms) Bpk, 'n maatskappy geïnkorporeer ingevolge die Maat-
skappywet, 1973, soos gewysig, en al sy divisies sowel as sy filiaal-
maatskappye.

4.4 "Lid"

'n Lid is 'n werknemer en afgetrede werknemer van Denel wat 'n lid
is van Denel se Mediese skema.

4.5 "Mediese skema"

UMED, 'n Mediese skema geregistreer kragtens die bepalings van die
Wet op Mediese Skemas (72 van 1967, soos gewysig) van 4de Vloer,
Pencardiagebou Nr 1, Pretoriusstraat 509, Arcadia, Pretoria of 'n
vervangende mediese skema wat kragtens die bepalings van die Wet
op Mediese Skemas geregistreer is, wat deur Denel (Edms) Bpk vir
sy werknemers, of lede van UMED of werknemers van sy filiaalmaat-
skappye en divisies mag oprig of aanstel of nomineer.

4.6 "Ouditeur"

Die Eksterne Ouditeure van Denel (Edms) Bpk.

4.7 "Reëls"

Die reëls van die Fonds, soos vervat in hierdie dokument, betreffende
voordele wat deur die Fonds verleen kan word.

4.8 "Trustee"

Die Trustee wat kragtens reël 9 aangestel is om die sake van die
Fonds te behartig.

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5. DOELSTELLING

Die doel van die Fonds is om vanaf die aanvangsdatum 'n fonds daar te stel deur middel van skenkings, donasies, bemakings of andersins ontvang, om voorsiening te maak vir die verlening van finansiële bystand aan lede om mediese en aanverwante uitgawes te bestry of te verlig deur tekorte op die mediese eise van die lid wat by Mediese skema ingedien is aan te vul tot voordeel van die lid

6. BYDRAE TOT FONDS

Enigeen kan vrywillig 'n donasie, skenking of andersins maak aan die Fonds. Die feit dat iemand 'n donasie of skenking maak of andersins bydra, sal onder geen omstandighede vertolk word as sou sodanige "bydraer" 'n reg op enige voordeel bekom nie.

7. AANWENDING VAN FONDSINKOMSTE EN -BATES

Al die inkomste en bates van die Fonds, ongeag die bron daarvan, word uitsluitlik aangewend vir die doelstellings van die Fonds, en geen gedeelte daarvan mag hoegenaamd, direk of indirek, by wyse van 'n verdeling, dividend, bonus of andersins aan of tot voordeel van iemand anders as die lede of hul afhanklikes aangewend word nie. Met dien verstande dat niks hierin bepaal verhoed dat die Fonds ter goeder trou redelike besoldiging aan enige werknemer of trustee van die Fonds kan betaal ter vergoeding van dienste wat sodanige persoon inderdaad aan die Fonds gelewer het.

8. WYSE WAAROP AANSOEK GEDOEN WORD VIR VOORDELE

- 8.1 Die lid moet 'n eis instel by die Mediese skema wat deur die Fonds goedgekeur sal word.
- 8.2 Die Mediese skema sal die administrasie van die eise vir voordele deur lede namens die Fonds administreer.
- 8.3 'n Administrasiefooi sal deur die Fonds aan die Mediese skema betaal word soos van tyd tot tyd ooreengekom met die Mediese skema.



9. WYSE WAAROP VOORDELE TOEGEKEN WORD

- 9.1 Alle toekennings word *ex gratia* gedoen aan of ten behoeve van enig-
een wat 'n lid of afhanklike is, uit hoofde van 'n Trusteebesluit, en
onderworpe aan die reëls soos hierin uiteengesit.
- 9.2 Alle toekenning en verdeling van die Fondsinkomste en Fondsbates
vind plaas na goeëdunke van die Trustees en die Trustees kan in-
komste en trustbates volgens hulle absolute diskresie en op sodanige
tydstip as wat hulle goed dink aan die lede toeken.
- 9.3 Die Trustees is verplig om die fondsinkomste en bates uitsluitlik aan
te wend vir die doeleindes in klousule 5 vermeld en mag dit onder
geen omstandighede vir enige ander doel aanwend nie.
- 9.4 Enige toekenning deur die Trustees aan die lede kan uitbetaal word
in kontant of by wyse van 'n oordrag na 'n rekening wat ten behoeve
van die lede deur UMED geadministreer word namens die Fonds.

10. BESTUUR

Die sake van die Fonds word kragtens hierdie reëls bestuur deur 'n Raad van
Trustees van minstens 3 en hoogstens 8 persone soos van tyd tot tyd deur
Denel vasgestel en aangestel.

11. TRUSTEES

11.1 *Aanstelling van Trustees*

- 11.1.1 Die Trustees aangestel in terme van klousule 9 van hierdie
ooreenkoms sal as die Eerste Trustees van die Fonds dien.
- 11.1.2 Daar moet te alle tye ten minste 3 (drie) Trustees in die
amp wees en indien die aantal Trustees, om welke rede
ookal benede die vereiste minimum daal, word die getal
binne 60 (sestig) dae deur die oorblywende Trustee aan-
gevol met dien verstande dat alleenlik persone wat deur die
direksie van Denel goedgekeur is, as Trustees genomineer
en aangestel mag word. Tot tyd en wyl die vakature gevul



is, is die oorblywende Trustee gemagtig om alle magte van die Trustees uit te oefen vir die behoud van die Fondsbates.

- 11.1.3 Geen aanstelling of benoeming van 'n Trustee is van enige krag alvorens dit deur die aangestelde of benoemde Trustee skriftelik aanvaar is nie.

11.2 *Beëindiging van die Amp van Trustee*

Die amp van 'n Trustee word onmiddellik en sonder verdere kennisgewing of tussenkoms van die Hof beëindig en die Fondsbates hou op om in 'n Trustee te vestig, indien -

- 11.2.1 die Trustee bedank deur skriftelike kennisgewing tot dien effekte aan sy mede Trustee te gee; of
- 11.2.2 as hy geestelik versteurd of swaksinnig raak; of
- 11.2.3 as hy om enige rede onbevoeg of onbekwaam is om as Trustee op te tree; of
- 11.2.4 as sy boedel gesekwestreer word, hetsy voorlopig of finaal, of as hy 'n kompromie met sy skuldeisers aangaan of 'n daad van insolvensie pleeg; of
- 11.2.5 as hy kragtens die Maatskappywet wat van tyd tot tyd van krag is gediskwalifiseer is om as direkteur van 'n maatskappy op te tree.

11.3 *Verrigtinge van die Trustees*

- 11.3.1 Mits die Trustees deurgaans gevolg gee aan die doelstellings van die Fonds en onderhewig aan die Trustees se vertrouenspligte, is die Trustees geregtig om in die behartiging en administrasie van die sake van die Fonds sodanige administratiewe prosedures te volg as wat die Trustees van tyd tot tyd mag bepaal.
- 11.3.2 Enige Trustee is geregtig om 'n vergadering van die



Trustees met 7 (sewe) dae skriftelike kennisgewing aan die ander Trustee(s) byeen te roep.

- 11.3.3 Die vereiste kworum vir 'n vergadering van Trustees is 3 (drie) Trustees.
- 11.3.4 Indien daar 10 (tien) minute nadat 'n vergadering aanvang geneem het nie die vereiste kworum van Trustees teenwoordig is nie, verdaag die vergadering van Trustees vir 'n periode van ten minste 3 (drie) dae en vergader op 'n datum, tyd en plek wat deur die Trustees by die verdaagde vergadering vasgestel word en waarvan aan alle Trustees skriftelik kennis gegee word. Die kworum vereiste vir sodanige verdaagde vergadering is 3 (drie) Trustees.
- 11.3.5 Behoudens enige uitdruklike bepalings van die ooreenkoms tot die teendeel word alle besluite en optredes van die Trustees geneem en gedoen by wyse van 'n eenparige besluit.
- 11.3.6 'n Besluit wat op skrif gestel en deur al die Trustees onderteken is, het dieselfde regsrag as 'n besluit op 'n behoorlike gekonstitueerde vergadering geneem.
- 11.3.7 Die Trustees is verplig om alle besluite aangaande die Fonds in 'n notuleboek aan te teken en in die verband sal dieselfde prosedures gevolg word as wat maatskappyc verplig is om te volg ingevolge Artikel 204 van die Maatskappywet, 1973 (Wet 61 van 1973) (soos van tyd tot tyd gewysig).
- 11.3.8 Die Trustees vergader so dikwels as wat die Trustees besluit maar ten minste een keer per jaar.
- 11.3.9 Die Trustees is geregtig om een of meer van die Trustees te magtig om alle dokumente vir amptelike doeleindes wat nodig is by die administrasie van die Fonds en ter uitvoering van enige transaksie wat verband hou met die Fonds se sake namens die Trustee te teken en enige besluite wat deur 'n Trustee gesertifiseer is as 'n ware



uittreksel uit die notule van 'n besondere besluit van al die Trustees, het in alle opsigte die regsrag van 'n besluit geteken deur al die Trustees.

11.4 *Sekuriteit*

- 11.4.1 Elke Trustee, hetsy 'n Eerste of daaropvolgende Trustee, is vrygestel van enige verpligting om sekuriteit in verband met sy aanstelling of vir behoorlike administrasie van die Fonds aan die Meester van die Hooggeregshof van Suid-Afrika of aan enige ander amptenaar soos bepaal in enige Wet wat van krag is of wat hierna van krag mag word in verband met die beskerming van die Fondsbates te verskaf en die Meester en enige sodanige ander amptenaar word hierby versoek om van enige sodanige sekuriteit af te sien.
- 11.4.2 Indien die Meester in sy diskresie vereis dat 'n Trustee sekuriteit moet stel, sal die koste verbonde aan die stel van sodanige sekuriteit deur die Fonds betaal word en die Trustees word hiermee gemagtig om sodanige betaling uit die Fonds se fondse te laat geskied.

11.5 *Diskresionêre Bevoegdhede van Trustees*

- 11.5.1 Die diskresionêre magte wat ingevolge hierdie ooreenkoms aan die Trustees verleen word is, tensy uitdruklik in hierdie ooreenkoms anders bepaal, absoluut en onbelemmerd.
- 11.5.2 Geen diskresie of bevoegdheid wat aan die Trustees verleen word ingevolge hierdie ooreenkoms word uitgeoefen of toegepas op 'n wyse wat die gevolg sal hê dat enige gedeelte van die Fondsbates of die inkomste van die Fonds direk of indirek aan 'n Trustee slegs in sy hoedanigheid as Trustee toegeken of tot sy voordeel aangewend word nie.

11.6 *Belange van die Trustees*

- 11.6.1 Enige Trustee mag die bevoegdhede en diskresies hierkragens of regtens aan hom verleen, uitoefen of met die uitoefening daarvan saamstem ondanks die feit dat hy 'n



direkte of persoonlike belang in die wyse of gevolg van die uitoefening van sodanige bevoegdheid of diskresie mag hê, maar 'n Trustee mag, nogtans, sonder dat hy verplig is daartoe en as hy so verkies, hom weerhou van enige optrede of uitoefening van 'n bevoegdheid in enige saak waarin hy 'n persoonlike belang mag hê en mag sy mede Trustee(s) toelaat om alleen op te tree in die uitoefening van die bevoegdhede en diskresies vermeld met betrekking tot sodanige aangeleentheid.

11.6.2 Elke Trustee wat sodanige belang het by enige handeling wat die Fonds raak, is verplig om die aard en omvang van sy belang vooraf skriftelik aan sy mede Trustee(s) te openbaar.

11.6.3 Indien enige voordeel, ongeag die aard daarvan, 'n Trustee toeval wat direk of indirek verband hou met enige transaksie waarby die Fonds betrokke is of indien 'n Trustee versuim om die openbaringsplig in klousule 10.6.1 na te kom, ontvang by sodanige voordeel ten behoeve van die Fonds en is hy verplig om dit op versoek van die ander Trustee(s) aan die Fonds oor te maak op die wyse en tydstip vasgestel deur die oorblywende Trustee(s).

11.7 *Magte en Bevoegdhede van die Trustees*

11.7.1 Die Fondsbates en inkomste van die Fonds vestig in die Fonds wat geadministreer word deur die Trustees in hulle hoedanigheid as Trustees en sodanige bates en inkomste maak nie deel uit van die Trustee(s) se persoonlike boedel nie.

11.7.2 Die Fondsbates en inkomste en alle magte wat aan die Trustees ingevolge hierdie ooreenkoms toegeken word, vestig in die Trustees in hulle hoedanigheid as Trustees ten einde hulle in staat te stel om met die Fondsbates en inkomste van die Fonds te handel ten behoeve van die Lede tot voordeel van die Lede en nie tot die Trustees se persoonlike voordeel nie.



- 11.7.3 Die Trustees is geregtig om enige handeling hoegenaamd te verrig wat hulle in hulle uitsluitlike diskresie noodsaaklik of bevorderlik vir die behoud en groei van die Fonds en inkomste van die Fonds en in belang van die Lede ag en mag vir die doel namens die Fonds enige handeling verrig wat 'n ten volle handelingsbevoegde natuurlike persoon ten opsigte van sy eie sake mag verrig.
- 11.7.4 Sonder om die algemeenheid van die bevoegdhede van die Trustees enigsins te beperk, is die Trustees gemagtig om -
- 11.7.4.1 'n bankrekening in die naam van die Fonds te open; tjeks daarop te trek en gelde daarop te deponeer, wissels en waarborge daarteen te laat uitreik en wissels ten gunste van die Fonds vir invordering te oorhandig. Vir doeleindes van hierdie subparagraaf is die handtekening van enige van die Trustees voldoende vir enige handeling met betrekking tot die bankrekening, mits die bevoegdheid aan 'n enkele Trustee verleen, deur 'n behoorlike besluit van die Trustees gerugsteun is. "Bankrekening" sluit ook rekeninge by of enige kredietreëlings met banke en erkende finansiële instellings in;
- 11.7.4.2 goedere van enige aard, roerend en onroerend, liggaamlik of onliggaamlik en waar ookal geleë, insluitende aandele, effekte, fondse, skuldbriewe en sekuriteite te koop, te verkoop of te ruil, en enige kredietooreenkomste en kontrakte van enige aard aan te gaan op sodanige voorwaardes as wat die Trustees bepaal;
- 11.7.4.3 enige vaste eiendom wat deel van die Fondskapitaal uitmaak, te verkoop, te verhuur, te verbeter, te verander en te onderhou, en, desnoods, vaste verbeterings te sloop en nuwe verbeterings op te rig;



- 11.7.4.4 by enige verkoop van bates wat deel van die Fondskapitaal uitmaak na hulle eie onbeperkte goeddunke sodanige verkoping per openbare veiling, openbare tender of uit die hand te doen en na hulle eie onbeperkte goeddunke krediet te verleen ten opsigte van die hele koopprys of 'n gedeelte daarvan, met of sonder sekuriteit of rente;
- 11.7.4.5 enige dokumente of aktes met betrekking tot vervoemding, verdeling, ruil, oordrag, verbandgewing, verhipotekering of andersins in enige Akteskantoor, Mynbriewekantoor of ander openbare kantoor wat handel met serwitute, vruggebruike, beperkte belange of andersins te verly, en om enige aansoeke te doen, toestemming te verleen en in te stem tot enige wysiging, verandering, rojering, sessie, ontheffing, vermindering, substitusie of enigiets wat in die algemeen betrekking het op enige akte, verband of dokument, en om vir enige doeleindes afskrifte van aktes, verbande of dokumente te verkry, en om in die algemeen enige handeling hoegenaamd in enige sodanige kantoor te doen of te laat doen;
- 11.7.4.6 huurkontrakte aan te gaan as huurder of verhuurder en indien as verhuurder, hurgheid in te vorder en huurkontrakte te kanselleer en die nodige stappe te doen vir die uitsetting van 'n huurder uit 'n verhuurde eiendom en dorpstigting en deeltitei ontwikkeling daarop te onderneem;
- 11.7.4.7 gelde wat deel van die Fondskapitaal uitmaak teen rente of rentevry te belê in sodanige sekuriteite en op sodanige wyse en voorwaardes as wat die Trustees bepaal;



- 11.7.4.8 enige belegging wat deel van die Fondskapitaal uitmaak in hulle diskresie in daardie vorm te behou of te wysig of te herbelê;
- 11.7.4.9 lenings vir doeleindes van die Fonds aan te gaan, met of sonder rente en met of sonder sekuriteit, en op sodanige voorwaardes as waarop met die persoon of instansie wat die lening aan die Trustees maak, ooreengekom word;
- 11.7.4.10 enige bate van die Fonds onder verband te bring, dit te verhipotekeer of 'n retensie daarop te gee;
- 11.7.4.11 regsgedinge in te stel, te verdedig of te skik;
- 11.7.4.12 vergaderings van skuldeisers van 'n privaat individu, maatskappy of liggaam wat 'n skuldenaar van die Fonds is by te woon, ongeag of die vergadering met insolvensie, likwidasie of geregtelike besnuur verband hou, te stem oor enige sake wat aan die vergadering voorgelê word, en, in die algemeen alle regte wat aan 'n skuldeiser in soortgelyke omstandighede toekom, uit te oefen;
- 11.7.4.13 die nakoming van die kontrakte of verpligtinge van enige persoon of maatskappy teen vergoeding of gratis te waarborg as borg- en medehoofskuldenaar en om vir die doel bates van die Fonds as sekuriteit te verbind;
- 11.7.4.14 kwitansies, ontheffings of vrywarings te gee ten aansien van enige bedrag of vordering wat ontvang is of waaraan voldoen is;
- 11.7.4.15 van die dienste van professionele adviseurs en van ambagsmanne vir die sake van die Fonds gebruik te maak en vir sodanige dienste uit die Fonds te betaal;



- 11.7.4.16 skenkings of erflatings ten behoeve van die Fonds van enigiemand te aanvaar, onderhewig aan die bepalings en voorwaardes van hierdie Fondsakte en onderhewig aan die bepalings en voorwaardes waarmee sodanige skenkings en/of erflating gepaard mag gaan;
- 11.7.4.17 enige besigheid in naam van die Fonds, hetsy vir wins of andersins, alleen of in vennootskap of assosiasie, te bedryf;
- 11.7.4.18 maatskappye in enige deel van die wêreld op te rig met sodanige doelstellings as wat die Trustees mag bepaal, die stemreg verbonde aan aandele, in enige maatskappy, wat in die Trustees vestig uit te oefen, en in die algemeen alles met betrekking tot 'n maatskappy te doen wat 'n aandeelhouer ingevoige die bepalings van die toepaslike Maatskappyereg kan doen;
- 11.7.4.19 in geval van 'n maatskappy of effektrust waarvan die statute die oordrag van aandele in naam van die Fonds of die Trustees as sodanig verbied, die aandele in hulle persoonlike name, of die name van hulle benoemdes te laat oordra en te hou as genomineerdes van en ten behoeve van die Fonds;
- 11.7.4.20 kontrakte met hulleself in hulle persoonlike hoedanigheid, gesamentlik en afsonderlik, te sluit, mits aan die voorskrifte van subparagraaf 10.6.2 voldoen word;
- 11.7.4.21 by die uitoefening van enige van die voormelde bevoegdhede alle dokumente te teken en alle stappe te doen wat nodig mag wees om sinvol aan 'n besondere bevoegdheid uitvoering te gee;
- 11.7.4.22 in die algemeen die magte en bevoegdhede van 'n maatskappydireksie uit te oefen en, meer



besonderlik, om *mutatis mutandis* die bevoegd-
hede in Bylae 2 tot die Maatskappywet Nr 61
van 1973 (of latere wysigings daarvan) aan 'n
maatskappy te verleen, uit te oefen;

- 11.7.4.23 om alle magte, regte en verpligtinge wat hulle
kragtens hierdie Fondsreëls verkry, in enige land
buite die Republiek van Suid-Afrika uit te oefen
en aan te gaan;
- 11.7.4.24 op naam van die Fonds lidmaatskap van en
enige kredietfasiliteite by enige landbou- of
ander koöperatiewe maatskappy of vereniging, of
enige ander vereniging, te verkry en te benut en
om vir die doel van Fondskapitaal of enige ge-
deelte daarvan by wyse van pand, hipoteek of
verband as sekuriteit te verbind.
- 11.7.5 Sonder om enigsins die algemeenheid van die Trustees se
fidusiëre pligte in te perk, is die Trustees verplig om -
- 11.7.5.1 skenkings ingevoige paragraaf 6 gemaak op te
volg en in ontvangs te neem;
- 11.7.5.2 onmiddellik 'n bank- of soortgelyke rekening by
'n erkende finansiële instelling op naam van die
Fonds te open en alle gelde wat die Fonds toe-
kom in die eerste instansie op sodanige rekening
te deponeer;
- 11.7.5.3 alle bates van die Fonds en alle titelaktes en
dokumente met betrekking tot die Fonds in besit
te neem en in veilige bewaring te hou;
- 11.7.5.4 behoortlik boek te hou of te laat hou van die
sake van die Fonds en uitvoering gee aan die
voorskrifte van subparagraaf 11.1;
- 11.7.5.5 nie oor enige bates van die Fonds vir hulle eie
voordeel of vir die voordeel van hulle boedels te



beskik nie, behalwe soos uitdruklik andersins bepaal in hierdie akte, en sal die boedel, bates, rekeninge en sake van die Fonds apart van die van die Trustees gehou, beheer en administreer word. Alie roerende, onroerende en verhandelbare bates, dokumente, beleggings, saketransaksies en besigheid moet in die naam van die Fonds geregistreeer word en geskied of in naam van die Trustees, maar dan met aanduiding dat dit ten behoewe van en in hul hoedanigheid van Trustees van die Fonds is.

11.8 *Persoonlike Aanspreeklikheid van Trustees*

'n Trustee is nie persoonlik aanspreeklik vir enige verlies wat die Fonds mag ly nie, ongeag die rede daarvoor, tensy sodanige verlies uit 'n opsetlike onregmatige handeling of late of die growwe nalatigheid van 'n Trustee voortspruit. 'n Trustee is nie vir 'n bedrieglike handeling van 'n mede Trustee aanspreeklik nie tensy daar samespanning tussen so 'n Trustee en die mede Trustee was.

11.9 *Vergoeding van Trustees*

Die vergoeding wat die Trustees vir hulle dienste mag eis word jaarliks vasgestel by wyse van 'n besluit deur die Trustees so na as moontlik aan die einde van die Fonds se finansiële jaar.

12. *PROFESSIONELE DIENSTE*

12.1 Die Trustee moet, indien daartoe deur Denel versoek, van tyd tot tyd 'n geoktrooieerde rekenmeester (in hierdie akte na verwys as die ouditeur van die Fonds) aanstel om as die ouditeur van die Fonds op te tree. Aan die einde van elke finansiële jaar sal die Trustees 'n rekening van die administrasie van die Fonds laat opstel waarin die kapitaal van die Fonds uiteengesit word met alle byvoegings daartoe en alle inkomstes en uitgawes deur die Trustees aangegaan en die wyse waarop dit alles gehou en belê is.

12.2 Die Trustees is geregtig om van die dienste van professionele persone gebruik te maak in soverre hulle sodanige dienste noodsaaklik of

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wenslik ag vir die doeleindes van die Fonds en daarvoor uit die Fonds se fondse te betaal.

- 12.3 Die feit dat 'n Trustee 'n professie beoefen of besigheid bedryf, sal geen beletsel vir hom of sy firma wees om in professionele of ander hoedanigheid opdragte van die Fonds te ontvang en uit te voer en daarvoor vergoed te word nie ewe asof hy nie 'n Trustee is nie.

13. *ONTBINDING*

- 13.1 Die Trustees mag met die toestemming van Denel te enige tyd in hulle absolute onbelemmerde diskresie die Fonds beëindig.
- 13.2 By die ontbinding van die Fonds, en nadat al die skulde van die Fonds betaal is, word die bates en enige inkomste van die Fonds (indien enige) gegee en oorgemaak aan 'n vereniging of inrigting wat dieselfde of soortgelyke doelstellings as die Fonds se hoofdoelstelling het.

14. *WYSIGINGS VAN REËLS*

- 14.1 Die Fondsreëls kan te enige tyd by ooreenkoms tussen Denel en die Trustees gewysig word met dien verstande dat klousules 5, 7, 8 en 12.2 en hierdie klousule 13.1 nie gewysig mag word nie.
- 14.2 Die bevoegdheid om die Fondsreëls te wysig het slegs betrekking op die bepaaings en voorwaardes van die reëls en verleen nie die bevoegdheid om verdere lede aan te stel of te verander nie of dat daaroor die fondsbates beskik kan word tot voordeel van Denel of die Trustees, siegs in hulle hoedanigheid as trustees, of enige ander persoon as die lede nie.
- 14.3 Enige byvoeging of verandering tot die Fondsreëls moet eers deur die Kommissaris van Binnelandse Inkomste goedgekeur word, voordat dit van krag word.

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DENEL (PROPRIETARY) LIMITED

Personnel & Remuneration Meeting to be held on : 2000-02-16

Memorandum Number : 1

Agenda Item Number : 5

File Reference : 2.5/180.05(8)

FUNDING OF HEALTHCARE LIABILITY

1. PURPOSE

The purpose of this submission is to get P & R Committee approval for the future strategy and funding of the healthcare liability of Denel aimed at decreasing the future risk to the Company.

2. DEFINITIONS AND EXPLANATIONS

Some of the terminology used in this memorandum is defined below for the convenience of the members of the Committee.

2.1 Umed

Umed is the in-house medical scheme for Denel's employees and continuation and widow members who obtained such membership as a result of previous employment with Denel. Armscor and Sita (previously Infoplan) are still participating employers of Umed.

As at 1 August 1999 Denel had 8566 members on Umed with the following profile:

Category	M	M + 1	M + 2	M + 3 or more	Total
Active members	1083	1042	1061	2583	5769
Pre 1 April 1990 continuation members	505	341	30	28	904
Post 1 April 1990 but pre 1 January 1994 continuation members	262	533	66	39	900
Post 1 January 1994 continuation members	166	557	166	104	993
TOTAL	2016	2473	1323	2754	8566

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2.2 Denpen / Denret

The Denel Pension Fund (Denpen) is a closed pension fund with a membership composition of 115 active, contributing members and 3835 pensioners. Denpen is a defined benefit pension fund which means that the employer, Denel, guarantees all pension benefits and will "stand-in" for any financial shortfalls that may arise.

The majority of employees still in service (7696) belongs to the Denel Retirement Fund (Denret) which is a defined contribution fund where all the pension risks lie with the members.

2.3 In-service members

Refers to those Umed members currently employed at Denel and who have the expectation that Denel will provide for their post retirement healthcare costs.

2.4 Current members

Includes retired employees (continuation members) and their dependants as well as in-service members and their dependants.

2.5 Continuation members

These are members who are already retired employees and on whose behalf Denel incur regular subsidy cost to meet their post retirement healthcare obligations.

2.6 Contribution liability

The present value of contributions for future post retirement healthcare that is payable in terms of Denel's healthcare policy. In other words, it represents the cash that Denel will need to set aside now to cover all future post retirement healthcare contributions of current members.

2.7 Past service liability

That portion of the current member's future medical aid contribution which need to be made by Denel which was effectively earned by the member from the date of his employment to the date of the actuarial valuation.

2.8 Future service liability

That portion of the current member's future medical aid contribution which need to be made by Denel which will be earned by the member from the date of the actuarial valuation until expected retirement date.

2.9 Medical Benefit Fund

The Medical Benefit Fund was up until 31 December 1999 a paragraph(c) fund in terms of the Income Tax Act, exempt from paying tax. From 1 January 2000, the Medical Benefit Fund lost its tax exempt status and legal opinion indicated that the Medical Benefit Fund can be regarded as a Common Law Trust from 1 January 2000.

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3. BACKGROUND

3.1 Liability in respect of expectation to pay portion of the post retirement contributions.

3.1.1 Denel like many other corporations and institutions in South Africa (*Discussed further at point 4 of this memorandum*) is faced with a liability in respect of an expectation created to pay a portion of Umed contributions due after retirement.

Continuation members which continue to belong to Umed belong to the following 3 categories with the following different contribution structures:

1. Pre April 1990 continuation members

These members pays 13% of the Umed active members rate. Umed pays the medical claims of these members and recovers the shortfall between the 13% contribution and claims from the Medical Benefit Fund.

2. Post April 1990 and pre January 1994 continuation members

These members pays 22% of the Umed active members rate. The shortfall between claims and the 22% contributions is subsidised by the Medical Benefit Fund.

3. Post January 1994 continuation members

Members retiring after 1 January 1994 have a contribution rate of 33% of the Umed active members rate. The subsidy from the Medical Benefit Fund is also calculated as set out above.

Continuation members were and are informed upon retirement of the amount payable by them which is effectively represented by one third of the full membership contribution contained in the schedule to the Umed rules (except for the continuation members pre January 1994 which pays a lesser percentage).

3.1.2 Denel's obligation and legal opinion

Although this practice is not contained in a specific written agreement between current members it seems as if practice had set a precedent for the following reasons:

1. The Umed rules (14 and 15) imposes an obligation on Denel to make payment of the contributions;
2. The Umed rules are incorporated into the standard contract of employment by reference;

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3. The audited annual financial statements of Denel in terms of the requirements of AC 305 of the Institute of Chartered Accountants contains a paragraph in the Directors' Report under the heading "Post-retirement Medical Benefits" which states that "Additional provision for future liabilities of post-retirement medical benefits is done through a medical benefit fund". The paragraph then proceeds to discuss the actuarial valuation of "future liabilities of the Group" and comes to the conclusion after reference is made to the annual contribution by Denel to the said fund that "under these circumstances no provision is deemed necessary". The fact that the Board of Directors considers it necessary to report on this "liability" seems to be in accordance with the widely held belief and expectation amongst employees and management of Denel than upon retirement the employee will only be liable for one third of the total medical aid contribution.

4. The retirement letter discussed under point 3.1.1

A legal opinion from attorneys Gildenhuis Van Der Merwe dated 6 December 1999 confirmed that "there is a risk that Denel may be held liable on the basis of either a tacit agreement or the principles of estoppel."

3.2 Current vehicle for funding of post retirement liability

Soon after Denel was established, the risk of funding the post retirement liability was identified. It was decided to do the funding outside of Umed for various reasons and Denel formed the Medical Benefit Fund in terms of paragraph (c) of the definition of "benefit fund" in section 1 of the Income Tax Act 58 of 1962 during February 1993 as a vehicle to fund its post retirement liability over the working life of in-service members so that the benefit is fully funded by the time the member becomes entitled to receive such benefit, which is the date of retirement.

Claims are regularly instituted by Umed against the Medical Benefit Fund for the difference between continuation member contributions and actual claims. After an initial lump sum contribution Denel continued to fund the Medical Benefit Fund at a rate of 25% of two thirds of the active member's medical contributions.

3.3 Funding level movement : Medical benefit fund vs liability

The actuarially calculated past service liability of the difference between the aforementioned continuation member contributions and actual claims progressed as follows:

DESCRIPTION	* REAL INTEREST RATES : 0%				
	1994	1996	1997	1998	Aug 1999
	R'000	R'000	R'000	R'000	R'000
Past service liability	536 115	565 788	746 565	1 147 125	978 522
Assets in the Medical Benefit Fund	(352 872)	(449 799)	(470 772)	(510 597)	(596 607)
Deficit	183 243	115 989	275 793	636 528	381 915

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* A 0% real interest rate assumes that medical inflation and investment income will be equal.

The significant increase in the post retirement healthcare liability after the initial improvement in 1996 was due to the:

1. Growth in the average age of members: new entrants is on average older when first employed;
2. Medical inflation being higher than investment returns;
3. In 1998, an increase of 25% in the average claims level exceeded the 13% expected; and
4. The employer is contributing to the Medical Benefit Fund at less than the rate required. The current funding level of 25% of two third of the employers contribution to Umed is substantially lower than the required contribution liability level of 59,4% based on a 2% real interest rate.
5. A reduction in overall membership of Umed with a concomitant deterioration in membership demographics due to the restructuring and downsizing of Denel.

3.4 Current impediments

The post retirement healthcare funding is complicated by the following:

3.4.1 On 1 January 2000 the Denel Medical Benefit Fund lost its favourable tax regime. The regulatory framework of these funds is not entirely clear but SARS have indicated that the existing approved funds have the following options:

- Register as a medical scheme which is not an option for Denel as multiple medical schemes are not allowed.
- Transfer to a registered medical scheme.
- Transfer to a registered insurer.
- Continue with the status quo, but without the current tax concession.

3.4.2 The Medical Schemes Act (No 131 of 1998) was promulgated on 1 February 1999 and Umed will have to comply with the Act by 1 January 2000. (*Discussed further at point 5 of this memorandum*)

3.4.3 With the current financial difficulty Denel is experiencing, it is not possible to continue with the present situation where an additional amount is being contributed to the Medical Benefit Fund and where the Company's obligation for future post retirement funding is increasing continuously.

In conclusion, the current open ended, defined benefit arrangement of Denel is clearly unsustainable and an already difficult situation is aggravated by the demise of the paragraph(c) fund in terms of the Income Tax Act and the new regulatory environment of the Medical Schemes Act.

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4. BENCHMARK EXERCISE

4.1 A benchmarking exercise was embarked upon to establish the following:

- The different medical aid schemes and benefit structures offered in the market;
- Future strategy of different employer groups regarding funding contributions for continuation members.

The following firms of consultants with extensive experience in the field of medical aids and healthcare funding were utilised by Umed, the Denel Medical Benefit Fund and Denel:

- PSG Health
- Fifth Quadrant
- Jacque Malan and Associates

4.2 Benchmarking

4.2.1 Medical aid benefit structure

Umed currently offers its members two medical packages with different benefit structures and for pensioners pre 1 January 1994 a separate package. These are referred to as *Package 1*, *Package 2* and *Table 2* respectively. These plans pay 80% of Scale of Benefits out-of-hospital treatment and prescription medication. In hospital procedures comprise a mixture of 100% and 80% benefits. The coverage provided under *Package 1* is more limited than under *Package 2* and *Table 2*: Auxiliary services are not covered and annual limits on certain categories of service are lower.

An analysis and comparison done by Fifth Quadrant of the benefits and cost of various medical schemes relative to Umed, *Package 2*, concluded that Umed offers good value for money. The analysis suggested that *Package 2* as currently designed caters mainly for the top-end of the market i.e. it offers very comprehensive benefits but at a fairly high cost. *Package 1* as currently designed caters mainly for the lower-end of the market.

In accordance with the provisions of the Medical Schemes Act, Umed redesigned the aforementioned three packages into two packages named: *Option 1* and *Option 2*. *Option 1* and *Option 2* provides simplified benefit structures to give Umed members a clear and easily understandable choice of products.

4.2.2.1 Impact of the changes in benefit structures

The impact of the changes in the Umed benefit structures are as follows:

- There is greater Umed membership responsibility for day to day expenses; and
- An aggressive healthcare management strategy aimed at improved and effective control over misuse, overuse and overservicing.

The ultimate goal is to ensure that membership contributions are affordable and at an optimal level and claims are reduced which should have a significant impact on the post retirement liability of Denel.

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4.2.2. Medical aid contribution structure

The contribution tables of Umed, as approved, compared to the current contribution tables are as follows:

Contribution per:	Option 1		Option 2 (19% increase)	
	1999	2000	1999	2000
Member	454	454	682	812
Member with 1 dependant	757	757	1159	1379
Member with 2 dependants	811	811	1255	1473
Member with 3 dependants	856	856	1318	1568
Member with 4+ dependants	874	874	1345	1601

4.2.2. Compensation structure of Denel

Denel currently remunerates employees on a total cost to company basis. Denel pays ~~three~~ thirds of the Umed contribution of an employee whilst in service. The employee pays tax on a third of the Umed contribution. When an employee retires he/she is notified that he/she will be responsible for one third of the Umed contribution. Denel currently pays the difference between the one third contribution of a continuation member and actual claims. Therefore, the post retirement benefit forms a component of the perks and remuneration packages of employees.

4.3 Continuation members - future funding

There is consensus in the market that undertakings (explicitly or implicitly) had been given by employers to contribute towards the medical cost of continuation members and that this real liability should be provided for and/or funded and disclosed appropriately. AC305 was issued in July 1995 by the Institute for Chartered Accountants and recommended that the unfunded liability should be provided for in full immediately, or over a period, not longer than the average remaining service period of in-service members

The Old Mutual Healthcare Report (*Annexure A*) among "a representative sample of large employers", revealed that 89% recognised that they had an obligation towards continuation members. 30% of the respondents indicated that they have recognised the liability (accounting wise), while another 27% said that they will recognise it within 4 years. 43% indicated they will not recognise it, unless required to do so by accounting practice. Almost all employers who have acknowledged their liability are setting aside some sum of funding to either fully or partly offset their post retirement liability. Some employers are using their current medical aid scheme to fund future liability and others have set up a separate retirement vehicle for this purpose. (It is suspected that these companies did not have an existing funding vehicle). Employers pensioner philosophy have not changed in emphasis, except that more employers are capping the retirement benefit and offering cash and other benefits in lieu of post retirement medical benefits.

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4.4 New employees - future funding

For new employees however, the strategies are different in that employers surveyed in the Old Mutual Healthcare Report have adopted a very different approach to managing this liability. The latest trend is that Employers are not offering company sponsorship of healthcare benefits during retirement which is the key cost control concept for 43% of employers surveyed. The future continuation members can remain on the medical aid scheme but will receive no company sponsorship. Employees would need to pre-fund as individuals for this eventuality. *(Later in this report it will be indicated that this will be a key cost control concept for Denel as well.)*

4.5 Other studies

In a survey by Pollitt (in 1998) among the top 100 companies on the JSE (identified by the Financial Mail's 1995 Survey of Top Companies), only 39 responded of which 14 did not pay post retirement healthcare benefits to employees. Of the remaining 25, only 7 prefunded these benefits. It was noted that 5 of the 25 indicated that they had already withdrawn the medical benefits to employees starting service after a specified date and another 14 planned to reduce the benefits in future. In spite of the fact that AC305 was issued 2 years earlier, 78% of the respondents were still accounting for the post retirement healthcare benefit on a cash basis.

The Jacque Malan and Associates Survey (*Annexure B*) among 310 industrial sector companies listed on the JSE indicated that of the companies that disclosed the liability in their financial statements, 28% indicated that they do cash prefunding, i.e. contributions to a fund or insurance policy. The survey includes the strategic plans of specific companies (their names are not disclosed which is due to the confidential nature of their investigation and negotiations). It is clear from this specific company survey that their strategic plans differ depending on current funding vehicles, the funding level or deficit, conditions of employment, medical scheme structure and other circumstances. In general, these companies are not providing post retirement benefits to new employees and are investigating or implementing strategies to cap their liability.

A few companies were approached by the Denel Human Resource Department to determine their strategies. Although most organisations including Sasol, SA Reserve Bank, Telkom, Escom and Iscor acknowledged their commitment to active and continuation member's post retirement subsidies they also confirmed that they are not giving this subsidy to new employees (Iscor, SA Munt and Sasol) or are in the process of reviewing their policy.

4.6 Conclusion of benchmarking exercise

In summary, most employers agree that:

1. They have a liability towards current pensioners (explicitly or implicitly);
2. The level of sponsorship is unsustainable;
3. The process of how healthcare during retirement will be funded have to change;
4. A pensioner liability in relation to financing of future healthcare should not be created for new employees; and

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5. They will not subsidise the members "extended family" which has to be dealt with in terms of the new Act on Medical Schemes.

In terms of in-service members expectancy the employers future strategy depends on its existing level of funding, human resource policy and budgetary constraints.

The future strategies involve the following:

1. Move from a commercial medical scheme to a restrictive medical scheme or vice versa depending on the impact on employers subsidy and cross subsidy liability. However, there is general agreement amongst virtually all experts in healthcare that a restricted membership scheme such as Umed will have huge advantages over an open scheme under the new Medical Schemes Act.
2. Cap the post retirement benefit and/or offer cash and other benefits in lieu of medical aid scheme sponsorship;
3. Continuing to fund the liability in a medical fund, retirement fund, cell captive or long term policy;
4. Buy-out the existing liability by granting additional benefits in the pension fund linked to the member's year of service; and
5. No retirement benefits for new employees.

5. IMPACT OF NEW ACT ON UMED AND THE POST RETIREMENT LIABILITY OF DENEL

5.1 Background

Denel has historically (since 1973) operated an in-house medical scheme (Umed) for its employees, pensioners and widow members who obtained such membership as a result of their employment with Denel. Umed is internally administered and provides a highly personalised service to its members. The strong position of Umed (solvency ratio of 62%) is at least partially due to the fact that Denel subsidises continuation members through the Medical Benefit Fund.

5.2 Impact on Umed

The new Medical Schemes Act had a profound effect on Umed (and virtually every other medical scheme in South Africa) by effectively outlawing Umed's current contribution table (the differentiation in contributions between in-service members and the different "classes" of continuation members) and option structures. The salient provisions in the Act are:

- Section 29(1)(17) provides that contributions may in future only be based on member's income and/or number of dependants.
- A medical scheme may offer more than one option, but all members of the scheme must have a free choice of which option he/she wants to belong to and to move between the various options on at least an annual basis. Therefore, the special dispensation for continuation members within the new structures of Umed is not financially viable as in-service members can belong to the special dispensation option of continuation members where they will only pay an insignificant portion of the one third contributions upon retirement and Denel the balance.

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The restructuring exercise in terms of the new Act is complete and resulted in a single contribution structure for the two medical benefit options. The new contribution structures and benefit options will be implemented on 1 April 2000. Members previously on *Package 1* will be on *Option 1* with no increase in contributions. Members previously on *Package 2* and *Table 2* will be on *Option 2* with a 19% increase in contributions. (Also discussed under point 4.2 of this memorandum).

5.3 Impact on Denel

An actuarial calculation done as at 1 August 1999 based on a 0% real interest rate having regard to the new Umed contribution structure and benefit options revealed the following impact on the accrued liability:

	R'000
Accrued liability (Past service)	978 522
Less assets	(596 607)
Deficit	381 915

In addition, there is a contribution liability which requires that the current funding level of 25% of two thirds be increased to:

Past service contribution	21%
Future service contribution rate	39,8%%
Total	60,8%

In addition to the 8566 Umed members there are another 4806 Denel employees (10575 employees less 5769 in service members) who are either not members of a medical scheme or registered dependants on their spouse's medical scheme. The potential liabilities associated with these employees can be significant. (It is guesstimated that if these members have the same profile as in service members and all of them join Umed the accrued liability could increase by as much as R260 million).

In conclusion, post retirement medical healthcare had escalated to such an extent that Denel cannot afford, given its current financial position and medical inflation, to proceed with a contribution liability level of 25% of two thirds (R4,1 million per year) let alone increase the funding level to 60,8% of two thirds.

This sentiment is shared by other employers as reflected in the Old Mutual Healthcare Report (*Annexure A*) and the Jacque Malan and Associates Survey Report (*Annexure B*)

6. PROPOSED FUTURE STRATEGY

6.1 Elimination of Cross Subsidisation

6.1.1 General

Denel's past service liability increased from R565 million in 1996 to R1,147 million in 1998 although an additional funding level of 25% of two thirds was sustained.

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If Denel proceeds with their current defined benefit arrangement, Denel will continue to carry the risk posed by the following circumstances:

- Medical inflation rates caused by changing economic conditions, advancements in technology and consequent increase in the cost of medical inflation;
- Fluctuating investments returns caused by the volatility in the current and future economic environment;
- The increased cost due to younger prospective membership declining; and
- Changes in the withdrawal rate of membership through accelerated or decelerated retirement of the current in service employees.

An in depth investigation to resolve this unaffordable dispensation were undertaken by management and the appointed consultant firm: PSG Health (Pty) Ltd which included discussions with various parties.

It is proposed that the following be implemented as soon as possible:

6.1.2 New employees - future funding contribution

In accordance with the results of the benchmarking exercise it is proposed to change the conditions of employment for all new employees to clearly state (in their letters of employment) that Denel will have no liability for post retirement healthcare subsidies. If Denel decide to make a defined monthly contribution into a prefunding vehicle such as the individual retirement fund account of the new employee the cost would be enormous and unaffordable. (*Annexure C*). Since this is an unaffordable option, it is recommended that retirement healthcare benefits are not given to new employers with inception 1 April 2000.

In addition this strategy will result in all of the in-service members and continuation members becoming a closed population where new employees will not negatively impact on the already unsustainable defined benefit subsidy and liability.

6.1.3 Medical Benefit Fund

It is recommended that the Denel Medical Benefit Fund continue as a separate legal entity (possibly as a trust for the time being), that Denel cease to contribute towards and that Denel manage the post-retirement healthcare liability of the current 8566 members on a "dying fund" basis, i.e. run out of money one day after the death of the last member (\pm 45 years from now).

In the first year (2000) the Benefit Fund will provide Umed with:

- A cross subsidy amount equal to the amount whereby the continuation members' claims are expected to exceed the (higher) contributions payable in terms of the new Umed contributions. It is estimated that this will amount to R26 million per annum; and

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- A contribution subsidy for those continuation members who are not members of Denpen so that they are in a similar position as the Umed continuation members who are members of Denpen.

In subsequent years, the trustees and management of the Medical Benefit Fund will, depending on the investment performance of the Fund, the mortality rate of the remaining beneficiary population and the prevailing tax arrangements, indicate to Umed what level of subsidy it can afford for the upcoming year. This information should then form part of the Scheme's annual budgetary processes to determine its own contribution requirements for the following year.

6.2 Proposal on future post retirement funding

6.2.1 Use of Denel Pension Fund surplus

Most of the continuation members at Denpen will move from their existing benefit package to *Option 2* with inception 1 April 2000. Due to the 19% increase in contributions for members on *Option 2* (*Annexure D, page 2*) and the single contribution structure required in the Medical Schemes Act (*Discussed under point 6.1.3 of this memorandum*), continuation members will be significantly out of pocket. The following proposal is aimed at resolving the financial impact on continuation members.

A current "overfunding" situation exists in the Denel Pension Fund due to so called excess contributions made by Denel over time, in respect of active members. Current legislation dictates that Denel is not entitled to any portion of these surplus funds except for a so called "contribution holiday" in respect of Denel's contributions for active members. Due to the fact that Denel has already taken a "contribution holiday" and the low number of active members future "contribution holidays" is insignificant.

On the other hand, active members and pensioners can only benefit from these surplus funds if the Board of Trustees approves an extraordinary allocation in terms of additional pension increases or improved/enhanced benefits. Therefore, it is clear that both Denel and the members depend on each other in the allocation of the surplus funds mentioned.

After going through a major process of investigation and consultation, the Board of Trustees currently prepared to utilise the surplus to enhance pension benefits in order to compensate the current and prospective members of the Pension Fund for post retirement healthcare benefits. (*Annexure D*)

The Pension Funds consulting actuary estimated that it will require R270 million of the surplus to increase the 1845 Umed pensioners current pensions to the extent that they will be no worse off as a result of the higher medical scheme contributions payable from 1 April 2000.

To preserve the equity between Umed members and non Umed members of the Pension Fund, non Umed members can receive a pension increase as if they were on *Option 1* (lowest cost) of Umed. According to the actuary, this will require another R124 million of the Funds' surplus.

Similarly, it is estimated that it will require R8 million to put the 115 in service Denpen members (Umed and non Umed members) in a similar position as their counterparts.

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The impact of utilising the Denpen surplus on Denpen is as follows:

	Rm
Surplus funds as at 31 December 1998	607
Allocation:	
1. To compensate for higher Umed contribution of 1845 members	(270)
2. To compensate for 115 in-service members	(8)
3. To preserve equity for 1990 non Umed pensioners	(124)
Reserve in surplus fund	205

The amount required as a cash bonus equal to a 13th cheque with effect 1 April 2000 will be approximately R7,5m.

The impact of utilising the Denpen surplus on the post retirement liability of Denel is as follows:

	R'000
Past service liability	978 522
Future service liability	375 445
Subtotal	1 353 967
Less impact of the Denpen surplus funding	(365 978)
Subtotal	987 989
Less assets in the Medical Benefit Fund	(596 607)
Deficit	391 382

In conclusion, this strategy will reduce the deficit from R757 360 000 to R391 382 000.

In addition this strategy will result in all of the in-service members and continuation members becoming a closed population where new employees will not negatively impact on the already unsustainable defined benefit subsidy and liability.

Legal opinion from Gildenhuis van der Merwe dated 6 December 1999 confirmed that "the proposed increase of benefits by Denpen to its members will, provided that the approval prescribed by the rules are obtained, is lawful"

6.3 Dependants

In terms of clause 1 of the Medical Schemes Act "dependants" means:

- (a) the spouse or partner, dependant children or other members of the member's immediate family in respect of whom the member is liable for family care or support; or

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- (b) any other person who under the rules of the medical scheme is recognised as a dependant of such a member and is eligible for benefits under the rules of the medical aid scheme.

This means that members can add on any number of persons as dependants. Umed cannot in terms of the Medical Schemes Act disallow these persons to become dependants but indications are that an additional premium will be charged. As the Medical Schemes Act becomes operational on 1 January 2000 Denel must limit the type of dependants it will subsidise so that the total contribution cost to include a person who receives family care and support from a member will be for the members own account.

Implementing the aforementioned three strategies will result in a capping of the liability (dependants and new employee), and a reduction in the existing liability (Denpen surplus

It will also be part of the duties of the trustees of the Medical Benefit Fund to maximise the returns and to optimise the tax dispensation of the monies over its expected lifetime.

It is recommended that Denel ceases the 25% of two thirds contribution to the Medical Benefit Fund and that the deficit in the future be funded via gradual (over many years) increases in the overall contributions in Umed and an element of cross subsidisation of continuation members by the younger in service-members. (This is the rule in almost all other medical schemes in South Africa). This will result in a saving for Denel of R14,3 million per year.

7. OTHER FUNDING OPTIONS CONSIDERED

The following alternative strategies and funding vehicles were considered due to the taxation of the Medical Benefit Fund from 1 January 2000 but are not recommended for the stated reasons: (*Annexure E*)

- Umed Medical Scheme as a funding vehicle
- A Pension of Retirement Fund as a funding vehicle
- Short term insurance cell captive as a funding vehicle
- Employees waive entitlement as an alternative strategy
- Section 21 Company

The Medical Benefit Fund trustees will continuously investigate alternative risk financing vehicles. Currently under investigation is a Finite Insurance Policy and a Long Term Insurance Cell Captive.

8. VISUAL PRESENTATION

The matters addressed in this memorandum are very complex. The information in this memo and annexures will be complimented with a visual presentation during the meeting.

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9. **CONCLUSION**

The P & R Committee is requested to take note of the cost and impact of the present dispensation and to approve the proposed future strategy in respect of:

- Utilisation of the Denpen surplus as proposed in 6.2.1;
- Change in service conditions not committing employee contributions after retirement to employees joining the Group after 1 April 2000;
- Changing the existing subsidy to Umed from a defined benefit to a defined contribution, utilising only the current assets in the Medical Benefit Fund (no employer contribution as from 1 April 2000); and
- The employer subsidy approach relating to "extended family".



HD DU P POTGIETER
GROUP DIRECTOR: FINANCE (acting)



MIC BIANCO
PRINCIPAL OFFICER:
MEDICAL BENEFIT FUND

	<h1>MEMORANDUM</h1>	
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TO : EXCOM MEMBERS

DATE : 19 FEBRUARY 2001

FROM : NICO BIANCO

ENQUIRIES : X2901

POST RETIREMENT UMED CONTRIBUTION SUBSIDIES

1. PURPOSE

To present the actuarial calculation of the liability for post retirement Umed contribution subsidies at the current level to the Denel Excom for cognisance.

2. BACKGROUND

2.1 Denel Healthcare Strategy

The Denel Healthcare Strategy approved on 16 February 2000 has the following main features:

2.1.1 New employees

Denel has no liability for post retirement medical aid contribution subsidies for employees appointed after 1 April 2000 except for employees who were in negotiation for permanent employment prior to 1 April 2000 but appointed after 1 April 2000.

2.1.2 Dependants

The subsidy will be limited to the spouse or partner and dependant children and not the extended family as defined in the Medical Schemes Act.

2.1.3 Future subsidies

Employees appointed before 1 April 2000, and who are members of Umed at retirement, are entitled to a subsidy which the Denel Medical Benefit Fund ("Fund") can afford to pay. This subsidy is determined by actuarial calculation.

2.2 Denpen

In addition the Denpen "surplus" was "utilised" to curtail the impact of medical aid contribution increases which also impacted positively on the liability. The impact is quantified below.

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3. ASSET LIABILITY MATCHING

3.1 Explanatory notes

- 3.1.1 According to the Healthcare Strategy the assets of the Fund will always match the liability of Denel.
- 3.1.2 The current subsidy level is two thirds of Umed contributions for all pensioners except for Denpen members who are subsidised at 15%.
- 3.1.3 The focus of the actuarial calculation therefore shifted from asset liability matching and required contributions from Denel (which is still reflected in the actuarial report) to determining whether the current subsidy level can be maintained.
- 3.1.4 If the liability to sustain the existing subsidy level exceeds the assets, the subsidy level must be reduced requiring a larger contribution from pensioners. In the alternative, Denel can decide to make an ex gratia contribution equal to the deficit.

3.2 Discussion

3.2.1 Historic comparison

The actuarial asset liability matching for the previous two years compared to the calculation as at 1 August 2000 is as follows:

Description	RM		
	1998	1999	2000
	2% Real Rate		
Assets	511	597	672
Liability	(1132)	(1014)	(650)
Surplus/(Deficit)	(621)	(417)	22

The positive effect of the Denel Healthcare Strategy and Denpen "surplus strategy" can be seen in the reduction of the liability from R1014m in 1999 to R650m in 2000.

Given the above scenario it would have been possible for the Fund to continue with the existing subsidy level if it was not for taxation.

3.2.2 Taxation

The aforementioned calculation assumes that the Fund will perform 2% better than medical inflation. It is estimated that taxation could reduce investment performance with 1%. The result of adjusting the real rate to 1% is as follows:

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Description	RM	
	2% Real	1% Real
Assets	672	672
Liability	(650)	(791)
Surplus/(Deficit)	22	(119)

Therefore, having regard to taxation the current subsidy level cannot be maintained due to a deficit of R119m.

3.2.3 Subsidy level and taxation

According to Umed the existing subsidy level will result in a cost of R15,2m for the Fund in 2001.

According to the actuarial calculation the Fund can only afford to pay R13,4m.

However, instead of reducing the subsidy level of pensioners and/or approaching Denel for an ex gratia top up to sustain the existing subsidy level, the Fund is investigating ways to reduce the tax burden of the Fund.

If successful, the current level of subsidy can be maintained. The investigation is near completion and a submission to the Denel Excom is anticipated in March/April 2001.

4. ATTACHMENTS

4.1 Actuarial report as at 1 August 2000 dated November 2000.

4.2 Sensitivity Analysis as at 1 August 2000 dated 14 November 2000.

If you have any queries please do not hesitate to contact the writer.

Kind regards


 N.C. B. CO.
 PRINCIPAL OFFICER:
 DENEL MEDICAL BENEFIT FUND

DISTRIBUTION LIST

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 Mr LJ Dirker
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 Mr T Swiegelaar
 Dr TJ van Reenen

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 AF



**Actuarial Valuation of the Employer's
Liability in respect of Medical Scheme
Costs for Current and Future Retirees of**

DENEL

As at 1 August 2000

*Prepared by : Jacques Malan & Associates
Consultants and Actuaries*

November 2000

*J.M.A.
AK*

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SECTION 1 - INTRODUCTION

The purpose of this report is to calculate the value of Denel's liabilities in respect of medical costs of retirees (current and future) as at 1 August 2000. The previous actuarial valuation of the medical aid liability was done by ourselves as at 1 August 1999.

We have calculated the liability based on the new contribution rates as outlined in Appendix 3. The employer's liability is now limited to $2/3^{\text{rd}}$ of the total future contributions with the continuation members paying $1/3^{\text{rd}}$. The employer will no longer meet the difference between the total medical costs and the contributions paid by the continuation members. In addition, members who are also members of the Denel Pension Fund will receive an amount from the Pension Fund to meet their medical aid contributions. This amount totals approximately 85% of the contributions. For these members we have therefore assumed the employer's liability is limited to 15% of the future contributions.

The liability for in-service members is not affected by their length of service with the employer, however, a view can be taken that the liabilities for these members accrue uniformly over the total period in service.

For valuation purposes, the liabilities may therefore be divided into two parts for these members, namely a past service and future service liability.

The past service liability can be viewed as being the liability which has accrued to date, whereas the future service liability can be seen to be the liability which will accrue over the future working lifetime of each member.

In addition we have provided a projection of the future cash-flows from the Fund. This is outlined in Appendix 9.

A summary of the subscription rates used is given in Appendix 3.

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SECTION 2 – MEMBERSHIP DATA

The valuation data was provided by UMED.

The membership data on which the calculations are based can be summarised as follows. Previous data shown for comparison purposes.

2.1 Continuation Members

	01/08/2000	01/08/1999
Number	2 760	2 797
Total Annual Contribution	R 40 137 876	R39 860 484
Average Annual Contribution	R 14 543	R14 251
Benefit Weighted Average Age	56 years 10 months	57 years 1 month

Main members who were indicated as “active” on the data provided, but who were older than 60 were valued as if they retired on 1 August 2000, i.e. were assumed to be continuation members and are included above.

2.2 In-Service Members

	01/08/2000	01/08/1999
Number	5 733	5 769
Total Annual Contribution	R 88 215 888	R 89 804 544
Average Annual Contribution	R 15 387	R 15 567
Benefit Weighted Average Age	44 years 9 months	47 years 10 months
Benefit Weighted Average Past Service	14 years 4 months	17 years 4 months

The ‘Annual Contribution’ indicated above are the medical aid contributions paid by members and pensioners based on the tables provided.

The decrease in the Benefit Weighted Average Age in 2.2 above seems to indicate that a number of active members retired during the past year. The data for continuation members supports this assertion to the extent that the Benefit Weighted Average Age has slightly reduced. It would however appear that there are some inconsistencies in the data provided. We are of the opinion that the differences will not be material in the context of the valuation.

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SECTION 3 – VALUATION METHOD AND ASSUMPTIONS**3.1 Liability Valuation Method**

The liabilities have been calculated as follows :

3.1.1 Continuation Members

The liability is taken as the present value of total continuation member contributions to the medical scheme, less the portion paid by the continuation members. Continuation member contributions are projected into each future year using the assumed rate of medical inflation and are then discounted back to the valuation date using the valuation rate of interest. The portion paid by the continuation members themselves differs according to whether they are members of the Denel Pension Fund or not. Members of the Denel Pension Fund will contribute 85% of the total contributions and other members will only contribute 1/3rd.

For each continuation member the projections are based on the probability of survival as per the mortality table outlined in section 3.3.5.

3.1.2 In-Service Members

The liability is also taken as the present value of total future continuation member contributions to the medical scheme, less the portion paid by the continuation members. Future contributions are projected into each future year using the assumed rate of medical inflation and are then discounted back to the valuation date using the valuation rate of interest. The portion paid by the future continuation members themselves also differs according to whether they are members of the Denel Pension Fund or not. Members of the Denel Pension Fund will contribute 85% of the total future contributions and other members will only contribute 1/3rd.

For each member this projection is based on the probability of survival to retirement age and beyond, taking into account the assumed rates of withdrawal and mortality, as outlined in section 3.3.

The past service liability for in-service members has been calculated by splitting the total liability in the ratio of the service completed to the potential full service of each member. (The liability for current continuation members is fully recognised as a past service liability.)

The future service liability of the in-service members is that which accrues over the future working life-time of these members and thus may be funded over this period. We have however not expressed this liability as a contribution rate, but only a total present value of future liability.

3.2 Asset Valuation Method

The assets taken into account for the purpose of the valuation are as follows:

Asset class	1/08/2000 R'000
Real Estate	10 074
Equities	265 954
Global assets	95 367
Interest Bearing	300 205
Total	671 600

All the above assets were valued at market value.

The biggest proportion of the assets were invested with RMB and a further amount is held within the Denel Medical Benefit Fund.

The value of the assets on the Valuation Date were provided to us by the Company.

3.3 Actuarial Assumptions

In order to carry out the valuation, it is necessary to make a number of assumptions.

The various assumptions should be assessed, not in isolation, but rather in relation to each other, e.g. interest rates and medical costs increases have historically tended to move in the same direction as they are both linked to inflation to a large extent. The difference between the two assumptions is, therefore, more important than the individual absolute values.

The actuarial assumptions used in this valuation are reviewed below, and summarised in Appendix 1.

3.3.1 Rate of Interest

The interest rate assumption reflects the investment return expected if funds are set aside to meet the emerging liabilities.

It has been assumed that any investments held on behalf of the Fund would yield a return of 12% per annum.

This has been reduced to 12% from 13% at the previous valuation as a result of the new tax regime under which the Fund operates.

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3.3.2 Rate of Inflation

It was assumed that general inflation would be approximately 10% per annum.

The rate of medical inflation has, in the past, exceeded the general inflation rate. We have assumed that the contributions required in respect of the medical scheme will increase at the same rate as medical inflation.

It has been assumed that medical inflation will be 11% per annum.

3.3.3 Retirement Age

It was assumed that all members would retire at age 60.

3.3.4 Withdrawal Rates

If an employee leaves employment or discontinues membership of the medical scheme, the liability in respect of medical costs after retirement will not emerge. Therefore, in order not to overstate the liability, it is necessary to make assumptions regarding withdrawal rates. The assumed rates of withdrawal are set out in appendix 1.

3.3.5 Mortality Rates

In service members: Mortality before retirement has been based on 75% of the SA 72/76 ultimate mortality table for males and 50% of the SA 72/76 ultimate mortality table for females.

Pensioners: Mortality after retirement has been based on the a(55) ultimate mortality table.

3.3.6 Continuation Membership

It has been assumed that all in service members reaching retirement will elect to continue as members of the medical scheme after retirement.

3.3.7 Marital Status and Dependant's ages

We have used the actual marital status and dependants age for existing continuation and active members.

To value the liability on death before retirement, we used the same assumptions regarding the proportion married at each age, the number of children and the age of the children and spouse as for the 1 January 2000 valuation. These are outlined in Appendix 1

3.3.8 Expenses

We have not allowed for any administration costs.

SECTION 4 - RESULTS

4.1 Past Service Liability

We have valued the assets and past service liability in accordance with the method and assumptions in Section 3. The previous liability is shown for comparison.

The liability in respect of service accrued to date is as follows:

Accrued Liability	R'000	01/08/2000	01/08/1999
In Service Members		402 693	315 057
Continuation Members		623 296	631 777
Pre 1 April 1990	533 856		
1 April 1990 to 1 January 1994	77 034		
Post 1 February 1994	12 406		
Total Accrued		1 025 989	946 834
In Service Member Contribution		139 251	109 475
Continuation Member Contributions		395 816	429 710
Pre 1 April 1990	342 227		
1 April 1990 to 1 January 1994	48 907		
Post 1 February 1994	4 682		
Total Member Contribution		535 067	539 185
Employer's Accrued Liability		490 922	407 649

Assets	01/08/2000 R '000
Total	671 600

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Funding Level	01/08/2000	01/08/1999
Assets (R'000)	671 600	596 607
Employer's Accrued Liability (R'000)	490 922	407 649
Surplus (Deficit) (R'000)	180 678	188 958
Funding Level	136,8%	146,4%

4.2 Future Service Liability

The future service liability of current In-Service Members is as follows:

Future Service Liability	01/08/2000	01/08/1999
Total Liability (R'000)	453 579	332 226
Future Member Contributions (R'000)	153 686	112 645
Net Employer Liability (R'000)	299 893	219 581

4.3 Required Contribution

The present value of the net future service liability amounts to R 299 893 000. This is larger than the surplus in the Fund based on past service. An additional contribution equal to R 119 215 as at 1 August 2000 is therefore required to fund the future service deficit.

4.4 Comments of Results

Data

The dates used to classify the continuation members into the three categories mentioned above differs from that used in the previous valuation. This does however not affect the size of accrual of the liability.

Valuation Basis

- The increase in the liabilities can be partly explained by the change in the valuation basis, necessitated by lower expected after tax returns.
- Furthermore, we do expect the liabilities to grow as the interest rate effect unwinds.
- This increase in liabilities has to some extent been offset by the fact that the assumed increase in the medical scheme contribution rate had not yet materialised at the valuation date.

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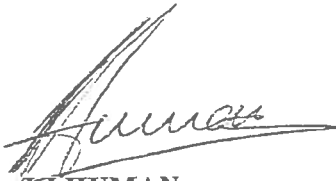
SECTION 5 – CONCLUSION

The past service liability for existing continuation members and for accrued service in respect of in-service members has been calculated as R 490 922 000. The value of the assets held to meet these liabilities is R 671 600 000. The accrued surplus therefore amounts to R 180 678.

The total future service liability of in-service members amounts to R 299 893 000. There is therefore a total shortfall of R 119 215 000 as at 1 August 2000.

The cost is directly related to the level of medical aid inflation before and after retirement. The results are also sensitive to the assumptions made. It is important to remember however, that the actual cost is dependent on actual experience, not assumptions made.

The attached appendices show more details of the assumptions used and the breakdown into some of the various categories requested.



JJ HUMAN

BBusSc FIA

In my capacity as an actuary and director of
Jacques Malan & Associates,
Consultants and Actuaries (Pty) Ltd



N SMIT

BCom(Cons)

In my capacity as an employee of
Jacques Malan & Associates,
Consultants and Actuaries (Pty) Ltd



Jacques Malan & Associates

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14 November 2000

Mr Nico Bianco
Principal Officer
Denel Medical Benefit Fund
Denel Building
Jochemus Street
ERASMUSKLOOF

Dear Sir

Sensitivity Analysis for the Actuarial Valuation Report as at 1st August 2000

Our actuarial report regarding the post-retirement healthcare liability for Denel is based on various assumptions. The liabilities calculated are thus a function of these assumptions. The actual liability which arises over time will be determined by the actual experience of the membership and the level of medical aid inflation.

In order to show the sensitivity of the liability to changes in the assumptions we have carried out tests to determine the effect should the actual experience be different from that assumed.

1 Investment Return

The size of the liability is sensitive to the investment return assumption. The absolute rates are not as important as the difference between the investment return assumption and the medical aid inflation assumption. It is this difference which has the biggest influence on the size of the current liability.

We have assumed that the investment return will be 11% and 13%, i.e. 0% and 2% greater than the assumed medical aid inflation rate of 11% respectively. The valuation was based on investment return of 12%.

The results are set out below, but the impact can be summarised as follows:

Investment return of 11% (i.e. equal to the assumed medical aid inflation)	:	increase in net past service liabilities in respect of in-service members of 24,4%
	:	increase in net liabilities in respect of continuation members of 13,6%
	:	increase in total net employer past service liabilities of 19,4%
Investment Return of 13% (i.e. 2% higher than the medical aid inflation)	:	decrease in net past service liabilities in respect of in-service members of 18,8%
	:	decrease in net liabilities in respect of continuation members of 11,1%
	:	decrease in total net employer liabilities of 15,2%

We also calculated the effect of the change in the assumption on the future service liability. This had the following effect:

A decrease in the Investment Return assumption to 11% led to a 29,4% increase in the net employer future service liability.

An increase in the assumption to 13% led to a decrease in the net employer future service liability of 21,8%.

These results can be summarised as follows:

	Valuation (1% Real)	0% Real	2% Real
Net Accrued Liability (R'000)	490 922	586 190	416 242
- In-service Members	263 442	327 820	214 043
- Continuation Members	227 480	258 370	202 199
Future Service Employer Liability (R'000)	299 893	388 064	234 491
Total Liability (R'000)	790 815	974 254	650 733



**Actuarial Valuation of the Liability in respect of Medical
Scheme Costs for Current and Future Continuation
Members of DENEL Medical Benefit Trust**

As at 1 April 2003

*Prepared by : Jacques Malan & Associates
Consultants and Actuaries*

April 2003

*C. W
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SECTION 1 - INTRODUCTION

The purpose of this report is to calculate the value of the Denel Medical Benefit Trust's liabilities in respect of medical costs of retirees (current and future) as at 1 April 2003. We have done an actuarial valuation of the medical costs liability as at 1 April 2002.

We have calculated the liability based on the 2003 Umed contribution table (outlined in Appendix 3) and valuation data. The Trust's Liability is limited to $2/3^{\text{rd}}$ of the total future contributions with the continuation members paying $1/3^{\text{rd}}$. (The employer will no longer meet the difference between the total medical costs and the contributions paid by the continuation members.) In addition, members who are also members of the Denel Pension Fund will receive an amount from the Pension Fund to meet their medical aid contributions. This amount totals approximately 85% of each member's total contribution. For these members we have therefore assumed the Fund's Liability is limited to 15% of the future contributions.

We have calculated the liability towards total future contributions and then offset the present value of future member contributions in order to determine the Denel Medical Benefit Trust's liability towards future medical costs.

SECTION 2 – MEMBERSHIP DATA

The valuation data was provided by UMED as at February 2003.

Subsidies are only payable to members that joined DENEL before 1 April 2000. It was assumed that members joined UMED on the same date that they joined DENEL.

The membership data on which the calculations are based can be summarised as follows. Previous data is shown for comparison purposes.

2.1 Continuation Members

	01/04/2003	01/04/2002
Number	2557	2674
Total Annual Umed Contribution	52,497,300	R 46,458,288
Average Annual Umed Contribution	R 20,531	R 17,374
Benefit Weighted Average Age	58 years 10 months	60 years 0 months

In-Service members who were over the age of 60 were valued as if they have retired on the particular valuation date.

2.2 In-Service Members

	01/04/2003	01/04/2002
Number	4689	5017
Total Annual Umed Contribution	R 108,882,582	R 97,084,548
Average Annual Umed Contribution	R 23,221	R 19,351
Benefit Weighted Average Age	48 years 0 months	47 years 0 months
Benefit Weighted Average Past Service	17 years 6 months	16 years 5 months

The 'Annual Contribution' indicated above (for 1 April 2003) is the value of the total annual medical aid contributions paid by In-Service members and Continuation members based on the contribution table provided.

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SECTION 3 – VALUATION METHOD AND ASSUMPTIONS**3.1 Liability Valuation Method**

The liabilities have been calculated as follows:

3.1.1 Continuation Members

The liability is taken as the present value of total continuation member contributions to the medical scheme, less the portion paid by the continuation members. Continuation member contributions are projected into each future year using the assumed rate of medical inflation and are then discounted back to the valuation date using the valuation rate of interest. The portion paid by the continuation members themselves differs according to whether they are members of the Denel Pension Fund or not. Contributions of 85% of the total medical contributions will be paid by the Denel Pension Fund on behalf of members on the Fund. All other members will make contributions of a 1/3 of their total medical contributions.

For each continuation member the projections are based on the probability of survival as per the mortality table outlined in section 3.3.5.

3.1.2 In-Service Members

The liability is also taken as the present value of total future continuation member contributions to the medical scheme, less the portion paid by the continuation members. Future contributions are projected into each future year using the assumed rate of medical inflation and are then discounted back to the valuation date using the valuation rate of interest. The portion paid by the future continuation members themselves also differs according to whether they are members of the Denel Pension Fund or not. Contributions of 85% of the total medical contributions will be paid by the Denel Pension Fund on behalf of members on the Fund. All other members will make contributions of a 1/3 of their total medical contributions.

For each member this projection is based on the probability of survival to retirement age and beyond, taking into account the assumed rates of withdrawal and mortality, as outlined in section 3.3.

3.2 Asset Valuation Method

All the assets were valued at market value. The total market value of assets was then adjusted for Debtors and Creditors.

The market value of the assets on 31 March 2003 was provided to us by the Denel Medical Benefit Trust.

The asset value as at 1 April 2003 amounts to R 748 720 000 and was determined as follows:

	(R'000)	(R'000)
Market Value as at 31 March 2003		708 709
Current Assets as at 31 March 2003		43 487
Bank	631	
Debtors	15 856	
Short Term Investments	27 000	
Current Liabilities as at 31 March 2003		(3 476)
Tax Provision	(3 285)	
Creditors	(191)	
Adjusted Market Value as at 1 April 2003		748 720

3.3 Actuarial Assumptions

In order to carry out the valuation, it is necessary to make a number of assumptions.

The various assumptions should be assessed, not in isolation, but rather in relation to each other, e.g. interest rates and medical costs increases have historically tended to move in the same direction as they are both linked to inflation to a large extent. The difference between the two assumptions is, therefore, more important than the individual absolute values.

The actuarial assumptions used in this valuation are reviewed below, and summarised in Appendix 1.

3.3.1 Rate of Interest

The interest rate assumption reflects the investment return expected if funds are set aside to meet the emerging liabilities.

It has been assumed that any investments held on behalf of the Trust would yield a return of 12% per annum.

3.3.2 Rate of Inflation

It was assumed that general inflation would be approximately 7% per annum.

Salary inflation was assumed to be 8% per annum. The rate of medical inflation has, in the past, exceeded the general inflation rate. We have assumed that the contributions required in respect of the medical scheme will increase at the same rate as medical inflation. It has been assumed that medical inflation will be 9% per annum.

Note that the assumptions for the previous valuation results (based on a 2% real valuation rate) were as follows:

General Inflation	: 8% p.a.
Salary Inflation	: 9% p.a.
Medical Inflation	: 10% p.a.
Investment Return	: 12% p.a.

We have adjusted the general inflation assumption from 8% p.a. to 7% p.a. as the South African monetary authorities have shown their resolve to reduce inflation to levels closer to the targets they have set.

Furthermore, the salary inflation and medical inflation rates are expected to stay in line with general inflation. We have therefore adjusted these assumptions so that the relationship between them remains consistent with respect to the previous year.

The investment return assumption was maintained at 12% p.a. This implies that we have assumed a higher rate of real investment return (the difference between nominal investment return and inflation) than in the previous valuation. The main reason for this is that assets are currently at very low historic levels when we consider the dividend yields and price/earnings ratios of the ALSI 40 index. AC116 requires that we use realistic best estimate assumptions for both asset values and investment returns. AC116 further requires that assets be valued at market value.

The asset value has depreciated since our previous valuation. As such, a higher expected return on the current asset value is in fact consistent with our previous valuation assumption, which used a lower real return on a higher asset valuation.

It should be kept in mind that the investment return assumption is a long term assumption and should generally remain constant over time. However, this would be inconsistent with valuing assets on a market value basis. If it were not for the requirements of AC116, we would have preferred to adjust the actuarial value of assets rather than the long term investment return assumption.

3.3.3 Retirement Age

It was assumed that all members would retire at age 60.

3.3.4 Withdrawal Rates

If an employee leaves employment or discontinues membership of the medical scheme, the liability in respect of medical costs after retirement will not emerge. Therefore, in order not to overstate the liability, it is necessary to make assumptions regarding withdrawal rates. The assumed rates of withdrawal are set out in Appendix 1.

3.3.5 Mortality Rates

In service members: Mortality before retirement has been based on 75% of the SA 72/76 ultimate mortality table for males and 50% of the SA 72/76 ultimate mortality table for females.
Pensioners: Mortality after retirement has been based on the a(55) ultimate mortality table.

3.3.6 Continuation Membership

It has been assumed that all in service members reaching retirement will elect to continue as members of the medical scheme after retirement.

3.3.7 Marital Status and Dependant's ages

We have used the actual marital status and dependants' ages for existing continuation and active members for pre- and post-retirement.

We did not make any allowance for future marriages, divorces or additional dependant children.

In order to allow for the possibility of dependant children studying fulltime after the age of 21, we assumed that all dependant children will be eligible for medical benefits until age 25.

3.3.8 Expenses

We have not allowed for any administration costs.

SECTION 4 - RESULTS

The results of the Valuation based on the assumptions in Section 3.3 are given in this section. A Sensitivity analysis based on different scenarios is given in Section 5.1. The results of the 1 April 2002 Valuation are given for comparative purposes.

4.1 Liability

	01/04/2003 (R'000's) (3% real)	01/04/2002 (R'000's) (2% real)
In Service Members	867,324	845,240
Continuation Members	536,583	603,684
Total Liability	1,403,907	1,448,924
In Service Members' Contributions	296,763	289,310
Continuation Members' Contributions	315,825	365,334
Total Members' Contributions	612,587	654,644
Trust's Liability	791,320	794,280

The Trust liability comprises the Past and Future Service Liabilities. These liabilities can be split as follows :

	Past Service Liability	Future Service Liability	Total
In Service Members	R 343,023,133	R 227,539,054	R 570,562,187
Continuation Members	R 220,757,424		R 220,757,424
Trust's Liability	R 563,780,557	R 227,539,054	R 791,319,611

4.2 Funding Level

	01/04/2003 (R'000's) (3% real)	01/04/2002 (R'000's) (2% real)
Market Value of Assets	748,720	805,649
Trust's Liability (Past and Future Service)	791,320	794,280
Surplus (Deficit)	(42,600)	11,369
Funding Level	94.62%	101.40%

In order to estimate the required contributions to be paid to fund the deficit, we have assumed that the annual contributions will increase in line with salary increases. This was estimated to be 8% per annum.

The contributions were calculated to reduce the deficit to zero over the average future working lifetime of the members. This is equal to 16 years without taking into account any possible

reduction in the retirement age. The annual contribution required to fund the deficit amounts to R 3 656 000.

Note that the above-mentioned funding level is the position when considering the total liability (i.e. past service and future service liability). For the purposes of AC116, it is the past service liability that needs to be considered. The liability and funding level on the AC116 basis is given in Section 6.

4.3 Comments on Results

The changes in the Trust's Liability during the inter-valuation period can be analysed as follows:

	(R'000's)
Liability as at 1 April 2002	794,280
Interest Cost	95,314
Payments for Continuation Members	(17,341)
Actuarial Adjustments	(80 933)
1. Inflation Cost	44,235
2. Mortality/Withdrawal/Retirement Experience	(17 339)
3. Change in Valuation Basis	(122,150)
4. New Active Members and Continuation Members	14,136
5. Miscellaneous	185
Liability as at 1 April 2003	791,320

Interest Cost

Based on a valuation interest rate assumption of 12% per annum, the liabilities of those active members and continuation members as at 31 March 2002 who were still entitled to post-employment subsidies as at 31 March 2003 would increase by this percentage.

Actuarial Adjustment

The Actuarial adjustment is the net effect of the following :

1. Inflation Cost

The actual medical inflation experienced by members on Option 1 was 11% while that of the members on Option 2 was 15%. This difference in inflation from that assumed in the previous valuation and that actually experienced by the Trust has resulted in an increase in Liability.

2. Mortality/Withdrawal/Retirement Experience

The actual movements out of the group of employees and continuation members qualifying for subsidies after employment were different from that assumed at the previous valuation. This item reflects the release of liability of active members who became continuation members during the inter-valuation period. This resulted in a profit for the Trust.

3. Change in Valuation Method

At the previous valuation we assumed that future medical inflation would be 10% per annum. We have changed our assumption for future medical inflation to 9% per annum. This change in valuation basis has resulted in a profit for the Trust.

4. New Active Members and Continuation Members

No provision was made at the previous valuation for additional members. There were additional active members who were employed prior to 1 April 2000 and who joined Umed after the previous valuation. There was an increase in liability as a result of the inclusion of these members in the valuation. This item also includes the new continuation members who were active members at the previous valuation.

5. Miscellaneous

The "Actuarial Adjustment" arises from the fact that it is virtually impossible to reconcile the Medical Aid Subsidy Liability on a daily individual basis as is necessary to get an exact balance. The adjustment should be small, may be positive or negative in any one year and is such that the build up of the Medical Cost Subsidy Liability account reconciles to the value of the liability on the valuation date.

SECTION 5 – SENSITIVITY ANALYSIS

We have been requested to calculate the impact of changes in future medical inflation on the liability of the Denel Medical Benefit Trust.

5.1 Medical Inflation (Total Liability)

We have recalculated the Liability by increasing and decreasing the medical inflation assumption by 1%. In other words, the Liability was revised based on a 2% and 4% real interest rate respectively.

Liability

	01/04/2003 (R'000) 2% Real Interest	01/04/2003 (R'000) 3% Real Interest	01/04/2003 (R'000) 4% Real Interest
In Service Members	1,058,365	867,324	718,479
Continuation Members	585,101	536,583	494,722
Total Liability	1,643,466	1,403,907	1,213,201
In Service Members' Contributions	361,705	296,762	246,128
Continuation Members' Contributions	343,426	315,825	291,950
Total Members' Contributions	705,131	612,587	538,078
Trust's Liability	938,335	791,320	675,123

Funding Level

	01/04/2003 (R'000) 2% Real Interest	01/04/2003 (R'000) 3% Real Interest	01/04/2003 (R'000) 4% Real Interest
Market Value of Assets	748,720	748,720	748,720
Trust's Liability	938,335	791,320	675,123
Surplus (Deficit)	(189,615)	(42,600)	73,597
Funding Level	79.80%	94.62%	110.90%

Required Contributions

The initial annual contributions required to fund the deficit amounts over the average future lifetime of working members are as follows:

	01/04/2003 (R'000) 2% Real Interest	01/04/2003 (R'000) 3% Real Interest	01/04/2003 (R'000) 4% Real Interest
Surplus (Deficit)	(189,615)	(42,600)	73,597
Annual Required Contribution*	15,096	3,656	-

*The annual contributions should increase in line with salary increases.

From the above results one can see that a small change in the assumption on the difference between the investment return and the medical aid inflation can have a significant effect on the size of the deficit and the subsequent Annual Required Contributions. It is therefore very important that the liability be valued at regular intervals in order to assess the effect of actual experience differing from the assumptions.

5.2 Medical Inflation (Past Service Liability)

We have recalculated the Past Service Liability by increasing and decreasing the medical inflation assumption by 1%. In other words, the Past Service Liability was revised based on a 2% and 4% real interest rate respectively.

	01/04/2003 (R'000) 2% Real Interest	01/04/2003 (R'000) 3% Real Interest	01/04/2003 (R'000) 4% Real Interest
Market Value of Assets	748,720	748,720	748,720
Trust's Past Service Liability (AC116)	653,397	563,781	491,463
Surplus (Deficit)	95,323	184,939	257,257
Funding Level	114.59%	132.80%	152.35%

Denel doesn't need to make any contribution with respect to the Past Service Liability because the funding level exceeds 100% in all three inflation rate scenarios.

SECTION 6 – ACCOUNTING IMPLICATIONS

We have assessed the accounting implications to the Trust according to AC116 and based on a real investment return assumption of 3% p.a. A sensitivity analysis based on different scenarios is given in Section 5.2. The liabilities as at 1 April 2003 on the basis of AC116 are as follows :

	Accrued Defined Benefit Obligation
In Service Members	R 343,023,133
Continuation Members	R 220,757,424
Trust's Liability (AC116)	R 563,780,557

As at 1 April 2003 the Asset Value amounts to R748 720 000 and is therefore greater than the Accrued Defined Benefit Obligation. This results in a funding level of 132,8%.

There are currently no unrecognised actuarial losses or past service costs, neither are there any economical benefits to the Employer expected in the future. As such, according to paragraph 59 of AC116, there is therefore no requirement to disclose the actuarial surplus on the balance sheet.

SECTION 7 – CONCLUSION

The Total Liability for the future medical contributions payable with respect to In-Service Members and current Continuation Members amounts to R 1 403 907 000.

The Present Value of contributions payable by In-Service Members and current Continuation Members amounts to R612 587 000.

The Trust Liability is therefore equal to R 791 320 000. Assets are valued at R 748 720 000. This results in a deficit of R 42 600 000.

The cost is directly related to the level of medical aid inflation before and after retirement. The results are also sensitive to the assumptions made. It is important to remember however, that the actual cost is dependent on actual experience, not assumptions made.

The attached appendices show more details of the assumptions used and the breakdown into some of the various categories requested.

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BBusSc FIA

In my capacity as an actuary and director of
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Consultants and Actuaries (Pty) Ltd

R BOTHA

BCom(Hons)

In my capacity as an employee of
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APPENDIX 1 – ACTUARIAL ASSUMPTIONS

The valuation has been conducted on the basis of the following assumptions:

1.1 Interest

An interest rate of 12% has been used to discount future liabilities.

1.2 Inflation

It was assumed that general inflation would be 7% per annum and that medical contributions would increase at a rate of 9% per annum. This is lower than the 10% per annum future medical inflation assumed as at the previous valuation.

1.3 Mortality

Pre-retirement: 75% of SA 72/76 ultimate for Males
50% of SA 72/76 ultimate for Females

Post-retirement: a(55) ultimate.

1.4 Withdrawal

Early withdrawal from the service of the employer or from the medical aid scheme was taken into account as follows:

Age	Annual Rate of Withdrawal
20	20%
30	15%
35	10%
45	0%

1.5 Retirement Age

All Members : 60 years

1.6 Dependants at Retirement

We have used actual marital status and spouse's and children's ages for both existing and future continuation members.

1.7 Continuation Membership

It has been assumed that all in-service members reaching retirement elect to continue as medical scheme members.

1.8 **Marital Status and Dependant's ages**

Actual marital status and dependants' ages for existing continuation and active members for pre- and post-retirement.

Dependant children are eligible until age 25.

1.9 **Expenses**

We have not allowed for any administration costs.

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APPENDIX 2 – MEMBERSHIP DATA

2.1.1 Active Members

The Active membership data as at 1 April 2003, by Age category and Benefit Option is as follows. This is based on the 2003 contribution rates as outlined in Appendix 3.

Age band	Data	Benefit Option		
		Option 1	Option 2	Grand Total
21 - 30	Number of Main Members	77	188	265
	Total Liability	812,088	4,479,806	5,291,894
	Total Employer Liability	541,392	2,966,843	3,508,235
	Total Current Umed Contributions	60,419	299,794	360,213
	Number of Dependants	59	176	235
31 - 40	Number of Main Members	238	920	1,158
	Total Liability	8,896,284	85,602,957	94,499,241
	Total Employer Liability	5,930,856	56,808,610	62,739,466
	Total Current Umed Contributions	220,854	1,873,412	2,094,266
	Number of Dependants	441	2,127	2,568
41 - 50	Number of Main Members	248	1,898	2,146
	Total Liability	26,022,084	413,415,069	439,437,154
	Total Employer Liability	17,260,129	274,063,934	291,324,063
	Total Current Umed Contributions	265,836	4,121,976	4,387,812
	Number of Dependants	657	5,282	5,939
51 - 60	Number of Main Members	84	942	1,026
	Total Liability	12,399,943	286,945,350	299,345,293
	Total Employer Liability	8,120,967	186,674,334	194,795,301
	Total Current Umed Contributions	87,902	1,964,988	2,052,889
	Number of Dependants	164	1,862	2,026
60 +	Number of Main Members	5	89	94
	Total Liability	696,588	28,053,333	28,749,920
	Total Employer Liability	410,526	17,784,596	18,195,122
	Total Current Umed Contributions	4,197	174,171	178,368
	Number of Dependants	5	118	123
Total Number of Main Members		652	4,037	4,689
Total Liability		48,826,986	818,496,516	867,323,502
Total Employer Liability		32,263,869	538,298,318	570,562,187
Total Current Umed Contributions		639,207	8,434,341	9,073,548
Total Number of Dependants		1,326	9,565	10,891

2.1.2 Continuation Members

The Continuation membership data as at 1 April 2003, by Age category and Benefit Option is as follows. This is based on the 2003 contribution rates as outlined in Appendix 3.

Age band	Calculation Description	Benefit Option		Grand Total
		Option 1	Option 2	
< 30	Number of Main Members	0	7	7
	Total Liability	0	641,691	641,691
	Total Employer Liability	0	304,172	304,172
	Total Contributions	0	8,062	8,062
	Number of Dependants	0	6	6
31 - 40	Number of Main Members	1	26	27
	Total Liability	172,901	11,109,718	11,282,619
	Total Employer Liability	115,267	5,102,468	5,217,735
	Total Contributions	619	47,390	48,009
	Number of Dependants	0	63	63
41 - 50	Number of Main Members	12	162	174
	Total Liability	2,422,918	57,473,195	59,896,113
	Total Employer Liability	904,901	23,155,744	24,060,646
	Total Contributions	11,894	281,825	293,719
	Number of Dependants	30	284	314
51 - 60	Number of Main Members	21	613	634
	Total Liability	3,148,331	180,320,991	183,469,322
	Total Employer Liability	1,335,180	96,232,571	97,567,752
	Total Contributions	19,424	1,144,649	1,164,073
	Number of Dependants	29	721	750
61 - 70	Number of Main Members	46	933	979
	Total Liability	4,971,926	194,382,673	199,354,599
	Total Employer Liability	2,072,019	75,815,172	77,887,191
	Total Contributions	42,373	1,667,064	1,709,437
	Number of Dependants	34	744	778
70 +	Number of Main Members	21	715	736
	Total Liability	1,438,630	80,499,558	81,938,188
	Total Employer Liability	252,082	15,467,846	15,719,928
	Total Contributions	19,382	1,132,094	1,151,476
	Number of Dependants	14	353	367
Total Number of Main Members		101	2,456	2,557
Total Liability		12,154,705	524,427,827	536,582,532
Total Employer Liability		4,679,450	216,077,974	220,757,425
Total Contributions		93,692	4,281,084	4,374,775
Total Sum of Dependants		107	2,171	2,278

The following tables provide a membership summary subdivided by business division.

2.2.1 Active Members

Business Division	Calculation Description	Benefit Option		Grand Total
		Option 1	Option 2	
Denel Aviation (2)	Number of Main Members	19	607	626
	Average of Main age	44	45	45
	Total Liability	1,877,723	121,494,631	123,372,354
	Total Accrued Liability	661,521	48,319,603	48,981,124
	Number of Dependants	48	1,416	1,464
PMP (3)	Number of Main Members	95	338	433
	Average of Main age	38	44	42
	Total Liability	4,982,493	61,954,862	66,937,355
	Total Accrued Liability	1,101,378	24,010,135	25,111,513
	Number of Dependants	166	739	905
LIW (4)	Number of Main Members	2	205	207
	Average of Main age	34	44	44
	Total Liability	29,210	39,852,446	39,881,656
	Total Accrued Liability	6,898	14,212,526	14,219,424
	Number of Dependants	0	552	552
SWARTKLIP (5)	Number of Main Members	60	71	131
	Average of Main age	42	49	45
	Total Liability	4,861,996	17,322,850	22,184,847
	Total Accrued Liability	1,547,314	7,688,966	9,236,280
	Number of Dependants	124	171	295
NASCHEM (6)	Number of Main Members	91	166	257
	Average of Main age	41	45	44
	Total Liability	6,567,671	34,391,054	40,958,725
	Total Accrued Liability	2,158,624	13,926,311	16,084,935
	Number of Dependants	213	429	642
SOMCHEM (7)	Number of Main Members	208	236	444
	Average of Main age	45	48	46
	Total Liability	20,910,430	58,371,784	79,282,214
	Total Accrued Liability	8,517,114	25,959,594	34,476,708
	Number of Dependants	504	640	1,144
DENPROP (9)	Number of Main Members		5	5
	Average of Main age		45	45
	Total Liability		823,547	823,547
	Total Accrued Liability		312,754	312,754
	Number of Dependants		10	10
ARIVIA KOM (13)	Number of Main Members		145	145
	Average of Main age		40	40
	Total Liability		20,106,830	20,106,830
	Total Accrued Liability		5,590,347	5,590,347
	Number of Dependants		306	306

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UMED (14)	Number of Main Members	2	13	15
	Average of Main age	39	43	43
	Total Liability	144,784	2,058,293	2,203,077
	Total Accrued Liability	44,587	713,436	758,023
	Number of Dependants	4	24	28
KENTRON (16)	Number of Main Members	40	521	561
	Average of Main age	39	45	45
	Total Liability	2,214,891	106,173,535	108,388,426
	Total Accrued Liability	632,148	41,373,705	42,005,853
	Number of Dependants	54	1,240	1,294
VEKTOR (19)	Number of Main Members	13	128	141
	Average of Main age	44	44	44
	Total Liability	759,272	24,895,719	25,654,992
	Total Accrued Liability	131,679	8,943,574	9,075,252
	Number of Dependants	18	325	343
ELOPTRO (20)	Number of Main Members	6	98	104
	Average of Main age	44	45	45
	Total Liability	467,829	19,694,179	20,162,008
	Total Accrued Liability	197,330	7,122,966	7,320,297
	Number of Dependants	7	217	224
PTB (24)	Number of Main Members	41	95	136
	Average of Main age	39	46	44
	Total Liability	2,755,289	20,821,088	23,576,377
	Total Accrued Liability	907,198	8,139,989	9,047,187
	Number of Dependants	82	255	337
HOUWTEQ (26)	Number of Main Members		7	7
	Average of Main age		47	47
	Total Liability		1,423,559	1,423,559
	Total Accrued Liability		693,259	693,259
	Number of Dependants		16	16
CSIR (MECHEM) (29)	Number of Main Members	1	33	34
	Average of Main age	31	44	44
	Total Liability	34,573	6,715,786	6,750,359
	Total Accrued Liability	5,105	2,119,632	2,124,737
	Number of Dependants	1	80	81
PMP (BESTUUR) (32)	Number of Main Members		24	24
	Average of Main age		49	49
	Total Liability		6,082,848	6,082,848
	Total Accrued Liability		2,609,319	2,609,319
	Number of Dependants		58	58
NASCHEM (BESTUUR) (35)	Number of Main Members		6	6
	Average of Main age		44	44
	Total Liability		1,169,043	1,169,043
	Total Accrued Liability		369,500	369,500
	Number of Dependants		21	21
DENEL (40)	Number of Main Members	3	75	78
	Average of Main age	40	45	45
	Total Liability	179,338	14,607,327	14,786,665
	Total Accrued Liability	37,470	4,950,351	4,987,821
	Number of Dependants	5	171	176

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DENEL (BESTUUR) (48)	Number of Main Members		34	34
	Average of Main age		52	52
	Total Liability		9,507,742	9,507,742
	Total Accrued Liability		4,432,861	4,432,861
	Number of Dependants		94	94
SITA (49)	Number of Main Members		302	302
	Average of Main age		44	44
	Total Liability		56,366,645	56,366,645
	Total Accrued Liability		20,927,404	20,927,404
	Number of Dependants		719	719
AMG (50)	Number of Main Members	4	254	258
	Average of Main age	43	48	48
	Total Liability	298,571	57,422,865	57,721,436
	Total Accrued Liability	125,884	27,390,966	27,516,850
	Number of Dependants	5	513	518
AMG (51)	Number of Main Members	10	251	261
	Average of Main age	36	46	46
	Total Liability	481,203	55,390,444	55,871,647
	Total Accrued Liability	187,683	25,289,076	25,476,759
	Number of Dependants	12	582	594
LA FORGE (53)	Number of Main Members		16	16
	Average of Main age		49	49
	Total Liability		3,771,677	3,771,677
	Total Accrued Liability		1,256,178	1,256,178
	Number of Dependants		31	31
DPS (57)	Number of Main Members	6	66	72
	Average of Main age	41	46	46
	Total Liability	473,775	13,726,265	14,200,041
	Total Accrued Liability	96,066	4,877,206	4,973,273
	Number of Dependants	14	156	170
SIMERA (62)	Number of Main Members	1	12	13
	Average of Main age	53	50	50
	Total Liability	151,300	3,140,877	3,292,177
	Total Accrued Liability	81,654	1,390,576	1,472,229
	Number of Dependants	2	29	31
AMIANTIT (65)	Number of Main Members	5	1	6
	Average of Main age	45	54	47
	Total Liability	603,295	290,309	893,603
	Total Accrued Liability	215,920	157,900	373,820
	Number of Dependants	12	3	15
SPP (69)	Number of Main Members	45	29	74
	Average of Main age	31	42	35
	Total Liability	1,033,346	4,437,441	5,470,787
	Total Accrued Liability	118,889	1,451,543	1,570,432
	Number of Dependants	55	64	119
SPARTAN (ARIVIA) (70)	Number of Main Members		15	15
	Average of Main age		37	37
	Total Liability		1,534,274	1,534,274
	Total Accrued Liability		286,929	286,929
	Number of Dependants		29	29

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TURBOMECHA AFRICA (71)	Number of Main Members		265	265
	Average of Main age		44	44
	Total Liability		51,235,433	51,235,433
	Total Accrued Liability		20,353,532	20,353,532
	Number of Dependants		623	623
FOREIGN DUTY/DENEL (96)	Number of Main Members		15	15
	Average of Main age		43	43
	Total Liability		3,045,287	3,045,287
	Total Accrued Liability		1,107,097	1,107,097
	Number of Dependants		43	43
MIT (116)	Number of Main Members		2	2
	Average of Main age		42	42
	Total Liability		375,413	375,413
	Total Accrued Liability		136,477	136,477
	Number of Dependants		5	5
ANDER PENS (191)	Number of Main Members		2	2
	Average of Main age		38	38
	Total Liability		292,462	292,462
	Total Accrued Liability		134,958	134,958
	Number of Dependants		4	4
Total Number of Main Members		652	4,037	4,689
Average of Main age		41	45	45
Total Liability		48,826,986	818,496,516	867,323,502
Total Accrued Liability		16,774,461	326,248,672	343,023,133
Total Number of Dependants		1,326	9,565	10,891

2.2.2 Continuation Members

Business Division	Calculation Description	Benefit Option		
		Option 1	Option 2	Grand Total
DENPEN PENSIONERS (91)	Number of Main Members	60	1,477	1,537
	Average of Main age	66	68	68
	Total Liability	6,626,490	258,465,632	265,092,123
	Number of Dependants	60	964	1,024
DENRET PENSIONERS (92)	Number of Main Members	41	979	1,020
	Average of Main age	59	60	60
	Total Liability	5,528,215	265,962,194	271,490,409
	Number of Dependants	47	1,207	1,254
Total Number of Main Members		101	2,456	2,557
Average of Main age		63	65	65
Total Liability		12,154,705	524,427,827	536,582,532
Total Number of Dependants		107	2,171	2,278

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APPENDIX 3 – CONTRIBUTION TABLES

The calculations have been based on the following contribution table for Umed for 2003.

	Option 1	Option 2
Member	R 603	R 1 122
Adult Dependant	R 456	R 897
Child Dependant	R 54	R 114

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Prepared by
NMG Consultants and Actuaries (Pty) Ltd
April 2021

DENEL GROUP
IAS 19 actuarial valuation report
Post-employment health care liabilities
as at 1 April 2021

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Executive summary

The primary purpose of this valuation is to enable Denel Group ('Denel') to comply with the requirements of IAS 19. The liability amounts are calculated in accordance with the amended IAS 19 accounting standards and actuarial practice note APN301 of the Actuarial Society of South Africa.

The table below shows the net liability/(asset) recognised for accounting purposes.

Net liability/(asset)

	1 April 2021 R'000	1 April 2020 R'000	1 April 2019 R'000
Liability	374 996	374 556	388 570
Assets	(1 645 114)	(1 485 729)	(1 393 868)
Net liability/(asset)	(1 270 118)	(1 111 173)	(1 005 298)
Unrecognised due to asset ceiling	1 269 250	1 110 145	1 003 803
Recognised liability/(asset)	(868)	(1 028)	(1 495)
<i>Funding level</i>	<i>438.70%</i>	<i>396.66%</i>	<i>358.72%</i>

The table below shows the expected expenses for the year ending 1 April 2022 to be recognised by Denel.

Expected expenses for the year ended 1 April 2022

	Liability R'000	Assets R'000	Net expense R'000
Service cost	211	-	211
Net interest cost	38 099	(172 471)	(134 372)
Annual expense	38 310	(172 471)	(134 161)
Expected benefit payments by DMBT	(32 986)	32 986	-

1. Introduction

NMG Consultants and Actuaries (Pty) Ltd ('NMG') has been requested by the Principal Employer, Denel and the Denel Group ('Denel') to estimate the present value of Denel's post-employment liabilities in respect of medical scheme benefits to employees, retired employees and their registered dependants ('members').

The effective date of this report is 1 April 2021. The previous valuation of Denel post-employment health care liabilities was performed by NMG as at 1 April 2020. We recommend that the next actuarial valuation be performed as at 1 April 2022.

This report contains all the information required for a full disclosure of the company's IAS 19 liability for post-employment health care and has been prepared in accordance with the ASSA APN 301 guidelines.

The following should be noted:

- The results of the valuation show the net liability and expenses that should be recognised by Denel in their annual financial statements. All liabilities shown in these results are past-service liabilities. The liabilities are therefore accrued over the working lifetime of an active employee, which results in an active employee's liability only being partially recognised.
- The discount rate assumption used to value the liability is set as prescribed by the accounting standards with reference to government bonds at a similar term of the liability. It is assumed that the assets backing these liabilities will receive an investment return equal to the risk free discount rate that is attainable in the South African market.
- The valuation implicitly allows for expenses through the net investment return.
- The valuation has been performed to comply with all the accounting requirements.

Employer beneficiaries of the Trust who have accepted a "buy-out offer" made by Denel in lieu of the post-employment health care benefit may transfer the benefit into the Denel Retirement Fund whilst pensioner beneficiaries who have accepted a "buy-out offer" could purchase an annuity option with an external insurer appointed by Denel. Members can accept these options at any time.

2. Data summaries and assumptions

2.1 Membership

Employees and continuation and widow(er) members ('CAWMs') of the Denel Medical Benefit Trust ('DMBT') participate on Discovery Health Medical Scheme ('DHMS'). Individual membership data was supplied by Momentum (administrator of the 'DMBT'), and the medical scheme administrator Discovery Health (Pty) Ltd and is effective 1 March 2021.

This report has been produced based on membership data provided by DHMS. We have not sought independent verification of any of the information provided to us, nor have we requested that the information be audited. However, we have undertaken reasonability checks and are satisfied that the data supplied to us is sufficiently accurate for the purposes of the valuation.

The membership statistics for all active employees and CAWMs who qualify for post-employment subsidies are summarised in the table below.

Status	Number of members	Subsidy weighted average age	Average past service	Proportion married	Average monthly subsidy 2021
Actives	32	60.7	33.6	59%	R4 781
CAWMs	625	71.5	-	52%	R4 032
Total	657	70.9	-	53%	R4 069

The average active employee subsidy summarised in the table above is calculated to allow for the proportion married at retirement assumptions detailed in Section 2.3.2.

The number of members who qualify for post-employment subsidies has decreased by 11 active employees and 1 CAWM since the previous valuation. These membership movements are summarised in the table below.

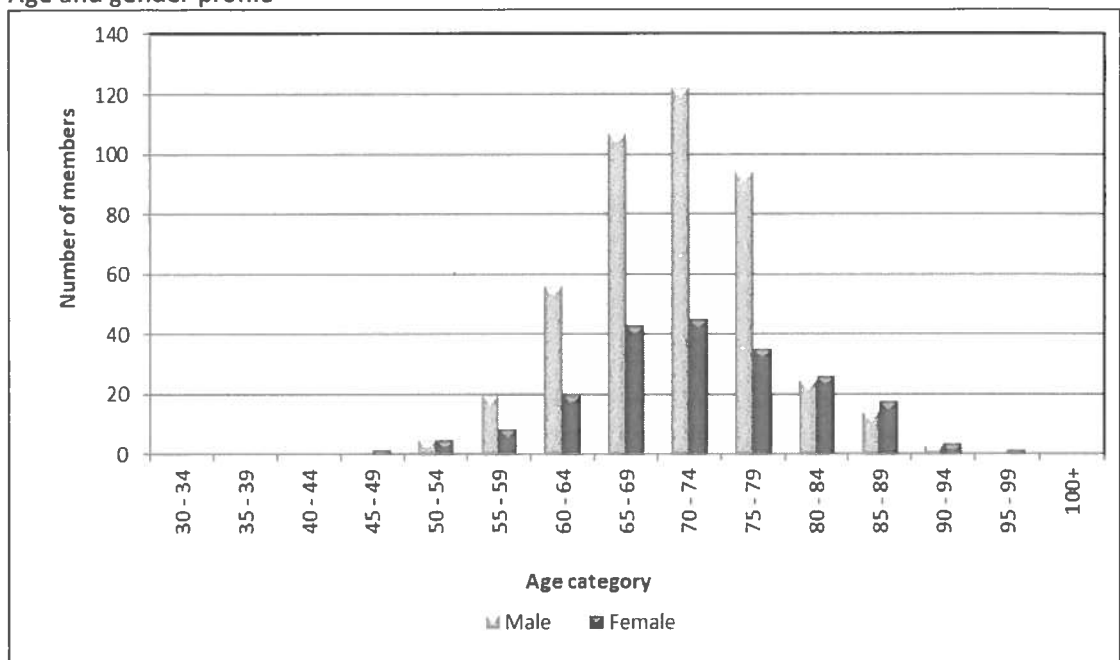
	Actives	CAWMs	Total
Number of members as at 1 April 2020	43	626	669
Deaths/Exits	-	(22)	(22)
New surviving spouses	-	7	7
Retirements	(12)	12	-
New entries	1	2	3
Members accepting the annuity	-	-	-
Number of members as at 1 April 2021	32	625	657

1 new active member and 2 new CAWMs were confirmed by the administrator as being eligible for subsidies, although not previously listed in the membership. They have been noted as new entries.

Average past service and proportion married

Age	Actual average length of service (years)	Proportion married
50-54	28.2	10%
55-59	32.5	38%
60-64	34.8	62%
65-69	35.8	59%

Age and gender profile



2.2 Benefits

We have valued the liabilities in accordance with DMBT’s subsidy policy and the DHMS benefit and contribution table that is effective as at 1 January 2021.

We have assumed that members will remain on their current medical scheme options for the next benefit year and into the future. The NRA for Denel employees is 65 years, but in line with past methodology, full accrual of benefits is reached at age 60.

The employees listed below are eligible to be members of DMBT.

- Employees who were in the employment of Denel and members of UMED before 1 April 2000.
- If an employee joined Denel after 1 April 2000 and was a member of UMED before or on 24 June 2004, the employee had until 24 June 2004 to ‘enrol’ as a beneficiary of DMBT.

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We have based our valuation on the subsidy policy detailed below.

Members who enrolled in the DMBT prior to 25 June 2004 are eligible for the following subsidies:

Subsidy policy

Members	Death-in-service and post-retirement
Denel Retirement Fund	66.67% of medical scheme contributions
Denel Pension Fund	15.00% of medical scheme contributions

Subsidies are capped at a maximum of the relevant subsidised proportion (66.67% or 15.00%) of the Essential Comprehensive membership contribution.

The valuation has been based on the monthly contributions summarised in the table below.

DHMS contributions 2021¹

Option	Principal member	Adult dependant	Child dependant	
Executive	R7 257	R7 257	R1 385	
Classic Comprehensive	R5 954	R5 633	R1 188	
Classic Delta Comprehensive	R5 362	R5 077	R1 069	
Essential Comprehensive	R5 003	R4 731	R1 008	
Essential Delta Comprehensive	R4 507	R4 257	R904	
Classic Priority	R3 814	R3 008	R1 526	
Essential Priority	R3 278	R2 577	R1 310	
Classic Saver	R3 290	R2 596	R1 318	
Classic Delta Saver	R2 628	R2 076	R1 056	
Essential Saver	R2 615	R1 961	R1 048	
Essential Delta Saver	R2 085	R1 575	R837	
Coastal Saver	R2 608	R1 962	R1 053	
Classic Core	R2 449	R1 931	R980	
Classic Delta Core	R1 960	R1 545	R784	
Essential Delta Core	R1 681	R1 265	R675	
Coastal Core	R1 946	R1 462	R774	
KeyCare Plus	R0 – R8 550	R1 207	R1 207	R439
	R8 551 – R13 800	R1 659	R1 659	R468
	R13 801+	R2 450	R2 450	R656
KeyCare Core	R0 – R8 550	R949	R949	R245
	R8 551– R13 800	R1 183	R1 183	R292
	R13 801+	R1 809	R1 809	R410
KeyCare Start	R0 – R9 150	R914	R914	R550
	R9 151– R13 800	R1 538	R1 538	R601
	R13 801+	R2 394	R2 394	R650

The benefit schedule for DHMS is available from NMG on request.

¹ An increase of 5.9% is expected 1 July 2021 and has been allowed for in the valuation.

DHMS had a statutory solvency level of 27.5% as at 31 December 2019 which exceeds the prescribed level of 25%, hence no further allowance for higher than expected cost increases in future were made.

2.3 Valuation assumptions and methodology

The post-employment health care liabilities have been valued using the Projected Unit Credit discounted cashflow method. This method was used to determine liabilities at the valuation date and projected annual expense in the year following the valuation date.

2.3.1 Financial assumptions

The key assumptions used in our calculations are shown below. The rates used have been confirmed with the employer.

Economic assumptions

Assumption	1 April 2021	1 April 2020
Consumer Price Inflation ('CPI')	6.68% p.a.	5.63% p.a.
Salary inflation	7.68% p.a.	6.63% p.a.
Health care cost inflation	8.18% p.a.	7.13% p.a.
Discount rate/ investment return	10.59% p.a.	9.60% p.a.
Real discount rate	2.23% p.a.	2.31% p.a.

The discounted mean term of the DMBT liability was approximately 8.9 years as at 1 April 2020. The CPI assumption has therefore been based on the 8.9 year yield from the South African zero coupon government bond yield curve as at 31 March 2021, as published by the Bond Exchange of South Africa. The table below shows the nominal and real yields at a 8.9 year term.

Rate	31 March 2021
Nominal yield	10.59% p.a.
Real yield	3.67% p.a.
Implied CPI	6.68% p.a.

The CPI assumption was derived by taking the difference between the nominal yield and real yield.

The discount rate/investment return was set equal to the nominal yield in accordance with IAS 19 requirements. The investment return assumption implicitly allows for investment expenses.

The health trend increase rate and salary inflation rate were set at levels of 1.5% and 1.0% above the underlying inflation rate. These additions were made to allow for the fact that medical scheme contribution increases and salary inflation are expected to outstrip general inflation over the long term.

The variable having the greatest effect on the liability is the real discount rate, i.e. the discount rate net of health care cost inflation. Even small changes to this assumption have a relatively large impact on the liabilities. We have used a real discount rate of 2.23% p.a. in the valuation.

The market values of the bond interest yields are available via subscription.

2.3.2 Demographic assumptions

Demographic assumptions

Assumption		1 April 2021	1 April 2020
Child contribution cease age		21.0 years 25.0 years if over 21.0 years	21.0 years 25.0 years if over 21.0 years
Spouse age difference	Actives	5 years	5 years
	CAWMs	Actual age difference	Actual age difference
Proportion married at retirement		Married actives: 100% Single actives: 50%	Married actives: 100% Single actives: 50%
Continuation at retirement		100%	100%

The assumptions shown above are consistent with those that are used in calculating the buy-out figures.

We have assumed that the income bands will increase annually with CPI and that an employee's salary will increase by the salary inflation assumption. The employee's salary at retirement will be used to determine the income band in retirement. Pensioners will remain in the same income band going forward.

Mortality tables

Age	Male	Female
Pre-retirement	SA85-90	SA85-90
Post-retirement	PA(90) (Males)	PA(90) (Females)

The above rates imply that the expected lifetime at retirement of a male is 18.0 years and 22.5 years for a female. This will remain the same in the future.

We allowed for medical scheme membership changes due to stated assumptions of mortality and withdrawal. Since DMBT members do not belong to a medical scheme that is closed to new entrants, we have not taken into account that the age profile of the medical scheme membership may change.

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Resignation and retirement rates

Age	Resignation		Retirement	
	Males	Females	Males	Females
35	8.00%	10.00%	0.08%	0.12%
36	7.60%	9.20%	0.11%	0.14%
37	7.20%	8.40%	0.13%	0.16%
38	6.80%	7.60%	0.16%	0.18%
39	6.40%	6.80%	0.18%	0.20%
40	6.00%	6.00%	0.21%	0.22%
41	5.60%	5.60%	0.24%	0.24%
42	5.20%	5.20%	0.28%	0.26%
43	4.80%	4.80%	0.31%	0.28%
44	4.40%	4.40%	0.35%	0.30%
45	4.00%	4.00%	0.38%	0.32%
46	3.60%	3.60%	0.47%	0.36%
47	3.20%	3.20%	0.56%	0.39%
48	2.80%	2.80%	0.64%	0.43%
49	2.40%	2.40%	0.73%	0.46%
50	2.00%	2.00%	0.82%	0.50%
51	1.60%	1.60%	1.05%	0.60%
52	1.20%	1.20%	1.28%	0.71%
53	0.80%	0.80%	1.50%	0.81%
54	0.40%	0.40%	1.73%	0.92%
55	0.00%	0.00%	31.96%	31.02%
56	0.00%	0.00%	12.17%	11.12%
57	0.00%	0.00%	12.38%	11.21%
58	0.00%	0.00%	12.58%	11.31%
59	0.00%	0.00%	12.79%	11.40%
60+	0.00%	0.00%	100.00%	100.00%

The retirement rates above include an allowance for medical disability benefits.

3. Results

3.1 Past-service liabilities

The table below summarises Denel’s past-service contractual liabilities, separately for active employees and CAWMs.

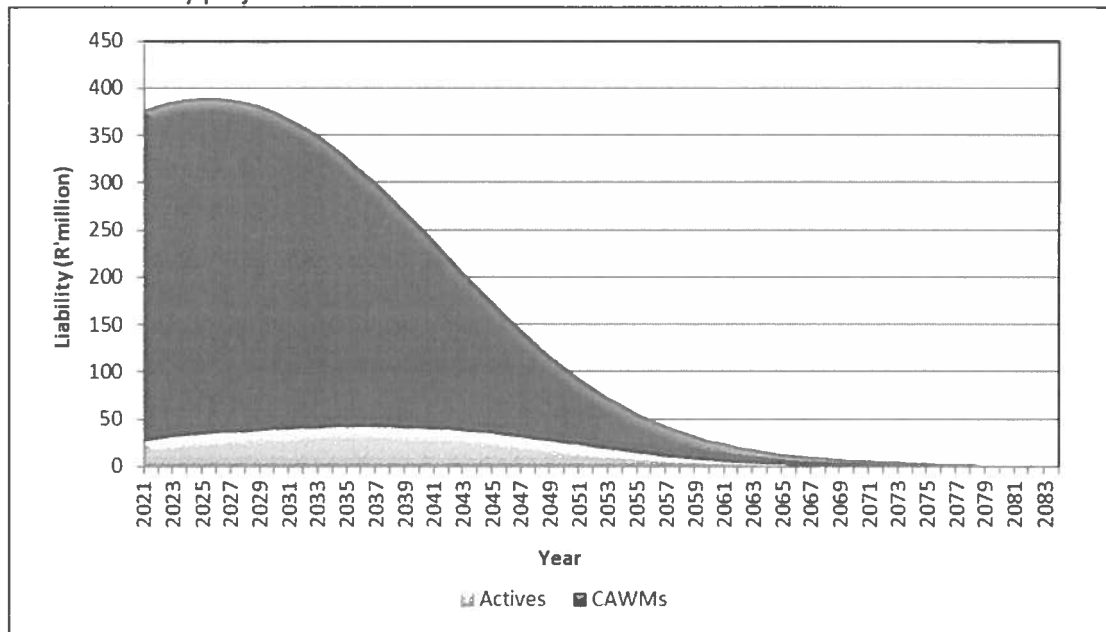
Accrued liabilities

Members	1 April 2021 R'000	1 April 2020 R'000	1 April 2019 R'000
Actives	27 431	36 464	46 264
CAWMs	347 565	338 092	342 306
All members	374 996	374 556	388 570

The discounted mean term of the liability is 8.8 years in 2021.

The liabilities shown above are in respect of the employer’s share of contributions only. Only the contractual liabilities are required to be recognised under the IAS 19 accounting standard.

Accrued liability projection



The liability recognised for accounting purposes is expected to increase until 2026. At this point benefit payments will start to exceed the service and interest costs, and will result in a decreasing recognised liability going forward. This assumes no change in the real discount rate and future membership progression is in line with assumptions and contribution increases are as assumed.

3.2 Assets

The value of the assets backing the DMBT is shown in the table below.

	Fair value of assets R'000
Assets as at 1 April 2021	1 645 114
Assets as at 1 April 2020	1 485 729
Assets as at 1 April 2019	1 393 868

The asset value as at 1 April 2021 is based on the market value of DMBT's assets as at 1 March 2021.

The strategic allocation as per the Investment Policy Statement (updated in 2018) is set as follows.

- 55% Domestic Equity
- 15% Global Equity
- 20% Domestic Fixed Interest
- 10% Domestic Cash

Small deviations are allowed and adherence is monitored on a continuous basis.

3.3 Net liability/ (asset)

The net liability/ (asset) obtained by comparing assets to liabilities is shown below.

	1 April 2021 R'000	1 April 2020 R'000	1 April 2019 R'000
Liability	374 996	374 556	409 967
Assets	(1 645 114)	(1 485 729)	(1 326 496)
Net liability/(asset)	(1 270 118)	(1 111 173)	(916 529)
Unrecognised due to asset ceiling	1 269 249 ²	1 110 145 ³	914 417
Recognised liability/(asset)	(869)	(1 028)	(2 112)
<i>Funding level</i>	<i>438.70%</i>	<i>396.66%</i>	<i>323.56%</i>

The net asset cannot be recognised by Denel according to the IAS 19 standards given that Denel cannot access the assets from the Trust to derive economic benefit, as this belong to the members of DMBT.

²In accordance with IFRIC14 guidance, the expected present value of the future service cost due on current active members that are below the assumed normal retirement age, has been used to reflect the expected benefit ('*recognised asset*') to the employer from the current projected surplus position of the fund.

³In accordance with IFRIC14 guidance, the expected present value of the future service cost due on current active members that are below the assumed normal retirement age, has been used to reflect the expected benefit ('*recognised asset*') to the employer from the current projected surplus position of the fund.

3.4 Annual expense

The projected expense in the year following the valuation date is shown below. The projected annual expense includes the cost of post-employment contributions payable by DMBT.

Expense component	Year ended 1 April 2022 R'000	Year ended 1 April 2021 R'000	Year ended 1 April 2020 R'000
Service cost	211	269	373
Net interest cost	(134 372)	(106 765)	(96 796)
- Interest cost on liability	38 099	34 315	35 827
- Interest on investments	(172 471)	(141 080)	(132 623)
Annual expense	(134 161)	(106 496)	(96 423)
Contribution payments by DMBT	(32 986)	(30 055)	(28 243)

The net interest costs are negative (i.e. reported as an income) given that the assets are larger than the liabilities for all three periods.

3.5 Sensitivity analysis

The effect of a 1% increase and decrease in the health care cost inflation assumption on the past-service contractual liability and the annual expense is shown in the table below.

Health care cost inflation

Variation	Health care cost inflation	Change in past-service contractual liability	Change in funding level	Change in service cost plus interest cost ⁴
+1%	9.18%	+8.4%	-34.1%	+8.8%
-1%	7.18%	-7.4%	+35.2%	-7.8%

The longevity of members in retirement is an important assumption, dictating the expected length of time over which benefits are paid. The effect of using lighter mortality assumptions post-employment is shown in the table below.

Mortality

Variation	Change in past-service contractual liability	Change in funding level	Change in service cost plus interest cost
PA(90)-1	+3.9%	-16.6%	+4.1%
PA(90)-2	+7.9%	-32.1%	+8.2%

⁴ Calculated on liability values

3.6 Reconciliation with results of previous valuation

The table below shows a reconciliation of the past-service contractual liabilities as at 1 April 2019 and 1 April 2020 with that as at 1 April 2021. We also set out the difference between the projected (or expected) result as at 1 April 2021 and the actual result of the valuation, i.e. remeasurements. Please note that a positive remeasurement represents an increase in the liability.

		Liability R'000	Assets R'000	(Surplus)/ deficit R'000
Past service liability as at 1 April 2019		388 570	(1 393 868)	(1 005 298)
Year ended 1 April 2020	Service cost	373	-	373
	Net interest cost	35 827	(132 623)	(96 796)
	Actual benefit payments	(28 243)	28 243	-
	Transfers into the assets	-	-	-
	Settlement	-	-	-
	Remeasurements	(21 971)	12 519	(9 452)
Past service liability as at 1 April 2020		374 556	(1 485 729)	(1 111 173)
Year ended 1 April 2021	Service cost	269	-	269
	Net interest cost	34 315	(141 080)	(106 765)
	Benefit payments	(30 055)	30 055	-
	Transfers into the assets	-	-	-
	Settlement	-	-	-
Expected past service liability as at 1 April 2021		379 085	(1 596 754)	(1 217 669)
Remeasurements		(4 089)	(48 360)	(52 449)
Actual past service liability as at 1 April 2021		374 996	(1 645 114)	(1 270 118)

The significant factors explaining the remeasurements (i.e. the difference between actual and expected results) are summarised overleaf.

The net asset cannot be recognised by Denel according to the IAS 19 standards given that Denel cannot access the assets from the Trust to derive economic benefit, as this belong to the beneficiaries of the Trust.

Factor	Liability R'000	Asset R'000
1. (Surplus)/deficit due to change in financial assumptions	1 740	-
2. (Surplus)/deficit due to actual health care cost inflation compared to that expected	(4 799)	-
3. (Surplus)/deficit due to plan changes	(2 188)	-
4. (Surplus)/deficit due to actual demographic profile of the membership compared to that expected	1 158	
5. (Surplus)/deficit due to actual investment returns compared to that expected	-	(48 360)
Total remeasurements	(4 089)	(48 360)

1. The discount rate of the current valuation has been revised to 10.59% p.a. from the 9.60% p.a. used in the 2020 valuation, with the health care cost inflation assumption increasing from 7.13% p.a. to 8.18% p.a. This resulted in a decrease in the real discount rate from 2.31% p.a. to 2.23% p.a., resulting in a deficit of approximately R1 740 000.
2. The average contribution increase that is expected to be experienced by members effective 1 January 2021 is 2.95%. This is notably lower than the expected increase of 7.13%, resulting in a surplus of approximately R4 799 000.
3. A surplus of approximately R2 188 000 can be attributed to plan changes by members and changes in the contribution structure of members' selected plans.
4. A deficit of approximately R1 158 000 on the liability is attributable to the actual demographic profile of the membership differing from that expected.
5. A surplus of approximately R48 360 000 was as a result of investment returns of 33.3%⁵ being higher than the expected return of 9.60% p.a. and any timing differences between actual and reported payments made.

⁵ Based on the internal rate of return calculated from cashflows between 1 April 2020 and 31 March 2021 and using the asset value as at 28 February 2021 as proxy for the asset value as at 1 April 2021.

3.7 Impact of asset ceiling

The table below shows the change in the impact of the asset ceiling since the previous valuation. This is based on the difference between the net liability and the present value of the future service cost of the active members.

		Net Liability/(Asset) R'000	Recognised Liability/(Asset) R'000	Unrecognised due to asset ceiling R'000
Past service liability as at 1 April 2020		(1 111 173)	1 028	(1 110 145)
Year ended 1 April 2021	Service cost	269	-	269
	Net interest cost	(106 675)	99	(106 666)
	Benefit drawdown	-	(269)	(269)
	Remeasurements	(52 449)	11	(52 438)
Past service liability as at 1 April 2021		(1 270 118)	869	(1 269 249)

A deficit of approximately R11 000 was as a result of a change in the financial assumptions and a drawdown of the expected service cost.

3.8 Ten year net liability projections

		Liability R'000	Assets R'000	Net liability/(asset) R'000
1 April 2021	Net liability/(asset)	374 996	(1 645 114)	(1 270 118)
Year ending 1 April 2022	Service cost	211		211
	Net interest cost	38 099	(172 471)	(134 372)
	Benefit payments	(32 986)	32 986	-
1 April 2022	Net liability/(asset)	380 320	(1 784 599)	(1 404 279)
Year ending 1 April 2023	Service cost	225	-	225
	Net interest cost	38 536	(188 989)	(150 453)
	Benefit payments	(34 935)	34 935	-
1 April 2023	Net liability/(asset)	384 146	(1 938 653)	(1 554 507)
Year ending 1 April 2024	Service cost	156	-	156
	Net interest cost	38 856	(205 303)	(166 447)
	Benefit payments	(36 492)	36 492	-
1 April 2024	Net liability/(asset)	386 666	(2 107 465)	(1 720 799)
Year ending 1 April 2025	Service cost	147	-	147
	Net interest cost	39 044	(223 192)	(184 148)
	Benefit payments	(37 880)	37 880	-
1 April 2025	Net liability/(asset)	387 977	(2 292 777)	(1 904 800)
Year ending 1 April 2026	Service cost	131	-	131
	Net interest cost	39 108	(244 845)	(205 737)
	Benefit payments	(39 211)	39 211	-
1 April 2026	Net liability/(asset)	388 005	(2 498 411)	(2 110 406)
1 April 2026	Net liability/(asset)	388 005	(2 498 411)	(2 110 406)
Five years ending 1 April 2031	Service cost	239	-	239
	Net interest cost	191 687	(1 584 812)	(1 393 125)
	Benefit payments	(212 626)	212 626	-
1 April 2031	Net liability/(asset)	367 305	(3 870 597)	(3 503 292)

4. Signatories

This report was prepared for the Board of Denel Group and is signed by:



Priya Makanjee
BSc (Hons) FASSA
Primary regulator: Actuarial Society of South Africa

in my capacity as an actuary of NMG Consultants and Actuaries (Pty) Ltd



Felicia Mhlanga
BSc (Hons)

in my capacity as an employee of NMG Consultants and Actuaries (Pty) Ltd

15 April 2021

Notes

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**DENEL MEDICAL BENEFIT TRUST
(TRUST NO: IT8466/02)**

**ANNUAL FINANCIAL STATEMENTS
FOR THE YEAR ENDED
29 February 2020**

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**DENEL MEDICAL BENEFIT TRUST
(TRUST NO: IT8466/02)**

FINANCIAL STATEMENTS FOR THE YEAR ENDED 29 FEBRUARY 2020

TRUSTEES AND ADMINISTRATION

TRUSTEES: HM Ivy (Chairperson)
T Zwelibanzi
PJ van der Merwe

DATE OF REGISTRATION: 5 December 2002

BENEFICIARIES: Capital: Employee Beneficiaries and Denel SOC Limited

Income: Denel SOC Limited

AUDITORS: PricewaterhouseCoopers Inc.
Postal address: Physical address:
Private Bag X36 4 Lisbon Lane, Waterfall City
Sunninghill Jukskei View
2157 2090
South Africa South Africa

REGISTERED OFFICE OF THE TRUST:
Postal address: Physical address:
P O Box 8322 Denel SOC Limited
Centurion Denel Corporate Office
0046 Nelmaphius Ave
South Africa Irene
1675
South Africa

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Trustees' responsibility for the annual financial statements	2 - 3
Independent Auditor's report	4 - 6
Statement of financial position	7
Statement of comprehensive income	8
Statement of changes in capital	9
Cash flow statement	10
Notes to the financial statements	11 - 16

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**DENEL MEDICAL BENEFIT TRUST
(TRUST NO: IT8466/02)**

TRUSTEES' RESPONSIBILITY FOR THE FINANCIAL STATEMENTS

The Trustees are required to maintain adequate accounting records and are responsible for the content and integrity of the financial statements and related financial information included in this report. It is their responsibility to ensure that the financial statements fairly present the state of affairs of the Trust as at the end of the financial year and the results of its operations and cash flows for the period then ended, in conformity with the accounting policies of the Trust disclosed in note 1 to the financial statements. The external auditors are engaged to express an Independent opinion on the financial statements.

The annual financial statements are prepared in accordance with the accounting policies of the Trust, disclosed in note 1 to the financial statements, and are based upon appropriate accounting policies consistently applied and supported by reasonable and prudent judgements and estimates.

The Trustees acknowledge that they are ultimately responsible for the system of internal financial control established by the Trust and places considerable importance on maintaining a strong control environment. To enable the Trustees to meet these responsibilities, the Trustees set standards for internal control aimed at reducing the risk and error in a cost effective manner. The standards include the proper delegation of responsibilities within a clearly defined framework, effective accounting procedures and adequate segregation of duties to ensure an acceptable level of risk. These controls are monitored by the Trustees and all stakeholders are required to maintain the highest ethical standards in ensuring the Trust's business is conducted in a manner that in all reasonable circumstances is above reproach. The focus of risk management in the Trust is on identifying, assessing, managing and monitoring all known forms of risks across the Trust. While operating risk cannot be fully eliminated, the Trustees endeavour to minimise it by ensuring that appropriate infrastructure, controls, systems and ethical behaviour are applied and managed within the predetermined procedures and constraints.

The Trustees are of the opinion, based on the information and explanations given by the administrator that the internal control provide reasonable assurance that the financial records may be relied on for the preparation of the annual financial statements. However, any system of Internal financial control can provide only reasonable, and not absolute, assurance against material misstatement or loss.

The Trustees have reviewed the Trust's cash flow for the year to 29 February 2020 and, in light of this review and the current financial position, they are satisfied that the Trust had or has access to adequate resources to continue in operational existence for the foreseeable future.


The external auditors are responsible for independently reviewing and reporting on the Trust's financial statements. The financial statements have been examined by the Trust's external auditors and the report are presented on pages 4 to 6.

DENEL MEDICAL BENEFIT TRUST
(TRUST NO: IT8466/02)

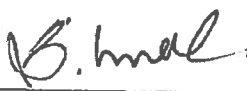
TRUSTEES' RESPONSIBILITY FOR THE FINANCIAL STATEMENTS

The external auditors were given unrestricted access to all financial records and related data. The Trustees believe all representations made to the external auditors during their audit are valid and appropriate.

The annual financial statements as set out on pages 7 to 16, which have been prepared on the going concern basis, were approved by the Trustees on 17/11/2020 and were signed on its behalf by:



TRUSTEE
Date: 17/11/2020



TRUSTEE
Date: 17-11-2020


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Independent auditor's report

To the Trustees of Denel Medical Benefit Trust

Our opinion

In our opinion, the financial statements of Denel Medical Benefit Trust (the Trust) for the year ended 29 February 2020 are prepared, in all material respects, in accordance with the basis of accounting described in note 1 to the financial statements.

What we have audited

Denel Medical Benefit Trust's financial statements set out on pages 7 to 16 comprise:

- the statement of financial position as at 29 February 2020;
- the statement of comprehensive income for the year then ended;
- the statement of changes in capital for the year then ended;
- the statement of cash flows for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies.

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

Independence

We are independent of the Trust in accordance with the sections 290 and 291 of the Independent Regulatory Board for Auditors' *Code of Professional Conduct for Registered Auditors (Revised January 2018)*, parts 1 and 3 of the Independent Regulatory Board for Auditors' *Code of Professional Conduct for Registered Auditors (Revised November 2018)* (together the IRBA Codes) and other independence requirements applicable to performing audits of financial statements in South Africa. We have fulfilled our other ethical responsibilities, as applicable, in accordance with the IRBA Codes and in accordance with other ethical requirements applicable to performing audits in South Africa. The IRBA Codes are consistent with the corresponding sections of the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* and the International Ethics Standards Board for Accountants' *International Code of Ethics for Professional Accountants (including International Independence Standards)* respectively.

Emphasis of Matter – Basis of Accounting

We draw attention to note 1 to the financial statements, which describes the basis of accounting. The financial statements are prepared in accordance with the trust's own accounting policies to satisfy the financial information needs of the trust's trustees. As a result, the financial statements may not be suitable for another purpose. Our opinion is not modified in respect of this matter.

PricewaterhouseCoopers Inc., 4 Lisbon Lane, Waterfall City, Jukskei View, 2090
Private Bag X36, Sunninghill, 2157, South Africa
T: +27 (0) 11 797 4000, F: +27 (0) 11 209 5800, www.pwc.co.za

Chief Executive Officer: L S Machaba
The Company's principal place of business is at 4 Lisbon Lane, Waterfall City, Jukskei View, where a list of directors' names is available for inspection.
Reg. no. 1998/012055/21, VAT reg.no. 4950174682

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Other information

The trustees are responsible for the other information. The other information comprises the information included in the document titled “Denel Medical Benefit Trust Annual Financial Statements for the year ended 29 February 2020”. The 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 trustees are responsible for the preparation of these financial statements in accordance with the basis of accounting described in note 1 to the financial statements and for determining that the basis of preparation is acceptable in the circumstances and for such internal control as the 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 trustees are responsible for assessing the Trust’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 trustees either intend to liquidate the Trust 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 Trust’s internal control.



- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the trustees.
- Conclude on the appropriateness of the 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 Trust'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 Trust to cease to continue as a going concern.

We communicate with the 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.

PricewaterhouseCoopers Inc.

Director: JJ Grové

Registered Auditor

Johannesburg

18 November 2020

DENEL MEDICAL BENEFIT TRUST
(TRUST NO: IT8466/02)

STATEMENT OF FINANCIAL POSITION AS AT 29 FEBRUARY 2020

	Notes	2020 R	2019 R
ASSETS			
Non-current assets		1,424,970,397	1,394,784,889
Investments	4	1,424,970,397	1,394,784,889
Current assets		1,389,160	4,130,397
Accounts receivable	5	32,326	25,483
Cash and cash equivalents	6	1,356,834	4,104,914
Total assets		1,426,359,557	1,398,915,286
CAPITAL AND LIABILITIES			
Capital	7	1,425,964,639	1,396,393,182
		1,425,964,639	1,396,393,182
Current liabilities		394,918	2,522,104
Accounts payable	8	394,918	2,522,104
Total equity and liabilities		1,426,359,557	1,398,915,286

DENEL MEDICAL BENEFIT TRUST
(TRUST NO: IT8466/02)

STATEMENT OF COMPREHENSIVE INCOME FOR THE YEAR ENDED 29 FEBRUARY 2020

	Notes	2020 R	2019 R
INCOME			
Investment income	10	<u>64,356,446</u>	<u>48,229,950</u>
		64,356,446	48,229,950
EXPENSES			
Operating expenses	9	<u>(6,109,997)</u>	<u>(5,965,735)</u>
Surplus before taxation		58,246,449	42,264,215
Taxation	12	-	-
Surplus after taxation		<u><u>58,246,449</u></u>	<u><u>42,264,215</u></u>

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**DENEL MEDICAL BENEFIT TRUST
(TRUST NO: IT8466/02)**

STATEMENT OF CHANGES IN CAPITAL FOR THE YEAR ENDED 29 FEBRUARY 2020

	Notes	Capital account R
Closing balance as at 28 February 2018		1,379,808,980
Surplus after taxation		42,264,216
Monthly medical premium subsidies		(25,680,014)
Closing balance at 28 February 2019		1,396,393,182
Surplus after taxation		58,246,449
Partial refund of final distribution received from Denel Post Retirement Trust	2	(1,111,500)
Employer contributions		468,708
Monthly medical premium subsidies		(28,032,200)
Closing balance at 29 February 2020		1,425,964,639

DENEL MEDICAL BENEFIT TRUST
(TRUST NO: IT8466/02)

CASH FLOW STATEMENT FOR THE YEAR ENDED 29 FEBRUARY 2020

	Notes	2020 R	2019 R
Cash flows from operating activities			
Cash paid to settle members' subsidy		(28,032,200)	(25,415,151)
Cash paid to service providers		(4,027,381)	(1,441,877)
Net cash flow utilised in operating activities		(32,059,581)	(26,857,028)
Cash received from investment activities			
Cash received from investment activities		29,311,501	14,788,811
Net cash received utilised in investing activities		29,311,501	14,788,811
Net decrease in cash equivalents		(2,748,080)	(12,068,218)
Cash equivalents at the beginning of year		4,104,914	16,173,132
Cash and cash equivalents at end of year		1,356,834	4,104,914

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**DENEL MEDICAL BENEFIT TRUST
(TRUST NO: IT8466/02)**

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 29 FEBRUARY 2020

1 ACCOUNTING POLICIES

The annual financial statements are prepared on the going concern basis and in accordance with the accounting policies set out below. The financial statements are prepared under the historical cost basis, except for investment in insurance policies which is stated at fair value as confirmed by the insurer. The basis of accounting and the presentation and disclosures contained in the financial statements are not intended to, and do not necessarily, comply with the requirements of International Financial Reporting Standards. The following are the principal accounting policies adopted by the Board of Trustees of the Trust and a basis consistent with the previous year.

1.1 Investment Income

The following classes of investment income are disclosed:

Annuity Income

Annuity income is received from an external insurer, namely Momentum Metropolitan Holding Group Limited, and is recognised as and when received.

Interest

Interest income is recognised on a time proportion basis.

Adjustment to fair value

Gains and losses arising from changes in fair value of 'Investments' are presented in the Statement of Comprehensive Income in the period in which they arise.

1.2 Financial Instruments

A financial instrument is any contract that gives rise to both a financial asset of one entity and a financial liability or equity instrument of any other entity. Purchases and sales of financial instruments are recognised on trade date - the date on which the Board of Trustees of the Trust commits to purchase or sell the instruments. Financial assets are derecognised when the right to receive cash flows from the investment has expired, or on trade when they have been transferred and the Trust has also transferred substantially all risks and rewards of ownership.

Upon initial recognition financial instruments are designated at fair value through the Statement of Comprehensive Income as they are managed and their performance is evaluated on a fair value basis and this results in more relevant information as it eliminates or significantly reduces an accounting mismatch that would arise from measuring assets or liabilities or recognising the gains and losses on them on different bases.

Financial instruments carried at fair value through profit and loss are initially recognised at fair value, and transaction costs are expenses in the Statement of Comprehensive Income.

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**DENEL MEDICAL BENEFIT TRUST
(TRUST NO: IT8466/02)**

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 29 FEBRUARY 2020

1.2 Financial instruments (continued)

Gains or losses from changes in the fair value are presented in the Statement of Comprehensive Income in the period in which they arise.

Subsequent to initial recognition, the Instrument is measured as set out below:

Insurance policies

Insurance investment policies with insurers are valued based on the policyholder's retrospective contribution to assets (i.e. accumulation at the investment return achieved on gross premiums) as confirmed by the insurer. Insurance investments policies are classified as non-current assets.

1.3 Expenses incurred in managing investments

Expenses in respect of the management of investments are recognised in the Statement of Comprehensive Income as the service is rendered and is classified as operating expenses.

1.4 Operating expenses

Operating expenses are recognised in the Statement of Comprehensive Income in the reporting period to which they relate. An expense is recognised if it is probable that any future economic benefits associated with the item will flow from the Trust and the cost can be reliably measured. In the event that an expense has not yet been paid at the end of the reporting period, the liability will be reflected in the accounts payable note. If an expense has been paid in advance or has been overpaid, the asset will be disclosed in the accounts receivable note.

1.5 Medical premium subsidies

Medical premium subsidies in respect of pensioner beneficiaries' monthly medical aid contributions are measured in terms of the Trust Deed. Medical premium subsidies are recognized as an expense when they are due and payable in terms of the Trust Deed of the Trust. Any medical premium subsidies not paid at the end of the reporting period are recognised as a current liability and are classified as medical premium subsidies payable under accounts payable.

1.6 Capital distributions to the principal employer

Capital distributions to the principal employer are measured in terms of the Trust Deed. Distributions are recognised as and when paid in terms of the Trust Deed, upon discretion of the Trustees.

1.7 Accounts receivable

Accounts receivable are recognised at fair value and are subsequently measured at amortised cost using the effective interest rate method, less impairment losses. Receivables with a short duration are not discounted, as the effects of discounting are immaterial.

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**DENEL MEDICAL BENEFIT TRUST
(TRUST NO: IT8466/02)**

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 29 FEBRUARY 2020

1.8 Accounts payable

Accounts payable are recognised at fair value and are subsequently measured at amortised cost using the effective interest rate method. Payables with a short duration are not discounted, as the effects of discounting are immaterial.

1.9 Taxation

No provision for taxation has been made as the Trustees have vested all income accrued for the year in the income beneficiary.

1.10 Cash and cash equivalents

Cash and cash equivalents comprise cash balance and call deposits. Cash and cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in fair value. Cash and cash equivalents are initially measured at fair value and subsequently at amortised cost using the effective interest method.

1.11 Employer contributions

Employer contributions comprise contributions received from the principal employer in order to fund the shortfall calculated by the Trust's actuary with regard to beneficiaries' early retirement. Employer contributions are recognised within the capital account when it accrues to the Trust.

1.12 Future liabilities: Post-retirement medical payments

The Trust provides monthly medical premium subsidies to current pensioners who were previously employed by the Denel Group of companies. The Trust's financial statements do not make provision for the estimated benefits of this future liability. As a result, no provision is made in the annual financial statements of the future liability in respect of medical premium subsidies.

2 PARTIAL REFUND OF FINAL DISTRIBUTION RECEIVED FROM DENEL POST RETIREMENT TRUST

The Denel Medical Benefit Trust received interest on unused capital on the closure of the Denel Post Retirement Trust after all offers were made and paid to the beneficiaries that accepted the buy out offer from Denel SOC Ltd. The Denel Post Retirement Trust overlooked an obligation to SARS when it transferred the funds to the Denel Medical Benefit Trust, via Denel SOC Ltd. The partial refund of the final distribution was made to Denel SOC Ltd to settle the obligation with SARS. Although this is in contravention of section 7.3 of the trust deed ("Capital may only be distributed to Denel by the Trustees in order to enable Denel to create a fund, trust or entity with the objectives substantially similar to the objectives of this Trust stipulated in clause 5."), and based on legal advice, this was done in order to avoid any further interest levied by SARS that would have been to the detriment of the beneficiaries of the Denel Medical Benefit Trust.

	2020	2019
	R	R
Partial refund of final distribution received from Denel Post Retirement Trust due to tax payable on interest received on unused capital	1,111,500	-
	<u>1,111,500</u>	<u>-</u>

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DENEL MEDICAL BENEFIT TRUST
(TRUST NO: IT8466/02)

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 29 FEBRUARY 2020

3 SUBSEQUENT EVENTS

Subsequent to the reporting date, the President of South Africa declared a national state of disaster as a result of the global COVID-19 virus pandemic. Even though South Africa is in the early stages of the COVID-19 virus outbreak, there are uncertainties about the potential impact of COVID-19 virus on the Trust and its beneficiaries. COVID-19 virus has had a severe impact on the financial markets and the Trust's investments have been negatively affected. The Trustees have however assessed that notwithstanding the impact of COVID-19 virus, the Denel Medical Benefit Trust is still a going concern.

	2020 R	2019 R
4 INVESTMENTS		
Momentum Linked Annuity Policy	1,424,970,397	1,394,784,889
	<u>1,424,970,397</u>	<u>1,394,784,889</u>
5 SUNDRY DEBTORS		
Interest receivable	5,843	-
Prepaid insurance premium	26,483	25,483
	<u>32,326</u>	<u>25,483</u>
6 CASH AND CASH EQUIVALENTS		
Current account	1,356,834	4,104,914
	<u>1,356,834</u>	<u>4,104,914</u>
7 CAPITAL		
Income vested to the Income Beneficiary and not utilised	-	2,822,038
Capital of the Trust	1,425,964,639	1,393,571,144
	<u>1,425,964,639</u>	<u>1,396,393,182</u>
8 ACCOUNTS PAYABLE		
Administration fees	173,075	-
Principal Officer fees	24,825	-
Consulting fees	57,063	48,417
Medical premium subsidies	-	2,356,789
Audit fee	139,955	116,898
	<u>394,918</u>	<u>2,522,104</u>

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**DENEL MEDICAL BENEFIT TRUST
(TRUST NO: IT8466/02)**

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 29 FEBRUARY 2020

	2020	2019
	R	R
9 OPERATING EXPENSES		
Audit fees	139,955	116,898
Bank charges	10,217	3,447
Administration fees	262,918	268,259
Principal Officer remuneration	298,319	285,850
Consultancy fees	581,015	640,075
Fidelity insurance	30,780	31,297
Postage	971	1,952
Trustee expense	-	1,088
Other fees paid	-	14,503
Legal fees	6,400	-
Investment Management fees	4,779,422	4,602,366
	<u>6,109,997</u>	<u>5,965,735</u>
10 INVESTMENT INCOME		
Annuity income	2,568,626	14,350,000
Interest income	80,014	438,811
Fair Value adjustment	61,707,806	33,441,139
	<u>64,356,446</u>	<u>48,229,950</u>
11 MONTHLY MEDICAL PREMIUM SUBSIDIES		
Monthly medical premium subsidies	28,032,200	25,680,014
	<u>28,032,200</u>	<u>25,680,014</u>
12 TAXATION		

No provision for taxation has been made as the Board of Trustees have vested all the income accrued for the year in the Income Beneficiary.

**DENEL MEDICAL BENEFIT TRUST
(TRUST NO: IT8466/02)**

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 29 FEBRUARY 2020

13 RELATED PARTY TRANSACTIONS:

The following transactions between the Principal Employer, Trustees, Principal Officer, Beneficiaries and the Trust occurred:

- During the period under review, the Principal Officer was paid R298,319 (2019: R285,850) for his services rendered to the Trust (refer to note 9 of the financial statements). The balance of R24,825 (2019: Rnil) payable as at 29 February 2020 (refer to note 8 of the financial statements).
- Trustee expenses to the value of Rnil (2019: R1,088) were paid during the period under review (refer to note 9 of the financial statements).
- A payment of R1,111,500 (2019: Rnil) was paid to Denel SOC Ltd during the period under review (refer to note 2 of the financial statements).
- Monthly medical premium subsidies of R28,032,200 (2019: R25,680,014) were paid on behalf of the beneficiaries of the Trust. The balance of Rnil (2019: R2,356,789) is payable as at 29 February 2020 (refer to note 8 of the financial statements).
- Employer contributions of R468,708 (2019:Rnil) were received from the principal Employer during the period under review in respect of early retirements before age 60 years.

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IN THE HIGH COURT OF SOUTH AFRICA
(GAUTENG DIVISION, PRETORIA)

CASE NO: _____

In the *ex parte* application of:

DENEL SOC LIMITED

Applicant

In re:

VARIATION OF THE TRUST DEED OF THE DENEL MEDICAL BENEFIT TRUST

EXPERT AFFIDAVIT


I, the undersigned,

ANTONY LESTER

do hereby make oath and state under oath as follows:

1. I am an adult male, practising as an investment consultant. I am currently the Managing Director of Towers Watson (Proprietary) Limited ("**Towers Watson**") which is a subsidiary of Willis Towers Watson. I reside at 14 Peter Cloete Avenue, Constantia, Cape Town, 7806.
2. The facts contained in this affidavit are within my personal knowledge, save where the context indicates otherwise, and are both true and correct.

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3. I refer to the founding affidavit deposited to by Khohlong William Hlakoane on behalf of the Applicant.
4. I depose to this affidavit:
 - 4.1. to elaborate on my expertise in relation to the subject matter of the two reports attached as FA9 and FA10 to the founding affidavit; and
 - 4.2. to confirm that I have read the founding affidavit and to confirm what is said in paragraph 98, paragraph 99, paragraph 118 and paragraph 128 of the founding affidavit insofar as they relate to me.
5. The two reports address the following:
 - 5.1. The first report analyses the financial history of the Denel Medical Benefit Trust in order to explain the reasons for the Trust having such substantial excess assets;
 - 5.2. The second report analyses the transactions that Denel proposes be implemented pursuant to the proposed variation of the Trust Deed of the Denel Medical Benefit Trust. The second report addresses whether:
 - 5.2.1. the offer that Denel will make to beneficiaries of the Denel Medical Benefit Trust (the "Individual Annuity Policy Offer" referred to in the founding affidavit) is a fair one; and
 - 5.2.2. there will be sufficient assets to meet the reasonable benefit expectations of the beneficiaries who do not accept Denel's offer once Denel has received the proposed distribution of the excess

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assets of the Denel Medical Benefit Trust pursuant to the proposed variation to the trust deed.

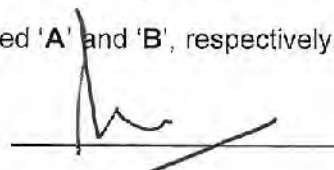
6. My employment and professional history is as follows:
 - 6.1. I currently hold a B.Sc degree in actuarial science from the University of Cape Town which I obtained in 1981.
 - 6.2. I joined Old Mutual in July 1985, first working in their life office valuation department. I worked in this role until sometime in mid-1989.
 - 6.3. I qualified as an actuary with the UK based Institute of Actuaries in 1989 and then moved to the pension valuation department of Old Mutual in mid- 1989, where in time I became the valuator to a large number of defined benefit arrangements.
 - 6.4. In 1994, I was appointed as the Managing Director of Old Mutual Actuaries and Consultants, which was set-up to provide consulting advice to their pension fund and medical scheme clients.
 - 6.5. In March 1998, I resigned from Old Mutual to set-up a firm called Fifth Quadrant Actuaries & Consultants ("**Fifth Quadrant**"). I was a founding shareholder and the Managing Director of the firm.
 - 6.6. In 2009, Fifth Quadrant sold 10% of its equity to Watson Wyatt, who later became Towers Watson. In 2011 Towers Watson had acquired a 50% +1 interest in Fifth Quadrant and then operated under the name of Towers Watson which subsequently became Willis Towers Watson.

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- 6.7. I continued to lead the South Africa business over most of this period and today I am still the Managing Director of the firm, which operates under the name of Towers Watson (Proprietary) Limited.
- 6.8. Since 1998 I have continued to provide clients with advice mainly around retirement funds. My expertise is in strategy work and investment consulting to our largest clients. I have provided consulting advice to many of the largest retirement funds in South Africa, particularly in relation to their investment strategies.
7. My professional experience includes:
- 7.1. I was the valuator to a large number of defined benefit retirement funds including some very large funds, having first started doing such valuations in 1989. However, since about 2008, I stopped being a valuator to retirement funds.
- 7.2. My main focus since 1998 has been in providing investment consulting advice to many of the largest local retirement funds. I continue to provide strategic employee benefit advice to clients periodically.
8. I gave up practicing as an actuary more than 12 years ago and I am no longer a member of any actuarial society. I did so because a much smaller proportion of my work required me to be an actuary. My focus had turned from the liability side of the balance sheet, to the asset side, because my belief is that the asset side is far more complex being related to investment markets and much of the liability side flows from investment returns (e.g. inflation which in turn affects salary increases, medical aid inflation and even resignation / retrenchment rates).

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- 9. I respectfully submit that considering my education, qualification and experience, I am qualified to furnish the two reports relied on by the Applicant and to do so as an expert.
- 10. As stated above, I have read the Applicant's founding affidavit and I confirm that what is said in relation to me in paragraph 98, paragraph 99, paragraph 118 and paragraph 128 of the founding affidavit is correct.
- 11. In addition, I also attach to this affidavit, copies of my final signed reports referred to at paragraphs 98 and 118 of the Founding Affidavit marked 'A' and 'B', respectively.



ANTONY LESTER

I certify that the deponent acknowledged that s/he knows and understands the contents of this affidavit, which was signed and sworn to before me at Wynberg on this the 25th day of **MAY 2021**, in accordance with Regulation No. R1258 dated 21 July 1972 as amended by Government Report R1648 dated 19 August 1977, as further amended by Government Report R1428 dated 11 July 1980, and by Government Report R774 of 23 April 1982.



COMMISSIONER OF OATHS

Designation and Area: Wynberg

Full Names: Z. Nkomo

Street Address: Church Street



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Analysis of the financial history of the Denel Medical Benefit Trust

Preamble

We have been requested by Denel SOC to provide an analysis of the financial history of the Denel Medical Benefit Trust ("DMBT") covering the period 1 August 2000 to 1 April 2021. To this end we were provided with the following information:

- Annual Financial Statements ("AFS") for the years 2007 to 2021; the 2007 AFS include the 2006 results.
- Actuarial valuation reports as at 1 August 2000 and then from 2003 to 2006 and finally from 2010 to 2021; again the 2003 report shows the 2002 results and the 2010 report shows the 2009 figures.

The information is not complete, but it is sufficient to enable a reasonable analysis of the financial history of the DMBT.

Nature of the arrangement

The DMBT was established to fund the Company's full post-retirement medical obligation ("PRMA") in respect of its in-service members when they retire and continuation (or pensioner) members. Thus, the intention at the outset was that the DMBT had sufficient assets so that Denel SOC would not be required to make any further contributions. Nevertheless, the Trust Deed does provide for Denel SOC (or any other party) to make additional donations (contributions) to the Trust.

At the time the Trust was established the correct amount of assets it required to meet the PRMA obligation was unknown and can only be determined once the last beneficiary had been paid. Consequently, the quantum could only be estimated by an actuary making assumptions about future investment returns, medical aid inflation, resignation rates, when members may retire, mortality rates for in service members and pensioner longevity, what medical aid option the member may chose at retirement and the number of dependents a member may have when he or she retires.

In most instances the most important driver of the true cost is the actual versus budgeted experience of investment returns and medical aid inflation. This is so because the Trust's assets grow with investment returns and the liabilities increase with medical aid inflation. An important insight is that what matters is how investment returns and medical aid increases evolve relative to each other, rather than the absolute level of return and increases. For example, if the valuation basis assumes investment returns to be 8% p.a. and medical aid inflation to be 6% p.a. (i.e. a 2% p.a. gap), but the actual experience is that investment returns are 12% p.a. and medical aid increases are 10% p.a. (i.e. the same 2% p.a. gap) very little surplus or deficit will emerge from these two factors (i.e. both are equally higher than budget).

South African actuaries commonly assess the financial position of a plan such as the DMBT using deterministic assumptions. This is a single set of assumptions which is intended to represent the best estimate of the future experience of the Trust. Best estimate is taken to mean that there is a 50% chance of the actual outcome being better or worse than that budgeted for.¹

Naturally, the Trust's actual experience will differ from the assumptions and one could expect most of the subsequent outcomes to fall within the range of normal error. There will also be rarer outcomes that fall within the range of plausibility and finally some very rare outcomes that fall into the outer reaches.

¹ At some time in the 2000's the Accounting Standards prescribed the valuation basis for the determining the financial position of the Trust for inclusion in the AFS of DENEL SOC. However, the actuaries also continued to report the financial position based on consistent long term assumptions until 2015.

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Obviously, outcomes that fall into the outer reaches category arise from rare experiences compared to long term averages but may also be attributable to good or bad luck. The critical point is that the observed financial outcome is often highly path dependent, meaning that the timing of when events happen can have a material impact. The consequence of path dependency is also described as "sequencing risk", noting that the timing of events tends to be more random, causing the lucky or unlucky outcomes to arise as described above.

There is one other important factor that may influence the observed financial position of the Trust at a point in time, namely the valuation assumptions that the actuary makes. The actuary can change the financial position at the stroke of a pen by simply changing the assumptions he or she makes. The easiest way to understand this is that the actuary's assumptions simply represent a budget of what the expected future experience of the Trust may be. If the actuary sets the budget at a more optimistic level, then the financial position of the Fund improves and vice versa. Thus, in providing an analysis of the financial history of the Trust one needs to isolate the effect of any valuation basis change on the observed outcome.

Financial history of the Trust

Surplus we analyse

The first actuarial valuation of the Trust was done as at 1 August 2000. The results were presented on two bases, namely that investment returns would exceed medical inflation by 1% p.a., alternatively that investment returns would exceed medical inflation by 2% p.a. The calculation based on the 2% p.a. gap revealed a surplus of R22 million. The reason why two bases were shown is that in 2000 there was the possibility that the Trust would need to pay tax on its investment return and the tax was expected to reduce the investment return by 1% p.a.

In the subsequent years up until 1 April 2015, the Trust's financial position was shown assuming investment returns would exceed medical aid inflation by 2% p.a. (the so-called funding valuation basis) and separate results were shown for accounting purposes. From 2016 onwards the valuation of the Trust was only shown on the accounting basis where the investment return and medical aid assumptions were varied to comply with the prescripts of the Accounting Standard IAS19. The 1 April 2021 valuation assumes investment returns to be 2.23% p.a. higher than medical aid inflation which means that a relatively small part of the surplus shown in this valuation arises from a basis change.

There is one other intermediate valuation point, namely 1 April 2005, where the calculated surplus, based on the 2% p.a. investment return / medical aid inflation gap, was R19.2 million (i.e. very close to the R22 million shown at the outset). This allows one to consider the build-up from a point where we have AFS and the reasons for the change in the surplus from 1 August 2000 to 1 April 2005 cancel out and don't need to be analysed.

The table below sets out the financial position of the Trust as at 1 August 2000, 1 April 2005, 1 April 2015 (all three valuations based on the 2% p.a. gap) and 1 April 2021 (2.23% p.a. gap).

	1 August 2000	1 April 2005	1 April 2015	1 April 2021
Liabilities	650.0	1 126.3	460.1	375.0
Assets	872.0	1 145.5	1 314.1	1 645.1
Surplus	22.0	19.2	854.0	1 270.1

We point out that the Trust earned a cumulative return of some 48% from 1 April 2015 to 1 April 2021. If the R854 million surplus that existed as at 1 April 2015 is increased by this 48% return, it amounts to R1 263.9 million, which is very close to the surplus reported on 1 April 2021 (R1 270.1 million) albeit that the latter surplus has been calculated on a slightly weaker valuation basis than the 2015 surplus (i.e. 2.23% p.a. return / increase gap versus 2% p.a.).

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Accordingly, we can reasonably conclude almost all the surplus that arose between 2015 and 2021 is mainly investment return on the 2015 surplus, with all the other factors more or less cancelling out. This allows us to narrow the focus on the reasons why the surplus increased from R19.2 million on 1 April 2005 to R854 million on 1 April 2015 knowing that the most important element of the actuarial assumptions, that being the investment return / medical aid inflation gap, was kept constant at 2% p.a.

Before we proceed with an analysis of the surplus it is worth explaining the main reason why the Trust's liabilities decreased from R1 126.3 million on 1 April 2005 to R460.1 million on 1 April 2015. Starting in November 2009 and each subsequent year, Denel SOC made a buy-out offer to members of the Trust. As per the Trust's AFS the first settlement of this liability occurred in the 2011 financial year, when a total amount of R970.5 million was paid to in-service and continuation members that took this buy-out option. As indicated above there were further settlements of the liability in each year from 2012 to 2015.

Investment return on the surplus as the 1 April 2005

The Trust would earn investment return at a rate of 13.2% p.a. (see below) on the R19.2 million surplus that existed as at 1 April 2005. This amount would have accumulated to an estimated R66.5 million as at 1 April 2015.

Investment returns versus medical aid inflation (1 April 2005 to 1 April 2015)

For each year, the actuary budgeted for medical aid inflation to be 2% p.a. higher than general inflation and for investment returns to exceed medical aid inflation by 2% p.a. This means that the actuary was budgeting for the assets to earn a real return of 4% p.a.

We were able to estimate the investment return earned over the 10 period using the AFS. The calculation is complicated by large outflows from 2011 onwards as the liability of members that elected the buy-out option was settled. Nevertheless, we are comfortable that our estimated returns are in the right ballpark. The valuation reports contained information on the increase in the medical aid contribution rate. We are missing that data for 2007 through to 2009, but again we could make a reasonable estimate with reference to the general increase in medical aid contributions over this period.

The table below shows the estimated investment returns and medical aid inflation compared to general inflation over the 10-year period.

	Investment returns	Medical aid inflation
Estimated	13.2%	10.0%
- General inflation	6.0%	6.0%
=Difference	7.2%	4.0%
Actuary's budget	4.0%	2.0%
Surplus / strain	3.2%	-2.0%

Thus, the surplus arising from the actual investment return being an estimated 3.2% p.a. more than budgeted for is partially offset by medical aid inflation being 2% p.a. higher than that allowed. We estimate that the net effect of this experience contributed some R607 million of the R854 million shown as at 1 April 2015.

There is an element of luck in the quantum of this surplus because in the 2006 financial year the assets earned a return of some 26% whereas medical inflation for that financial year was just below 5% (i.e. the gap was 21% versus the budgeted 2%). In subsequent years many members exited the fund via the buy-out option, but also via resignation. This extinguishes the liability so, if future medical aid is much higher than budgeted for, the deficit emerging is less because the liability on which it can arise is much lower.

Impact of resignations

Another relevant actuarial assumption is the rate of resignation the Actuary budgets for. This is important because any member of the Trust that resigns from Denel will not receive any PRMA benefit. The 2005 valuation report sets out the withdrawal assumptions shown in the table below – the same assumptions were used in the 1 April 2010 valuation. Subsequently, the withdrawal assumptions were changed, but the effect hereof was limited because by then many members had left the Trust via the buy-out option.

Age	Annual rate of withdrawal
20-29	20%
30-34	15%
35-44	10%
45+	0%

We are not surprised by these assumptions; actuaries have a bias to be conservative. The effect of the assumptions is that from 2005 to 2010, the actuary was budgeting for no resignations from age 45 onwards; to the extent that any member of the Trust aged 45 and older resigned, a surplus would arise. In addition, if the resignation rates at the younger ages were higher than that budgeted for, this too would be a source of surplus.

It is clear that surplus arose from the actual resignation rate being higher than that assumed since the 2005 and 2006 valuation and some of the post-2010 valuation reports refer to there being a withdrawal profit. Using this information, we roughly estimate that some R140 million of the surplus as at 1 April 2015 is attributable to this source.

Consolidated position

The table below sets out our estimated consolidated analysis of the surplus over 1 April 2005 to 1 April 2015.

Item	R'm
Surplus 1 April 2005	19.2
Investment return on this surplus	47.3
Investment returns higher than budgeted, partially offset by medical aid inflation being higher than budgeted	607.0
Resignation and exit profits	140.0
Unexplained	40.5
Surplus as at 1 April 2015	854.0

The unexplained item represents 4.75% of the surplus as at 1 April 2015.

Summary and conclusion

The DMBT was funded in 2000 on the basis that the Trust would have sufficient assets to meet the past and future PRMA obligation of Denel SOC. Obviously, the actual liability could only be known once the last member had received their benefit. Accordingly, the Fund's actuary had to make assumptions about the future experience of the Trust, the most important of which was investment returns and medical aid inflation. Arguably the second most important assumption was the withdrawal rate because the company's liability would be extinguished for members that resigned.

The actual experience was always going to be different from the actuary's assumptions. We were provided with reasonable information to analyse the Trust's experience between 1 April 2005 and 1 April 2015. Over this period the surplus grew from R19.2 million to R853 million. If we accumulate this surplus with investment returns to 1 April 2021, we get an expected surplus of R1 263.9 million which is close to the reported surplus of R1 270.1 million at this date.

In our opinion the observed outcome of a surplus of R1 270.1 million as at 1 April 2021 falls beyond the range of normal error and is a rarer event which falls into the category of plausible outcomes. Our analysis suggests that there are three main reasons for this very positive outcome:

- As explained above, the surplus arises almost entirely over the ten years spanning 1 April 2005 to 31 March 2015. Over this period the Trust's assets earned an estimated return of 13.2% p.a. with inflation averaging 6.0% p.a. over the same time. The observed volatility (as measured by standard deviation) of this return was 8.1% p.a.

Under normal market conditions one would expect to earn a real return of some 4% p.a. for a portfolio that has a risk budget of 8% p.a. This 4% p.a. real return is also consistent with the actuarial assumption of future investment returns. The estimated actual real return of 7.2% p.a. (13.2% - 6.0%) is well above what we would expect. We estimate that for a portfolio with an 8% p.a. risk a real return of 7.2% p.a. or higher over 10 years will only be observed about 15% of the time.

- As explained previously the investment return surplus was boosted by the path of the membership numbers. In particular, in the 2006 financial year the assets earned a return of some 26% whereas medical inflation for that financial year was just below 5% (i.e. the gap was 21% versus the budgeted 2%). In subsequent years many members exited the fund via the buy-out option, but also via resignation. The liability was extinguished for these exits, so to the extent that future medical aid was much higher than budgeted for (which it was), the deficit emerging from this factor was less because the liability on which it could arise was much lower.
- The observed resignation rate was higher than actuary budgeted for

Finally, in our opinion, there is an element of good fortune which is always difficult to anticipate in the observed outcome as there usually is when the results fall into the rarer category of beyond normal error and in the range of plausible outcomes.

This report was prepared by Antony Lester.



Antony Lester

Date: 21 May 2021



Assessment of the proposed transaction in respect of the Denel Medical Benefit Trust

Introduction

I have acted as the advisor to the Denel Retired Employees Medical Scheme ("DREMS") Forum in negotiating the proposed buy-out transaction of Denel SOC's post-retirement medical aid ("PRMA"). I highlight that the parties agreed that my fees for advising the DREMS would be paid by Denel.

My initial understanding was that all members of the Denel Medical Benefit Trust ("DMBT") would need to accept the offer if it were to be implemented. However, Denel SOC has now amended the approach and members of the DMBT will have the choice to accept the offer or remain members of the DMBT with their existing PRMA benefits unchanged.

As part of the transaction, Denel SOC will be approaching the High Court seeking an amendment to the Trust Deed which will provide that the excess assets of the Trust may be paid out to the Company. Consequently, the two aspects I need to deal with in this report are:

- Is the proposed buy-out offer fair to members of the DMBT? and
- Will sufficient assets be left in the DMBT so that the reasonable benefit expectations of the members that elect to remain in the Trust will be met

The offer

The buy-out offer to members is as follows:

1. The benefit that will be secured for members is the current PRMA subsidy as at date the transaction becomes effective but assuming that all members are on the Discovery Health Essential Comprehensive Plan. This means an increase in the benefit for members that have elected a lower cost medical option than the Essential Comprehensive Plan.
2. The amount in 1 above will then be increased by 20%
3. The total benefit (i.e. including the 20% enhancement) will then be secured via a life annuity policy issued by an Insurer where the terms guarantee a lifelong pension to the member and his or her dependents increasing on each 1 January by 100% of the annual inflation rate to the preceding 30 September plus 4% p.a.

It is always easier to explain by way of example; let us assume that a member has chosen a lower cost option than the Essential Comprehensive Plan and his or her current PRMA subsidy is R5 000 per month. However, had the member been on the Essential Comprehensive Plan the subsidy would have been R6 500 per month. A member that accepts the offer will receive a benefit of R7 800 per month (i.e. R6 500 increased by 20%) plus insurer guaranteed annual future increases on 1 January each year of CPI + 4% p.a.

Importantly, for members that elect to remain with the DMBT, the assets of the Trust will be an insurance policy which provides the identical benefit, but with the benefit being paid to the Trust. However, the members' current subsidy will be unchanged. Using the above example, the DMBT will receive R7 800 per month increasing on each 1 January by inflation plus 4% p.a. Nevertheless, the Trust will only pay R5 000 p.m. increasing by the actual increase in the medical aid contribution rate to Discovery Health. In this way the DMBT will build-up a surplus, at least initially, to the extent that the amount received from the Insurer exceeds the amount that is paid to Discovery Health for the remaining members. The proposed amendment to the Trust Deed provides that 50% of any surplus built-up in this way should be paid to DENEL SOC every three years, noting that such repatriation can be done more frequently should the Actuary of the Trust so advise.

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Assessment – risks and opportunity for members that elect the buy-out option

It may be best to start with the opportunity that the offer provides for a member that elects the option. From the effective date of the transaction he or she will receive a monthly pension that is at least 20% higher than their current PRMA subsidy. For members that have elected a lower cost option than the Essential Comprehensive Plan, the additional amount received will be higher.

My understanding of the current tax regime is that the member will not pay any tax on that part of his/her pension that is contributed to Discovery Health. However, the part of the pension that is not paid to the medical scheme, will be taxable income in the member's hands.

Accordingly, the benefits accruing to a member that chooses the buy-out option are:

1. Additional income of at least 20% at the effective date of the transaction which is taxable unless the member elects to apply this amount to secure better medical aid benefits.

For members that are on a lower cost option than the Essential Comprehensive plan the additional amount will be higher.

2. Certainty of future pension increase of CPI (year on year to the preceding 30 September) + 4% p.a. on each 1 January on the total lifelong pension including lives of their dependants.

It is important to explain how the pension changes if the member or one of his or her dependants passes away. Again, this is best done by example. The current full contribution rate for the Essential Comprehensive plan is R5 003 p.m. for a single member and R9 734 p.m. for a member with one adult dependant. Accordingly, for a member with Denel SOC's subsidy of 67%, the current subsidy is R3 352.01 p.m. and R6 521.78 p.m. respectively. The subsidy for a single member is thus 51.4% of that of a member with one adult. When one of the parties passes away, the pension will reduce to 51.4% of the pension payable whilst both were alive.

3. The flexibility to choose what they do with their pension. If the member elects a lower cost medical aid option, he or she will still receive the same pension, noting that as per the above any pension not applied to the medical scheme will be taxable. Such flexibility may be valuable to some members.
4. Receipt of a pension that can be applied in part, or full, to pay medical scheme contributions independent of the financial fortunes of Denel. On the other hand, it is unclear as to what may happen to the member's medical aid subsidy if Denel's financial position were to deteriorate to the point where the viability of the company is at risk or if Denel were to be liquidated or subject to some other form of insolvency proceedings.

Naturally, the buy-out offer is not risk-free and the most important risks we have identified are:

- Future medical aid increases by exceed inflation plus 4% p.a. However, the 20% enhancement to the current subsidy provides a buffer against much higher medical aid inflation. The table below estimates how many years it would be before the buy-out pension is exceeded by medical aid increases above inflation by scenario

Medical aid increase from 2022 onwards	CPI + 4.5%	CPI + 5.0%	CPI + 5.5%	CPI + 6% p.a.
Cross over year	2061	2041	2035	2032

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For example, it would take an estimated 20 years for the subsidy to exceed the buy-out pension if medical aid inflation exceeds CPI by 5.0% p.a. from 2022 onwards. However, should medical aid inflation exceed general inflation by 5.5% p.a. the cross over point would be in 14 years time. The reality is that period is longer because the member could invest the difference between the pension received and the amount paid to the medical scheme and this would provide an additional buffer. It follows from the above the risk of medical aid inflation exceeding inflation plus 4% p.a. is more acute for younger members (or members that have young adult dependants).

It is worth highlighting that the actuarial valuation report of 1 April 2021 shows the subsidy weighted average age of the 625 members already in receipt of subsidy ("continuation members") to be 71.5 years. The combined life expectancy of the aggregate continuation membership is estimated at 15 years. This is very close to the 14 year cross-over period should medical aid inflation exceed general inflation by 5.5% p.a., which for the reasons set out below we consider unlikely.

Over the ten year period from 2011 to 2020 the Discovery Essential Comprehensive contribution rate exceeded general inflation by 4.6% p.a. The industry view is that medical aid inflation is expected to exceed inflation by 2% to 3% p.a. in the future. Presumably this estimated is derived from the data which shows that for the 20 years covering the period 2000 to 2019 medical aid inflation across all medical schemes averaged 7.8% p.a. whereas inflation averaged 5.6% p.a.

Our judgement is that at the boundary of the range of plausible outcomes, medical aid inflation could exceed inflation by 5.5% p.a. There is, of course, an outcome beyond the range of plausible outcomes, but we would assign a low chance to such outer reaches outcomes. We say this because there is a constraint on how much members can, firstly afford to pay and, secondly would be willing to pay, for medical aid benefits. To give context, we estimate that if medical aid inflation exceeds inflation by 5.5% p.a. a member that is currently contributing 15% of his or her total income for medical aid contributions would need to allocate 30% (i.e. double) of his or her money for this purpose in fifteen years' time. If the member were currently allocating 20% of income for medical aid, this would increase to 40% after 15 years i.e. the allocation of income doubles after 15 years.

Consequently, it seems to us much more likely that the medical scheme will gradually reduce its benefits to keep the contribution rate affordable as this is somewhat easier to do than hike contributions at a rate that exceeds inflation by more than 5.5% consistently. Alternatively, the member may choose a lower benefit option on the basis of affordability.

Naturally, there are scenarios (the outer reaches) where medical aid inflation exceeds general inflation by such a margin that members that opt-out are worse off. As highlighted above, this risk is more acute for younger members and members with young adult dependants. However, members can reduce this risk by saving the excess pension above their medical aid contribution, although we expect that few will do so.

- The insurance company paying the pension gets into financial difficulty and reduces pension significantly. This risk is mitigated by the choice of Insurer which we understand will be one of Old Mutual, Sanlam or Momentum Metropolitan who are large insurers with reserves that are currently just below twice the Statutory Capital Requirements. Old Mutual is 175 years old, Sanlam is 102 years old and Momentum has been in business for more than 50 years.

Furthermore, the policy would fall under the class of business known as "non-profit". If an Insurer gets into financial difficulty the first loss is borne by the shareholders, then by the with-profit policyholders and then only the non-profit policyholders. In our opinion it would take an extreme event for an insurer like Old Mutual, Sanlam or Momentum to burn through so much capital and adaptive buffers that they would need to reduce the benefits of non-profit policyholders.



- The last material risk we would identify is a legislative change which adversely affects policyholders, with the same legislation not being applicable to the DMBT. Again, we would assess this to be a low probability event. The reason we say this is that the policy and DMBT are intended to deliver the same form of benefit, namely the member's PRMA obligation. Consequently, it is difficult to see why legislation would create a loophole by allowing a favourable environment for one funding vehicle and an adverse environment for another. This is even more so the case because legislation commonly has as one of its stated objective to level the playing fields between market participants to increase competition.

However, we accept the argument that the Trust may have more flexibility to change the arrangement in response to adverse legislation than an Insurer may.

Our sense is that the best way to consider the buy-option is to answer the question: "If my parents were provided with this buy-out offer, would I recommend that they accepted it?" Based on the above analysis our answer is that we would counsel our parents to accept the buy-out offer as we assess that there is a high chance that they will be better off. Of course, there are scenarios where they can be worse off, but in our view this falls into the outer reaches of potential outcomes which have a low probability. We suspect that the main reason for members not to accept the offer is that they are anxious about change and are concerned that they don't understand all the issues fully.

The position of members that elect to stay with the DMBT

As explained previously, the proposed transaction for members that remain in the DMBT is to purchase a group pension that provides for exactly the same benefits as for members that elect the buy-out offer. However, the key difference is that the DMBT will only pay across to Discovery Health the member's current PRMA subsidy, with any subsequent increases thereon (i.e. the member does not receive any part of the enhancement).

For this reason, at least in the early years, the DMBT will receive more income than what it needs to pay away to Discovery. This surplus will be invested in the Fund and 50% of the amount so accumulated must be returned to Denel SOC every three years. The three year period was chosen to correspond to the statutory period for the actuarial valuation of defined benefit arrangements, which is the nature of the Trust. In addition, the Trust Deed will be amended to allow for more regular repatriation of surplus if the Trust's actuary certifies that it is prudent to do so.

Members that elect to remain in the DMBT face the same risks as members that choose the buy-out option, albeit that these risks are lower. We say this for the following reasons:

1. The Trust will build-up a reserve equal to 50% of the excess benefits received from the policy compared to the actual subsidies it pays. Such excess assets can be invested thus earning a return, but at the end of each three years 50% of the reserve will be paid-out to Denel SOC. Effectively this means that the reserve the Trust will build-up over time is 50% of the aggregate excess amount accumulated with investment returns.

Should the subsidy exceed the policy proceeds, the reserve can be used to finance the shortfall to the extent that is able to do so. We highlight that in theory a member that elects the buy-out option could invest the entire excess, but very few are likely to opt to do so and unlike the Trust, the investment return will not be tax-free.

2. The terms of the life annuity policy that the Trust holds will provide for termination on favourable terms for specified breaches including if the Insurer's solvency reserve margin drops below an agreed level. Thus, in the unlikely event that the Insurer starts moving towards a situation where their financial soundness may come under pressure, the Trust will be able to exit the investment. The same right to terminate will not apply to members that opt out of the Trust.

3. It is possible that the Trust will have more flexibility to amend its strategy than an Insurer may have in the event of adverse legislation.
4. Finally, for members that elect to remain with the Trust, the Denel SOC PRMA obligation is unchanged. Thus, the company would need to negotiate in good faith any reduction in the subsidy should the Trust have insufficient assets to meet the subsidy requirement in future.

It is obvious that the higher assets the Trust has, the less likely it is that it will have insufficient money to pay the PRMA subsidy in future. By returning some R800 million of the Trust's assets to the Company, the security of benefits for members is reduced, albeit it in our opinion, slightly if due consideration is taken of the above.

What the term "reasonable benefit expectation" means has never been defined by the Courts. However, most agree that a reasonable expectation means more than a 50% chance of the outcome and some have suggested that to be "reasonable" the chance of the targeted outcome must be at least 80%. Our analysis suggests that the chances of the Trust being able to finance the Denel SOC PRMA liability from the insurance policy only (with the excess assets being returned to the Company) meets this 80% threshold based on known information.

Summary and conclusion

In our opinion, the proposed buy-out offer to the members of the DMBT falls into the category of generous. Naturally there are circumstances in which the member that elects this option is worse off than if they remained in the Trust, but we assess this to be a low probability outcome. On the other hand, there is better than a 50% chance that the member that elects this option will be better off, particularly if one takes the view that medical aid inflation is unlikely to exceed general inflation by more than 4.5% p.a. over the long term and if this happens members, in any way, would move to lower cost benefit options simply on the basis of affordability.

It follows that we are also of the opinion that the Trust will be able to meet the reasonable benefit expectations of members that remain in the Trust with a high probability.

This report was prepared by Antony Lester.



Antony Lester

Date: 21 May 2021



IN THE HIGH COURT OF SOUTH AFRICA
(GAUTENG DIVISION, PRETORIA)

Case no.:

In the *ex parte* application of:

DENEL SOC LIMITED

Applicant

In re:

VARIATION OF THE TRUST DEED OF THE DENEL MEDICAL BENEFIT TRUST

SUPPORTING AFFIDAVIT

I, the undersigned

HENDRIK DANIEL DU PREEZ POTGIETER

do hereby make oath and say that:

- 1 The facts contained in this affidavit are both true and correct and, unless the context indicates otherwise, fall within my knowledge or are apparent from the documents under my control.
- 2 This affidavit is a supporting affidavit to the founding affidavit (the "**Founding Affidavit**") deposited to by Khohlong William Hlakoane on behalf of Denel SOC Limited ("**Denel**"). I have read the Founding Affidavit and confirm the statements made in the affidavit insofar as they relate to me.



- 3 The purpose of this supporting affidavit is to give the background and early history of the establishment of the Denel Medical Benefit Trust ("**Trust**") which took place in the period from 1992 to the early 2000s.

My background

- 4 At the outset, I wish to highlight that my history at Denel is as follows:

4.1 Denel was established in 1992, following a financial reconstruction process in terms whereof the industrial and commercial part of the Armaments Corporation of South Africa ("**ARMSCOR**") was split off to form Denel.

4.2 I am currently one of the officials and member representatives of the Denel Retired Employees Medical Scheme Forum (the "**Forum**"). The Forum's management team is comprised of 8 members. This said, myself and Mr Paul Botha ("**Mr Botha**") predominantly take the day to day managerial decisions. I am told that Mr Botha's affidavit will be delivered separately.

4.3 I have specific knowledge of the history of the Trust and medical aid funding in the Denel Group as a result of being responsible for and/or fulfilling the following roles and positions:

4.3.1 when the preliminary studies were done resulting in the establishment of Denel in 1991/92, I was in charge of the financial work stream;

4.3.2 I was appointed as the Group Financial Director from 1992 to 1997. During this time, I was also involved in the process of forming the

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Denel Medical Benefit Fund ("**Medical Benefit Fund**") which was the predecessor of the Trust;

- 4.3.3 I was appointed statutory director of Denel from 1996 until early retirement in 2005;
- 4.3.4 Sometime around the middle of 1996 until early 1998 I was one of two department Deputy Group Chief Executive Officers;
- 4.3.5 When the structure of Denel changed in 1998, there was a repositioning that took place and I then took over the management responsibility of the Commercial and Information Technology business of the Denel Group while remaining a statutory director. In addition to my role as a director, I would also assist as Group financial director when requested to do so;
- 4.3.6 I retired from Denel in May 2005 and became entitled to post-retirement medical aid contribution subsidy in terms of my service conditions at Denel and consequently also became a beneficiary of the Trust. However, shortly after my retirement, and still in 2005, I was called back by Denel on a contractual basis where I was responsible for managing the disposal of the non-core assets and businesses of the Denel Group. I served on the Board of Trustees of the Trust until 2006. My contract with Denel ended on 31 October 2007;
- 4.3.7 I was an elected Employer representative trustee on Umed, the medical aid scheme of the Denel and ARMSCOR Group for most of

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the time between 1992 and 2005 and was elected member trustee in 2008. At the same time I was elected, as Chairperson of Umed by the trustees until completion of the amalgamation of Umed with Discovery Health Medical Scheme by the end of 2010.

The Start of the Medical Benefit Fund

- 5 Denel was incorporated as a company on 01 April 1992 in terms of the South African Companies Act (No. 61 of 1973) where it was formed out of the industrial part of ARMSCOR.
- 6 During 1992, Denel undertook a due diligence exercise. I was in charge of the financial work stream as part of this process. One of the issues that arose during the associated due diligence, was the risk of the future funding of the pensioners' medical aid at that point in time. The medical scheme and the funding thereof and service conditions were integrated. This was addressed in the "*Verdelings ooreenkoms*" concluded at the time between the Minister of Finance, Public Enterprises, Denel and ARMSCOR.
- 7 There was R100 million reserved for funding the deficit on pensioner medical aid contributions in terms of the said "*Verdelings ooreenkoms*". The reason for the deficit was that at the time of establishment of Denel , Denel and ARMSCOR were appointing very few new younger employees with a lower medical claims profile , and as such there was a reduction in staff from approximately 20 thousand to 12 thousand over a period of 2 years resulting in an unfavourable age profile of the workforce. As a result of the Defence Force's failure to honour its contracts, there was a claim in 1992 against the Defence Force. Furthermore, the SA National Defence Force reimbursed Denel/Arm Scor in 1992/93 for the cost of supply contract



cancellations. The part of the claim allocated to the medical aid funding deficit amounted to R116,7 million and the money was kept in trust together with the R100m referred to above.

- 8 Various options were investigated in order to preserve the money reserved for the underfunding of the medical aid deficit. Moreover, Denel attended discussions with the South African Revenue Services ("SARS") where discussions were held and a partner from Coopers Du Toit Incorporated (now part of PwC), Koos van Wyk, worked on the tax issues. The final recommendation was to keep the money in trust. Following discussions with SARS the recommendation by Willem Coetzee of SARS was that the money should be put in a vehicle which was, in legal terms the Medical Benefit Fund. The Medical Benefit Fund had a favourable tax treatment particularly in relation to paragraph c under the definition of *benefit fund* in section 1 of the Income Tax Act (No.58 of 1962). Essentially the Medical Benefit Fund was tax exempt. As such, the funds were put in the Medical Benefit Fund which process was approved by the board of Denel in 1992.
- 9 As part of the financial reconstruction transaction with the establishment of Denel, the net value of the assets and liabilities thereof were split out of the ARMSCOR group and there was a capital reduction on ARMSCOR's side. In *lieu* of this, shares in Denel were issued to the Government.
- 10 During this period (1992/1993) of establishing Denel and the Medical Benefit Fund, there had been no discussions as to what would happen should there be a surplus in the Medical Benefit Fund. The way that the Medical Benefit Fund was managed was that it was used as a vehicle to fund the monthly deficits on the Denel Medical Scheme. Calculated on an actuarial basis for current and future funding the Medical Benefit Fund was underfunded and there were consequently contributions made by

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Denel that were based on the Denel medical aid scheme monthly contributions. The scheme was also not a closed one at that point and it would have been possible to reduce the ongoing contributions of Denel to ensure that a surplus never arose. As such there was no need to deal with a surplus of assets relative to a closed pool of pensioners and there was therefore no discussion of how to deal with such a surplus.

Formation of the Trust

11 In the period between 1999 and 2000, the following two things happened:

11.1 Parliament enacted new medical aid scheme legislation. This meant that the way that the funding was being done in the Medical Benefit Fund could not be continued. Persons in receipt of a pension could not pay less than those who were not, as the legislation required uniform contributions ; and

11.2 tax legislation changed and the Medical Benefit Fund no longer benefitted from an exemption from paying tax as envisaged at establishment in terms of paragraph c under the definition of benefit fund in section 1 of the Income Tax Act (No.58 of 1962.

12 Additionally, there was underfunding in the Medical Benefit Fund, and it became clear from the increase in medical contribution costs that it would be impossible for Denel to carry on running and funding the medical aid cost of employees and pensioners through the Medical Benefit Fund as envisaged in 1992. Thus, a proposal to change the service conditions of the Denel Group was made so as to provide that new appointments would not qualify for post-retirement medical benefit subsidies. Accordingly, a closed liability was created. To fund part of this liability, the surplus of



the defined benefit pension fund of Denel, this being the Denel Pension Fund, was used to compensate this section of pensioners through an increase in monthly pension against a reduction in post-retirement medical scheme contributions.

- 13 Approval for the strategy above was obtained around April 2000. Ways of dealing with tax issues for the previous benefit policies were considered, Metropolitan was approached and this assisted in tax liability reduction. SARS had approved this approach, and the approval required in terms of the Public Finance Management Act (No.1 of 1999) was obtained in late 2000. As a result, the Trust Deed was signed in October/November 2002.
- 14 Forming the Trust was simple. The assets of the Medical Benefit Fund were transferred to the Trust. The transfer was done from the Medical Benefit Fund, as founder of the Trust, to the Trust which Trust was then, and is now, governed by the current Trust Deed. At the time that the Trust was established it had a small actuarial surplus . At this point, (subject to some exceptions) the beneficiary base of the Trust was closed as the service conditions of the Denel Group had been changed to accommodate the new strategy.
- 15 Similar to the events in 1993, there had been no considerations of a surplus arising. The intention was to release the monthly financial burden on Denel. Denel's monthly contribution based on the then current medical scheme contributions ended at that point in time giving some relief. Denel was only required to make a contribution to the Trust where a beneficiary retired early. This was based on an actuarial calculation using the remaining period to normal retirement age. As a result of the focus on an under-funded position, there was no regard given to the possibility of there being a surplus.




16 The Denel Personnel and Remuneration Committee Memorandum, attached in the Founding Affidavit as "FA4" sets out the strategy for revisiting the funding of the healthcare liability. The memorandum was signed in February 2000 and the Trust deed signed, as stated below in October/November 2002. In sum, the sequence is as follows:

16.1 31 March 2002 – approval;

16.2 October 2002 – Trust Deed signed and capitalised; and

16.3 Following a period of a year, the assets were at R845 million, which was paid to Metropolitan as a premium for a with profit annuity policy.

17 Subsequent to the strategy, Denel passed resolutions which show that there had been a number of meetings held to try and get the relevant parties to agree to the strategy. We needed to do a few things at this point, that is:

17.1 One of the Trustees of the Denel Pension Fund went out to get all the buy-in from the members;

17.2 Once obtained, this was taken to management; and

17.3 There needed to be the support for the Metropolitan Policy which was still subject to a tax regime being obtained.

18 The Executive Committee of Denel approved the Metropolitan Policy principle and the tax matter was referred back due to the tax directive not being obtained at the time. Following this, the Minister of Public Enterprises approved the entity. At this point, I was no longer the Financial Director. Once all of the above was done to completion, the Trust could continue to run in its format.

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- 19 The Fund had to be liquidated at the point of transfer. The Trust mainly functions as a vehicle to meet Denel's current and future obligations. The Trust holds assets for the benefit of the beneficiaries. It does not guarantee Denel's obligations but simply holds the assets against Denel's liability.

Early Retirement of Beneficiaries

- 20 The funding of the Trust and the strategy approved in 2000 was based on members who retired at age 65. In the case of people retiring prior to the age of 65, annual actuarial valuations were done to state what would be needed if someone retired at 55 to cover the funding between 55 and 65 years. The actuarial valuation determined what Denel's contribution would be to make good for the early retirement. Denel therefore was, until 2007 responsible for putting this money into the Trust. This was Denel's only contribution to the Trust between 2001 and 2007.
- 21 The amounts were relatively small, as the big obligation was funding from retirement until death. Overall, until 2007, the Trust was funded by its initial capital, and in respect of early retirement by a top up amount to cover the period between actual date of retirement and projected retirement at age 65. The principle at that time was that there were delegations of authority, where if the early retirement decisions were taken elsewhere (eg a Denel Division in Cape Town) these costs were also taken into consideration. The recommendation to waive early retirement contributions was made in 2006.

Contemplation of excess assets

- 22 The reason for the excess assets are mainly two-fold:

22.1 Better returns on investment; and



- 22.2 Buyouts of the future subsidy funding obligation that Denel offered to employees and pensioners accepted by some employees and pensioners since 2008 which offers were lower than what the cost would have been if the members remained beneficiaries of the Trust until death.
- 23 In the case of the Medical Benefit Fund, the scheme operated so as to ensure there was no surplus – this was because the Medical Benefit Fund received ongoing employer contributions and was open to new members. In the case of the Trust, the main focus was on curing the actuarial deficit hence the possibility of a surplus arising was not considered when the Trust was established.
- 24 As mentioned earlier, when the Trust was being formed, there was no anticipation of a surplus. Moreover, the aim and plan was that the benefits would be adjusted as and when people die. The fund would thus be a *diminishing fund*. Since 2008, Denel made buyout offers to the Denel employees and pensioners which were accepted by some. Buying out members constitutes one of the reasons for the surplus in addition to there being favourable returns. In light of this, there was also flexibility in relation to the contributions that Denel could make to the Medical Aid liability as well as in relation to what benefits would be covered by the Trust. Accordingly, Denel would not have had a material surplus in the Trust because the liabilities would 'exceed' the surplus or be provided for from the surplus, should it arise. To the extent that there was a surplus, it could be managed with either contributions or by benefit adjustments being effected by Denel.



11


HENDRIK D.D. POTGIETER

I certify that the deponent acknowledged that s/he knows and understands the contents of this affidavit, which was signed and sworn to before me at Centurion on this the 25th day of **MAY 2021**, in accordance with Regulation No. R1258 dated 21 July 1972 as amended by Government Report R1648 dated 19 August 1977, as further amended by Government Report R1428 dated 11 July 1980, and by Government Report R774 of 23 April 1982.

KAREN CROUSE
COMMISSIONER OF OATHS R.S.A
PRACTISING ATTORNEY
CONVEYANCER
CNR SAXBY & FREDERIK ST
ELDORAINNE - CENTURION
GAUTENG



COMMISSIONER OF OATHS

Designation and Area:

Full Names:

Street Address

IN THE HIGH COURT OF SOUTH AFRICA
(GAUTENG DIVISION, PRETORIA)

Case no.:

In the *ex parte* application of:

DENEL SOC LIMITED

Applicant

In re:

VARIATION OF THE TRUST DEED OF THE DENEL MEDICAL BENEFIT TRUST

SUPPORTING AFFIDAVIT

I, the undersigned

PAUL ROUX BOTHA

do hereby make oath and say that:

- 1 The facts contained in this affidavit are both true and correct and, unless the context indicates otherwise, fall within my knowledge or are apparent from the documents under my control.
- 2 This affidavit is a supporting affidavit to the founding affidavit (the "**Founding Affidavit**") deposed to by Khohlong William Hlakoane on behalf of Denel SOC Limited ("**Denel**"). I confirm that I have read the Founding Affidavit and confirm the statements made in the affidavit insofar as they relate to me.



- 3 The purpose of this supporting affidavit is to give the background to the negotiations and communications that took place in the period from 2011 to 2021 between Denel and the Forum.

My background

- 4 At the outset, I wish to highlight that my history at Denel is as follows:
- 4.1 in 1992 when Denel was established following a financial reconstruction process in terms of which the industrial and commercial part of the Armaments Corporation of South Africa ("**ARMSCOR**") was split up, I was appointed International Marketing Manager at Denel reporting to the Group Marketing Director. This position was similar to the position I previously held at ARMSCOR.
- 4.2 In about 1996, I was appointed as Director Marketing Asia and Middle East;
- 4.3 I retired from Denel in 2004 and as a beneficiary of the Denel Medical Benefit Trust (the "**Trust**") and became entitled to a post-retirement medical aid contribution subsidy in terms of my service conditions at Denel .
- 4.4 I am currently one of the officials and member representatives of the Denel Retired Employees Medical Scheme Forum (the "**Forum**") and was also elected Chairman of the Forum. The Forum's management team is comprised of 8 members. This said, only two people predominantly take the day to day managerial decisions, that is myself and Mr Hendrik Potgieter ("**Mr Potgieter**"). I am advised that Mr Potgieter has delivered a separate affidavit in this matter.



- 5 The Forum was established in 2010. The main purpose of its establishment was to promote and protect the interests of retired employees insofar as the post-retirement medical aid scheme benefits in terms of their service conditions with Denel were concerned. The Forum was further established with an intention to safeguard the interests of the retired employees in the Trust. The Forum's establishment occurred at a time when there were changes in benefits due to the amalgamation of the UMED with Discovery, following which a number of buy-out offers were made by Denel to beneficiaries which the Forum did not consider to be fair and equitable for the beneficiaries. As I understood it, the purpose of the then buy-out offers by Denel was to remove the obligation to fund the post-retirement benefits from the balance sheet of the company. I was integrally involved in those negotiations on behalf of the Forum. This said, given the amount of time that has lapsed since the negotiations took place, I rely hereunder on the related documents and correspondence which are in my possession.
- 6 On 3 May 2011, the Forum sent a letter to the Denel Group's former Chief Executive Officer, Talib Sadik (the "**Mr Sadik**"). In this letter, the Forum proposed to Mr Sadik a solution that would assist in removing the obligation to fund the post-retirement medical contributions subsidy that Denel owed to pensioners who were beneficiaries of the Trust from the company's balance sheet. At the same time, this solution would enable Denel to offer a fair alternative dispensation to beneficiaries. A copy of this letter is attached as "**PB1**".
- 7 Denel had sent buy-out letters to the members of the Forum three years before this communication as sent to them. The Forum was of the view that the buy-out offers made by Denel were not 'attractive' to the beneficiaries. The buy-out offer at that point in time was only accepted by approximately 50% of the beneficiaries of the

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Forum. I pause to mention that according to the Forum, some of the reasons why the offer was not accepted included *inter alia* that (i) the pensioners were offered only one option; (ii) the option was tax inefficient for pensioners under the age of 65; (iii) the quantum being offered was insufficient; and (iv) the beneficiaries were not consulted prior to the offer being made.

8 In light of the above, the Forum made the following proposal in the aforementioned letter which is attached as “PB1”:

8.1 First, that Denel should appoint a core team which would include two Forum members; the Board of the Trust; a representative to function as Denel’s Human Resources and the Principal Officer of the Trust;

8.2 Second, that the core team would be responsible for defining the terms of the offer and reaching agreement with Denel and the Board of the Trust; and

8.3 Third, that the core team would investigate and formulate options to be made available to the beneficiaries taking into consideration the interests of the beneficiaries. The Forum further proposed that specialist advice would have to be sought on this point, and that the Board of the Trust and Denel would be approached to approve a final proposal made by the core team. This process was to be completed by December 2011.

9 On 1 September 2011, the Denel Group HR, Patience Mushungwa (“Ms Mushungwa”) provided an explanation of the amalgamation of UMED and Discovery which had taken effect on 1 August 2011. Ms Mushungwa indicated that Denel had not decreased the subsidy policy in any manner. This only dealt with one



element of the letter from the Forum dated 3 May 2011. A copy of Ms Mushungwa's letter is attached hereto marked "PB2".

10 On 17 October 2011 and 23 November 2011, the Forum sent two further letters to Mr Sadik, copies of which are attached hereto marked "PB3" and "PB4", respectively.

10.1 In the 17 October 2011 letter, the Forum noted that its intention was to work with Denel constructively in reaching a solution for Denel's desire to remove the post-retirement obligation from its balance sheet.

10.2 In the letter dated 23 November 2011, the Forum expressed distrust in the Group Executive: HR and requested direct representation on the Board of Trustees.

11 Denel's Group Chief Executive Officer, Riaz Saloojee ("Mr Saloojee") wrote back to the Forum on 9 March 2012 ("PB5"). Mr Saloojee denied the Forum's request to have direct representation in the Board of Trustees of the Trust. Mr Saloojee assured the Forum that Denel's financial soundness and its ability to meet its financial obligations was not a concern.

12 On 16 November 2012, a meeting was scheduled to take place between two Denel officials, Themba Zwelibanzi ("Mr Zwelibanzi") and Mike Ngidi ("Mr Ngidi") Denel's acting Group HR Director at that time, and Mr Potgieter representing the Forum. Feedback provided by Mr Potgieter regarding the post-retirement obligation after the meeting was as follows:

12.1 Objectives of Denel with remaining post retirement obligation:

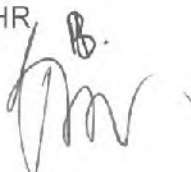
12.1.1 To get rid of the obligation on its balance sheet;



- 12.1.2 To gain access to the surplus in the DMBT to the benefit of Denel;
 - 12.1.3 To demonstrate progress at financial year-end (31 March 2013)
- 12.2 Opinion expressed by/position of the two officials of Denel:
- 12.2.1 They realize the benefit of cooperating with an organised group like the Forum;
 - 12.2.2 They realize that the representatives from the Forum need to be involved at an early stage of the process;
 - 12.2.3 They did not disagree when it was put to them that somebody independent needed to facilitate exploring of new options;
 - 12.2.4 They agreed that a formal process such as the recent Denel Retirement Fund process needs to be followed; and
 - 12.2.5 The parties agreed that the first meeting with Forum representatives would be scheduled for 5 December 2012.
- 13 A full meeting of the Forum management was held on 22 November 2012 where feedback of the meeting held with Denel officials on 16 November 2012 was provided. This meeting (and the discussions thereof) was held in accordance with the agenda attached hereto as "PB 6". At the meeting, the Forum management provided Mr Potgieter and I with the support and mandate to negotiate with Denel.
- 14 On 5 December 2012, I wrote to the Forum giving feedback on the meeting that Mr Potgieter and I had with the Mr Ngidi and Mr Zwelibanzi:



- 14.1 From a summary of the meeting that I sent to Mr Potgieter, a copy of which is attached to this affidavit as "PB7", it appears that myself, Mr Zwelibanzi and Mr Ngidi agreed on the principle of "gain share" for Denel and the members of the Forum. The principal of "gain share" was based on the fact that the beneficiaries were to derive a further benefit which was in addition to the obligation that Denel owed to them as a result of the additional risk which the beneficiaries would have to carry with the removal of the guarantee from Denel and part of the surplus funds in the Trust being allocated to Denel.
- 14.2 There was also agreement on the fact that an independent consultant should be appointed, and that the consultant would need to give their views on the available options and a fair split of the reserves in the Trust. The preferred consultant that was mentioned by Mr Potgieter was Antony Lester of Willis Towers Watson ("**Mr Lester**").
- 15 On 12 January 2013, I received an email from Mr Zwelibanzi indicating that Mr Ngidi was working on the matters arising from the meeting of 5 December 2012. The email is attached to this affidavit as "**PB8**".
- 16 Although Mr Potgieter and I maintained contact with Mr Zwelibanzi from Denel's side, no progress was made until the next meeting between the ourselves and Denel on 13 August 2013. I believe one of the reasons is the passing away of Mr Ngidi during this period.
- 17 On 5 August 2013, Mr Potgieter and Sam Basch one of the management members of the Forum ("**Mr Basch**"), attended a meeting with the Denel and on behalf of the Forum. The erstwhile Denel Chief Financial Officer Fikile Mhlontlo ("**Mr Mhlontlo**"), Gawie van Zyl ("**Mr van Zyl**"), Mr Zwelibanzi and Ms Makatini, one of the HR,



members of Denel attended the meeting. Following this meeting, Mr Basch sent an email to the members of the Forum management on 7 August 2013 providing feedback on the discussions. The discussions in the meeting related to the policy options that Denel was considering as well as approval that had been obtained from the South African Revenue Services (“SARS”). A copy of this email is attached as “PB9”.

- 18 In the meeting it was clearly stated by Mr Potgieter that the buy-out option tabled by Mr Mhlontlo will not be recommended to the beneficiaries by the Forum as it was not considered to be fair. The parties, however, agreed to remain in contact to arrive at a mutually beneficial solution. Mr Potgieter also proposed the option where the beneficiaries would take over the Trust as part of a settlement. In terms of this solution, Denel would be released of its obligation and a part of the surplus in the Trust would be distributed to Denel with a fair amount of funds being retained in the Trust for a distribution that would cover the future obligation towards beneficiaries including a risk premium and an enhancement.
- 19 On or about 9 December 2013, Denel proceeded with the process of offering buy-out options to beneficiaries again. The view of the Forum management was that the annuity options included in the offer was not fair and equitable. The Forum consequently could not recommend it to members. The option of a beneficiary managed Trust was put as an option by Denel without quantifying the amounts or basis of calculating such amounts to be retained in the Trust for the benefit of the beneficiaries. During this period, 450 beneficiaries indicated that they would be interested in the beneficiary-managed trust option;
- 20 A meeting was held with Denel delegates at their offices on 27 May 2014.

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- 20.1 The following matters were discussed:
- 20.1.1 The appointment of a suitably qualified impartial consultant to assist with the process; and
- 20.1.2 A plan as regards how to deal with the beneficiaries who did not react to the choices of alternative benefits offered.
- 20.2 At the meeting, the Denel delegates indicated that these beneficiaries would be defaulted to the Trust option).
- 21 On 11 June 2014, Mr Zwelibanzi sent the Forum an email following the meeting that Denel had with the Forum management representatives on 27 May 2014 as described above, a copy of which is as "PB10". The purpose of this email was to give a written update that an independent adviser had been appointed to look at the options that were available as well as to express a view on the advantages and disadvantages of each option that Denel was proposing to the beneficiaries.
- 22 At this point I wish to highlight the following:
- 22.1 The scope of the work of the independent adviser was focused on facilitating an agreement between Denel and the remaining beneficiaries of the Trust.
- 22.2 In light of Denel seeking to be relieved of the post-retirement medical aid liability, the scope also included looking at, *inter alia* investment return in excess of medical inflation; medical inflation in excess of consumer price index ("CPI"); mortality post-retirement; mortality status assumptions; CPI in general and a "sweetener". The scope of work is attached to this affidavit as "PB11".



- 22.3 The independent adviser was also required to provide, (i) input on the structuring of the Trust and investment policy; (ii) guidance on the best possible ways of structuring the benefits; and (iii) input regarding the documentation for the final solutions that would be agreed upon between Denel and the Forum.
- 23 On 31 October 2014, it was confirmed that Mr Lester would advise the Forum, and the Terms of Engagement were provided by the Forum. These terms are attached to this affidavit as "PB12".
- 24 Thereafter, in November 2014, Mr Lester delivered a report to the Forum which dealt with the quantum of assets to be retained in the Trust to meet its future obligations for medical aid contributions (the "Report"). This report is attached as "PB13".
- 25 On 21 January 2015, I sent feedback to the rest of the Forum management regarding a meeting that Mr Potgieter and I had with Denel where we discussed the Report prepared by Mr Lester ("PB14"). It appeared from the feedback that Mr Mhlontlo, was not happy with the total amount to be allocated to beneficiaries that had been recommended in the Report. The email relaying this is attached as "PB14".
- 26 On 27 January 2015, the Forum wrote a letter to Denel responding to its rejection of the amounts arrived at in the Report, requesting an explanation of which assumptions are being disputed, a copy of which is attached as "PB15". In this letter, the Forum also indicated that it was of the opinion that a suitable resolution for all parties could be achieved and accordingly proposed a meeting to discuss the Report.
- 27 On 4 February 2015, Mr Mhlontlo wrote to the Forum stating that Denel would not be considering the proposal made by the Forum any further. The letter is attached to this

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affidavit as "PB16". Instead, Mr Mhlontlo advised that Denel would be exploring other avenues including the possibility of restructuring the Trust with Denel remaining as the underwriter; offering annuity insurance to pensioners receiving medical subsidies at that time. Additionally, the options included making lump sum payments to active Denel Retirement Fund ("DENRET") members and paying cash to those who were not DENRET members. As a result, the negotiations were terminated.

- 28 On 5 March 2015, the Forum addressed correspondence to Denel wherein they accepted Denel's position with regard to the termination of negotiations regarding their proposal ("PB17"). Further, the Forum noted a large difference in the figures that Denel had in their solution compared to those of the Report prepared by Mr Lester.
- 29 Thereafter, on 23 March 2015, a meeting was held between Denel and the Forum representatives where the Report was discussed, including the concerns that Denel had raised with the Report. This meeting was attended by Mr Potgieter and I on behalf of the Forum and feedback was provided to the other Forum representatives thereafter. The main concern raised at the meeting was that the gap between the calculations and assumptions Denel made in their solution was very significant when compared to those made by Mr Lester. It would be difficult to bridge the gap given the large disparity.
- 30 On 21 May 2015, Mr Basch and Mr Potgieter attended a meeting with Mr Mhlontlo where the aim was to revive the negotiations and consultations between the Forum and Denel with regard to the post-retirement medical benefit trust proposal. Following this meeting, Mr Mhlontlo wrote to the Forum informing us that the offers that Denel was willing to make were examined by independent advisers each of whom made



their own industry based-assumptions in respect of each offer. The independent advisers were Towers Watson and NMG. This letter dated 12 June 2015, is attached as "PB18".

31 Following the reports of the two independent advisers, Denel clarified the offers that it was willing to make to the Forum. After receiving a report from NMG as well as the Report from Towers Watson, the Forum wrote back to Denel on 12 June 2015 proposing that NMG and Towers Watson provide a consolidated report.

32 On 24 June 2015, Mr Mhlontlo responded to the Forum rejecting their suggestion for a consolidated report from the two independent advisers, and emphasising the fairness and reasonableness of Denel's proposal in the letter. The 24 June 2015 letter is attached as "PB19".

33 Thereafter, the Forum requested that Denel afford us a reasonable amount of time to engage with NMG and to get clarification with regard to its report. This request was made by email on 25 June 2015 to Mr Mhlontlo who then emailed the Forum back on 26 June 2015 acknowledging our request to communicate with NMG without Denel interfering. This communication is attached as "PB20".

34 On the other hand, Denel refused the request made by the Forum to delay distributing offer letters to pensioners. The reason for Denel's refusal was that it intended for the negotiations to be finalised by December 2014 and it was not in a position to keep the matter open endlessly.

35 On 15 July 2015, NMG delivered an explanatory letter pertaining to its report to the Forum dealing with the report's appropriateness and the assumptions made in compiling the report. This letter is attached as "PB21". The crux of this matter was

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that the figures of NMG were based on the Accounting Standard AS 19 which led them to arrive at the obligation disclosure in the Annual Financial Statements of Denel. The letter from NMG acknowledged that their report was not appropriate for the purpose of determining the required asset value to back future benefit payments as it provided a best estimate of the liability values with a 50% chance of understating the liability. NMG further acknowledged that a more prudent approach would be more appropriate to be used for this purpose.

36 Two days later, on 17 July 2015, a meeting was held by Denel. This meeting was attended by Mr Potgieter and myself on behalf of the Forum. At this meeting, the Forum discussed with Denel the reports from NMG and Towers Watson as well as the Forum's concerns with the offer Denel was making to the beneficiaries. The Forum decided that they would communicate with the members, letting them know that they had been unable to reach a suitable agreement with Denel after the negotiations.

37 Five months later, on 1 December 2015, the Forum represented by Mr Potgieter and I had another meeting with Denel, this time with Mr Ntshepe, the acting Group Chief Executive Officer at the time. At this meeting, it was discovered that Denel was in the process of making another buy-out offer to the beneficiaries. The Forum presented Denel with a further solution that they were to discuss with the erstwhile CFO and acquire the approval of the Board of Trustees prior to making a decision. The offer made by Denel in December 2015 again included annuity options based on assumptions that the Forum considered unfair to beneficiaries. Additionally, Denel offered beneficiary-managed Trust options without quantifying the amount to be held in the Trust for the benefit of the beneficiaries. This offer was not supported by the Forum due to it being unfair and lacking transparency.



- 38 On 4 April 2017 a meeting was held on request of Denel between the Forum management represented by Mr Potgieter and myself and Denel represented by Mr Van Zyl (then acting CFO of Denel) and Mr Zwelibanzi. Mr Van Zyl indicated that Denel reconsidered their position and were open to accept a settlement with beneficiaries with the 2014 Report with adjustments to future investment return assumptions as a point of departure.
- 39 Following the meeting of 4 April 2017 on 19 May 2017, the Forum submitted a summary document to Denel for the attention of Mr Van Zyl and Mr Zwelibanzi which dealt with securing post-retirement medical aid subsidies for the remaining members. The summary document is attached as "PB22".
- 40 On 29 January 2019, a meeting was between the Forum management (represented by Mr Potgieter and I) and Denel (represented by Mr Van Zyl and Mr Wim de Klerk, who was seconded to Denel by the Board). The Denel delegates confirmed that they were keen to reach a mutually beneficial agreement with the Forum.
- 41 Following the meeting, and on 22 July 2019, the Forum sent an updated proposal to Mr van Zyl which dealt with *inter alia* review assumptions, tax dispensation and future obligations. This proposal is attached as "PB23". In execution of the first point in the proposal of 22 July 2019, Towers Watson was appointed to prepare an updated report and recommendation. On 25 October 2019, Towers Watson signed a contract of engagement with Denel, attached hereto as "PB24".
- 42 The Forum provided Denel with a revised proposal and insurer quotes obtained by Towers Watson for their consideration in the hope of revising the negotiations between them and Denel. This letter was sent to Mr van Zyl on 27 January 2020 and is attached as "PB25".



- 43 In March 2020, Towers Watson provided Denel with a further report. This report is attached as "**PB26**". The report indicated that Denel and the Trust were considering reaching an agreement in terms of which the obligations of current beneficiaries would be outsourced in the form of an annuity to an insurer. This report also dealt with the assumptions regarding medical inflation; risk premium, taxation; a proposed legal structure; and a way forward for the proposed outsourcing of the liabilities.
- 44 On 18 June 2020, I sent an email to the other representatives of the Forum, attached as "**PB27**". It included an email from Mr van Zyl stating that Denel was comfortable with the assumptions made by the insurers in the insurer quotes and made a counter-offer that the Forum's requested 25% risk premium be reduced to 15%.
- 45 Nine days later, on 27 June 2020 the Forum responded to Denel with a further proposal that the reduction of the proposed risk premium be limited to 5%. As such, the Forum was willing to accept a risk premium of 20% over Denel's counter-offer of 15%. This response is attached as "**PB28**".
- 46 Following the letter of the Forum, a Zoom meeting was held between Mr Potgieter and I on behalf of the Forum and the Denel Audit and Finance Committee on 2 July 2020 where the terms as proposed in the said letter were agreed on and subsequently confirmed by the Denel Board. The feedback email regarding this meeting is attached as "**PB29**" and the draft letter to pensioners/beneficiaries to this effect from Mr van Zyl is attached as "**PB30**".
- 47 From the above, it is evident that the negotiations between Denel and the Forum were fruitful and a solution that satisfies both parties was ultimately agreed upon.

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48 In the Founding Affidavit, Denel seeks a variation and amendment of the trust deed of the Trust (the "Application"). The objective of the Application to amend the trust deed of the trust as described in the Founding Affidavit is two-fold. First, the amendments will make it possible to issue a group annuity to the Trust and individual annuity policies to beneficiaries who elect to receive such a policy; and second, the amendments will authorise the Trustees to distribute the Trust's excess assets to Denel as capital distributions.

49 Since the beginning of 2021, Denel has been in contact with Mr Potgieter and I regarding various aspects of their Application. The last meeting was held on 8 April 2021 with Denel and their attorneys of record discussing details regarding communications strategies and the offer to be made to the beneficiaries of the Trust.



PAUL ROUX BOTHA

I certify that the deponent acknowledged that ^Bhe/she knows and understands the contents of this affidavit, which was signed and sworn to before me at PRETORIA on this the 24th day of MAY 2021, in accordance with Regulation No. R1258 dated 21 July 1972 as amended by Government Report R1648 dated 19 August 1977, as further amended by Government Report R1428 dated 11 July 1980, and by Government Report R774 of 23 April 1982.




COMMISSIONER OF OATHS

Designation and Area: Attorney; Pretoria

Full Names: Brezilda van Heerden

Street Address 204 Xcel Park; Cnr. Lynnwood & Roderick Roads; Lynnwood; Gauteng; 0081

<small>I CERTIFY THAT THIS DEPONENT HAS ACKNOWLEDGED THAT HE/SHE KNOWS AND UNDERSTANDS THE CONTENTS OF THIS AFFIDAVIT THAT HE/SHE DOES NOT HAVE OBJECTION TO TAKING THE OATH, AND THAT HE/SHE CONSIDERS IT TO BE BINDING ON HIS/HER CONSCIENCE, AND WHICH WAS SWORN TO AND SIGNED BEFORE ME AT <u>PRETORIA</u> ON THIS THE <u>24th</u> DAY OF <u>MAY 2021</u>, AND THAT THE ADMINISTERING OATH COMPLIED WITH THE REGULATIONS CONTAINED IN GOVERNMENT GAZETTE NO. R1258 OF 21 JULY 1972, AS AMENDED</small>	
<u>Brezilda van Heerden</u>	<u>24.05.2021</u>
<small>BREZILDA VAN HEERDEN ATTORNEY COMMISSIONER OF OATHS (RSA) 204 XCEL PARK, LYNNWOOD, PRETORIA</small>	<small>DATE</small>

THE DENEL RETIRED EMPLOYEES MEDICAL SCHEME FORUM

3 May 2011

Attention: Mr. Talib Sadik

Group Chief Executive Officer
Denel (Pty) Ltd
PO Box 8322
Centurion
0046

Dear Mr Sadik,

PROPOSED SOLUTION TO REMOVE THE OBLIGATION TO FUND POST RETIREMENT MEDICAL CONTRIBUTION SUBSIDY FROM THE BALANCE SHEET OF DENEL

1. Purpose of this letter:

The purpose of this letter is to propose a solution to Denel for your kind consideration that would remove the obligation to fund the post retirement medical contribution subsidy from the balance sheet of Denel to the mutual benefit of Denel and pensioners and future pensioners that are beneficiaries of the Denel Medical Benefit Trust ("DMBT").

2. Background on the Denel Retired Employees Medical Scheme Forum:

We would first like to take the opportunity to introduce our organization to you. The Denel Retired Employees Medical Scheme Forum ("The Forum") is a voluntary association of retired Denel employees established in 2010 to promote and protect the interest of its members by:

- Promoting their continued membership of an effective and competitive medical scheme;
- Protecting their rights to a continued percentage subsidy as per service conditions;
- Safeguarding their rights as capital beneficiaries of the DMBT;

The Forum soon attracted a membership of approximately 150 and is continually growing.

In striving to achieve its objectives, the Forum wants to engage with the DMBT and Denel in a constructive way. We would also like to state that we were in support of the initiatives of Umed and Denel to find a solution for sustainable medical scheme benefits through the amalgamation with DHMS and appreciate your personal role (and that of the Group Director HR and Transformation), in the long and cumbersome process.

Chairperson: P Botha.

Other Officials: Dr TJ van Reenen, SA Louw, H D du P (Pottie) Potgieter, J Swart, JJ van Rensburg, F Naude, J P van Wyk



THE DENEL RETIRED EMPLOYEES MEDICAL SCHEME FORUM

3. Importance of post retirement medical scheme contribution subsidy benefit to Denel pensioners:

Most of the pensioners spent their professional life in an era where remuneration packages comprised of lower cash packages but with more perks than today's norms. Consequently amongst Denel pensioners one would find many pensioners who were in senior professional positions during their careers, with relatively low pensions and insignificant personal balance sheets. For this reason pensioners put a high value to benefits that they are entitled to in terms of their service conditions such as the post retirement medical scheme contribution subsidy benefit. One should not blame them if changes to benefits sometimes become an emotional matter as it is quite often due to lack of communication and/or insufficient and incorrect information.

4. Our understanding of Denel's desire to free themselves of the post retirement medical scheme contribution subsidy obligation:

We as a group have a good understanding of Denel's desire to get the post retirement medical scheme contribution subsidy obligation off the balance sheet of the company as was communicated in the two buy-out offer letters received from Denel during the last three years. We furthermore understand that Denel needs to focus on its core business and that all additional issues consume very scarce management resources. However, a buy-out offer needs to be beneficial to both parties and we did not consider the buy-out offers received to date attractive, in particular not to pensioners. Our opinion is that this is the reason why less than 50% of beneficiaries accepted the last offer. Our reservations regarding the previous offer and the prime reasons why the offer was not accepted are the following:

- Pensioners were only offered one option based on a group annuity;
- It is tax inefficient to pensioners under the age of 65;
- The quantum of the offer was insufficient;
- Beneficiaries were not consulted but were only confronted with an offer.

We believe that an important reason why different options were not offered or pursued can be attributed to the fact that the process was to a very large extent driven by an outside service provider that also had the business goal of offering the group annuity. This was a clear position of conflict of interest.

The pensioners in general experience a lack of communication from Denel regarding matters important to them. This was again demonstrated in the confusion regarding the level of post retirement subsidy after the implementation of the Discovery amalgamation. We understand that communication with pensioners from Denel's position is difficult particularly in view of the many restructuring events the Denel Group and before that the Armscor Group was subject to. However, if there is still a service condition link such as

Chairperson: P Botha.

Other Officials: Dr TJ van Reenen, SA Louw, H D du P (Pottie) Potgieter, J Swart, JJ van Rensburg, F Naude, J P van Wyk



THE DENEL RETIRED EMPLOYEES MEDICAL SCHEME FORUM

the post retirement medical contribution subsidy, good communication remains essential. In the interest of efficiency it is advisable to arrive at an amicable settlement to sever the link. Our proposal below is aimed at achieving that.

In any new endeavour to entirely remove the obligation from Denel's balance sheet, it is important that lessons are learnt from the previous process. Perhaps the most important lesson is the one of proper communication and prior consultation and involvement that would go far to let reasonable people buy into a proposal.

We do not have the exact figures on the obligations and funding level of the DMBT at our disposal and are aware that an actuarial valuation is being done for 31 March 2011 as part of the annual exercise. However, based on the projected figures from last year as well as the lower than assumed increase for 2011 by DHMS, we believe that the current funding level of the DMBT is very favourable. This provides a good platform from which to formulate our proposal.

5. Proposal for your kind consideration:

Our proposal is aimed at an equitable outcome for both the remaining beneficiaries of the DMBT and Denel. Regarding the position of Denel the intention of the proposal is to specifically achieve the result of discharging the post retirement obligation from the service conditions of pensioners that are DMBT beneficiaries resulting in the removal of the obligation from Denel's balance sheet as well as the management and communication burden. It would have similarities to the recent very successful process whereby the old Denel Pension Fund was converted to a defined contribution fund..

The proposal is as follows:

- Nominate a core team comprising of two members of our Forum, two members of the BoT of the DMBT, a representative of Denel HR and the Principle Officer of the DMBT to drive the process;
- The core team, needs to define the terms of reference and reach agreement with Denel and the DMBT BoT thereon;
- Thereafter the core team should embark on a process to investigate and formulate the different options that are possible and available taking into consideration the interest of beneficiaries;
- The core team needs to have an open mind on options. Options may even include retaining a similar structure as the DMBT but without Denel's underlying obligation;
- To achieve the above specialists in this field will be used, including legal advice where required and different financial institutions will be contacted;
- The DMBT BoT and Denel will be approached to approve the final proposal of the core team;

Chairperson: P Botha.

Other Officials: Dr TJ van Reenen, SA Louw, H D du P (Pottie) Potgieter, J Swart, JJ van Rensburg, F Naude, J P van Wyk



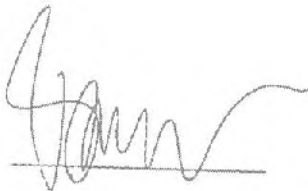
THE DENEL RETIRED EMPLOYEES MEDICAL SCHEME FORUM

- After the above approval the core team will embark on a communication and approval process with beneficiaries. This would include beneficiaries that are active members as well as pensioners;
- After the beneficiary communication and approval process the final implementation process can commence.
- The process should be completed by December 2011 or soon thereafter provided that it is initiated soon.

In conclusion we want to state that we would like to arrive at a situation of gain sharing between Denel and the beneficiaries whereby any surplus funding in the DMBT can be distributed in a fair and equitable way.

We addressed this letter to you with keen intentions to resolve the current matter that has been a burden to Denel and a serious concern and bone of contention to beneficiaries over the past number of years. We would be keen to meet with you to explain our proposal to you should you be able to accommodate it in your busy schedule.

Kind regards,



PAUL BOTHA
CHAIRMAN

Chairperson: P Botha.

Other Officials: Dr TJ van Reenen, SA Louw, H D du P (Pottie) Potgieter, J Swart,
JJ van Rensburg, F Nauda, J P van Wyk





DENEL GROUP

Mr P Botha
Chairperson
The Forum: Denel Retired Employees
Medical Scheme Forum

1 September 2011

Dear Mr Botha

**IMPLEMENTATION OF REVISED MEDICAL CONTRIBUTION SUBSIDY POLICY FOR
PENSIONER BENEFICIARIES ON 1 APRIL 2011**

We refer to your letter dated 5 April 2011 and various telephonic and email correspondence between the undersigned and Mr Pottie Potgieter on this matters.

Denel congratulates the retired pensioners for establishing The Forum. We believe that the Forum will provide, amongst other methods, an appropriate vehicle through which Denel can communicate with pensioners.

We view the matters you raised in a very serious light hence we spent time investigating and considering the proposals you made.

In addressing Part A of the letter, Denel would like to respond as follows:

- With the amalgamation of UMED and Discovery on 1 August 2010, it was necessary that options on Discovery were identified that would most closely match those on UMED. This was an exercise done by the Board of Trustees of UMED prior to the amalgamation (refer to the paragraph 4 of UMED's communiqué addressed to its members dated 1 May 2010 attached hereon as **Annexure A**). The two default options chosen were the **Essential Comprehensive option** to replace the UMED Classic option and the **Keycare Plus** to replace the UMED Value option.
- In the same paragraph, UMED made it clear that Discovery Plans chosen as default options were not identical to UMED's options but were comparable more or less. Therefore, it is not correct to argue now that UMED's benefits and contributions are less than those of Discovery. The rationale for amalgamating the two schemes was precisely because UMED was becoming uncompetitive (i.e. benefits outweighed contributions and the surplus was dwindling at a rapid rate). To illustrate this point, the contribution comparison of UMED's Classic option versus Discovery's Essential Comprehensive option was as follows as at January 2010:

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UMED:	Main Member	Spouse	Child
Classic	2 199	1 842	309
Discovery Health Medical Scheme:			
Essential Comprehensive	1 972	1 865	394

- The suggestion that Denel should annually review the option which is most comparable to UMED'S previous Value and Classic options is not feasible. However, Denel will review from time to time how annual increases on Discovery options are impacting the Trust.
- Forum members should note that members of Discovery can chose whichever option they want. However, the subsidy will remain limited to the two default options mentioned above.

In responding to Part B of your letter, it is important to state the following:

- In amalgamating UMED with Discovery, Denel did not change the subsidy policy. In fact, prior to the road shows taking place, on 19 March 2010, the Board of Trustees of UMED wrote to the Principal Officer of the Denel Medical Benefit Trust (DMBT) asking whether the DMBT subsidy will apply to any option on Discovery. This letter is attached as **Annexure B**. The Principal Officer responded on 29 March 2010 that the subsidy policy will be maintained until otherwise decided. This letter is attached here as **Annexure C**. The UMED Board of Trustees confirmed this to members in paragraph 10 of their communiqué attached hereon as **Annexure D**.
- Based on the above, Denel is keeping to the promise it made to the DMBT members that they would be subsidized on the two UMED options on a Denret 2/3 and Denpen 15% basis. The only difference is that the UMED options have been replaced by the two default options of Discovery that were brought about as a result of the amalgamation between the two schemes.
- Denel has no interest of reducing the subsidy to members. This is evidenced by the payment that Denel made on 22 December 2010 via the DMBT to Discovery to ensure that the amalgamation took place and that members, especially pensioners, are housed in a sound medical scheme.

In responding to Part C of the letter, the following can be said:

- The error that led to over-deductions of members' portions of the contribution by Discovery from 1 August 2010 to April 2011 is one of the teething problems that are experienced in transactions of this nature and is highly regretted. Denel is currently working with the relevant parties, i.e. the DMBT that pays monthly subsidies to Discovery, Alexander Forbes who are the pensioner brokers for Discovery and the Denel Retirement Fund that settles the subsidy on behalf of pensioners to ensure a smooth running of the system going forward.

Denel SOC Ltd, Reg No 1992/001337/07, Nellmapius Drive, Irene
P O Box 8322, Centurion, 0046, South Africa. Tel: +27 (0)12 671 2700, Fax: +27 (0)12 671 2751
Directors: N R Kunene (Chairman), M T Sadik¹ (Group Chief Executive Officer), G Badela, Dr G C Cruywagen,
Ms M J Janse van Rensburg; Prof T Marwala; Ms Z Mathenjwa, F Mhlonlolo¹, N J Motseki, M Msimang, B F Ngwenya, Prof S M Nkomo,
Adv M Ntshikila, Ms B Paleli, M Ratshimbilani, Ms S Sebotsa


¹Executive Director



- Denel will in future endeavour to use appropriate mechanisms to communicate to pensioners and to do so in a timely manner.

We thank you for your suggestions and we look forward to similar fruitful engagements going forward.

Kind regards



Patience Mshungwa
Group Executive: HR and Transformation

cc: Talib Sadik
Group CEO

Themba Zwelibanzi
Group Risk and Compliance Manager





COMMUNIQUÉ 1 MAY 2010

AMALGAMATION OF UMED MEDICAL SCHEME WITH DISCOVERY HEALTH MEDICAL SCHEME

Dear Member

The member communiqué during March 2010 refers.

The purpose of this communiqué is to update members on the positive outcome of the voting process of the proposed amalgamation of Umed with Discovery and to explain the way forward. We want to inform members of their opportunity to choose a Discovery option that suits their needs the best.

The Board of Trustees (Board) of Umed Medical Scheme (Umed) is pleased to announce the positive outcome of the member voting on the amalgamation of Umed with Discovery Health Medical Scheme (Discovery). This will now enable Umed and Discovery to continue with the amalgamation process. The Board's pro-active approach has secured a long term membership, at reasonable cost, to members with a reputable and willing open medical scheme.

1. Result of member voting

The deadline for submitting of votes was 15 April 2010 after which the votes were counted. The auditors of the Scheme, PricewaterhouseCoopers audited the votes and released the results on 20 April 2010. We take this opportunity to sincerely thank all our members who voted. The results are as follows:

- There were 7 909 members in total eligible to vote.
- 4 219 valid member ballots were received (53.3%) and counted.
- 3 690 members did not vote (46.7% of eligible votes).
- 3 927 members voted in favor of an amalgamation (49.7% of total eligible votes and 93.08% of members voted).
- 292 voted against the amalgamation (3.7% of eligible votes).

The actual percentage members that voted and the majority of votes being in favor of the amalgamation are in full compliance to the Rules of Umed and the Council for Medical Schemes for an amalgamation transaction.

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2. Amalgamation

The amalgamation of Umed and Discovery, with the overwhelming support from members who responded by means of a vote, will now go ahead for implementation on 1 July 2010, pending completion of the entire process, approval of the additional funding and final approval by the Council for Medical Schemes and Competition Commission.

The amalgamation means that all members of Umed will be enrolled as members of Discovery from 1 July 2010, while membership of Umed will be terminated on 30 June 2010.

3. Role of brokers in future

Brokers in the open medical scheme environment play an important role in service delivery also to Discovery and members. All members will from the amalgamation date be serviced by a broker appointed by the employers. The respective Human Resources Departments will receive the names of the brokers by the main employers.

4. What are members required to do now?

Members need to decide which Discovery Option they want to be on as from 1 July 2010. Discovery Plans are not identical to the current Options of Umed, but the default options are comparable or more or less the same. Please ensure that you contact Alexander Forbes Health if you have any questions on benefits or contributions offered by any of the Discovery plans.

The contact details for Alexander Forbes are as follows:

Phone Alexander Forbes Health – 011 269 2690 during office hours (7:30 -17:00).

SMS "medical aid" to **31768** (normal sms cell phone rates apply) with your contact telephone or cell number. An Alexander Forbes Health Consultant will then phone you back within 24 hours to assist with any further questions, queries you may have on benefits and or contributions.

E-mail: hccclientservices@aforbes.co.za with your enquiry **OR**

Log onto: <https://extranet.alexanderforbes.com/hcc2010/umed/Main/Default.asp>

You have to **decide by not later than 31 May 2010** whether you **accept the automatic default Discovery Plan** as indicated below or would like to choose another Discovery Plan that suits your specific needs. If you do accept the automatic default Discovery Plan, you do not have to do anything.

Used Classic Option	will automatically default to	Discovery Essential Comprehensive
Used Value Option	will automatically default to	Discovery Key Care Plus

However, if you have studied the Discovery Plans Summary and you consider choosing any one of the other Discovery plans available, you may do so. In this case you must do one of the following:

Armcor Active and Pensioner members – please contact your Human Resources Department and inform them of your selection.

Danel Active members – please contact your Human Resources Department and inform them of your selection.



Denel Pensioners (Retirement and Pension Fund) members – please contact Alexander Forbes Health at the above number to inform them of your selection.

Important: The next opportunity to change plans will be on 1 January 2011.

5. Umed Value Members being defaulted to KeyCare Plus Plan

Members going onto the KeyCare Plan needs to select a doctor per family member and also submit proof of income. If no proof of income is received the members will be placed on the highest income band. If you don't select a GP, you won't be able to access your day-to-day benefits. Please contact the Umed Call centre on 0860 118 633 who will be able to assist you in identifying a GP on the network in your area. The attached document must be completed and returned as stipulated.

6. Rule on studying children – Discovery Plans

On Umed a child dependant who studies full time and provides proof will be covered as a child dependant up to the age of 25. This is different on Discovery all children over the age of 21 will be considered adult dependants and the adult rate will be billed accordingly.

7. Information sessions on the Discovery Benefit Plans/Options

Sessions will be held to explain to members how the Discovery benefit plans work and what is covered/funded on the various plans

For active members information session will be scheduled at the various company sites. Please contact you Human Resources Department for information regarding the sessions.

For the pensioner members as conveyed at the information sessions held during March 2010, the dates and venues for the Benefit Plan information sessions are as follows:

Region	Date	Time	Physical address
Western Cape	21 May	09:30-14:30	Rhein-Metall (old Somchem) Cnr of Reeb and Macassar Road, Macassar
KwaZulu Natal	20 May	09:30-14:30	Riverside Hotel, No. 10 Northway Road, Durban North
Free State	14 May	09:30-14:30	Emoya Estate 8 Franskleinhans Groenvlei Bloemfontein
Centurion	19 May	09:30-14:30	Denel Dynamics (Kentron), Nelmapius Drive, Irene
North West	17 May	09:30-14:30	Potchefstroom Rhein-metall Office (Old Naschem) Carletonville Road opposite Boskopdam
Gauteng	18 May	09:30-14:30	Denel Aviation, Atlas Road, North Campus, Benaro Park, Sabi Hall

As some of the sessions will be held in access-restricted areas, you are also requested to bring your ID document along with you.

8. Questions and Answers

Q What support can I expect once our Scheme amalgamates with Discovery?

Umed's future support role

- The Umed Call Centre (0860 11 86 33) at Discovery will remain open until 31 October 2010 to assist members with final claims for services rendered up to and including 30 June 2010.

Alexander Forbes's future support role

- As required by the Discovery Health Medical Scheme, each Discovery member or employer group must have a broker.
- Denel has decided to appoint Alexander Forbes Health as the Discovery broker for all present Denel pensioners. Alexander Forbes will be sending a letter to all the Denel pensioners clarifying their role and contact details.
- Alexander Forbes and the employers brokers is in the position to resolve any queries you may have. Alexander Forbes Helpline was set up to provide a professional service during the amalgamation process. This service to all Umed members will be discontinued on 30 June 2010.
- You may SMS "medical aid" to 31768 (normal sms cell phone rates apply) and your contact telephone number or cell phone number and send it to 31768. An Alexander Forbes consultant will then phone you back within 24 hours to assist you or
- You may phone Alexander Forbes Health on 011 269 2690 with your query.

Discovery's future support role

- You will be a member of Discovery and will receive all relevant information regarding your new membership directly from Discovery.
- You will receive a new membership number to be used from 1 July 2010. Please inform your service provider of the new number.
- You will have access to the Discovery Call Centre for assistance on 0800 99 88 77 effective 1 July 2010.
- You will have to follow Discovery's rules in terms of obtaining authorizations for operations etc, and adhering to the benefits you are entitled to. It is important that you always ask your doctor and/or healthcare service provider whether they charges the Discovery Scheme Rates or not. This is the only way you will know whether you will have to pay in a difference or not
- You will have access to any other related benefits Discovery has to offer, for example Vitality's gym access benefit, HealthyFood™ discounts at Pick n Pay and other related Vitality benefits.
- You may upgrade your Discovery Plan on 1 January each year and downgrade once during the year.
- The employers will continue to make deductions from a member's monthly salary as before.
- The employers or their funding vehicles will continue to pay over the subsidies on membership fees on behalf of those pensioner members who qualify for a subsidy

Q Where should I submit my claims to after 1 July 2010?

Please continue to submit your (old) claims as usual to Umed for all services provided up to 30 June 2010. You have four months to submit a claim after date of service.

Claims for services provided from 1 July 2010 onwards must be submitted to Discovery and must reflect your new membership number. You can use one of the following options:

- **Fax your claim to 0860 329 252**
- **Email scanned copies to: claims@discovery.co.za** (please include your membership number in the subject line of any email)
- **Post your claim to: Discovery – Claims, P O Box 784262, Sandton, 2146**



- Put your claim in an envelope and drop it in the claim drop-off box at one of the following addresses:
 - 155 West Street, Sandton
 - 2 Frosterly Park, Armstrong Drive, La Lucia Ridge, Umhlanga
 - Discovery Health Building, Century Boulevard, Century City, Cape Town
 - Techno Park, 35 Tegel Avenue, Highgrove Extension 14, Highveld, Centurion
 - Sandton Clinic, Sandton
 - Morningside Clinic, Sandton
 - Park Lane Clinic, Parkhurst
 - Put your claim in an envelope and drop it in one of the boxes available at certain Virgin Active and Planet Fitness gyms
- There are also a number of participating pharmacies and healthcare practitioners who have claim drop-off boxes on their premises for your convenience.

Q Will I have a savings account at Discovery?

Discovery will allocate a six month pro rata savings account (1 July 2010 to December 2010) on 1 July 2010 as you already had six months cover from Umed and you will only be covered for a six month period at Discovery from 1 July 2010

Q When will I get my new Discovery Membership card?

You can expect to receive your new Discovery Membership card towards the end of June 2010.

Q Will I have a new medical aid membership number?

Yes, you will have a new medical scheme membership number. Please inform your doctors and dentists about your new membership number and new medical scheme details.

Q What must I do if my address or any other personal details change before 30 June 2010?

Please phone the Umed Call Centre on 0860 11 86 33 to inform them.

Q Until when will the Umed Call Centre be open?

The Umed Call Centre will be open until 31 October 2010. They will handle queries on claims submitted with a service date up to 30 June 2010.

Q Is any additional cover available for as gap cover?

Medical schemes can in terms of the Medical Schemes Act not give additional cover to members. A product called Admedgap, an insurance product is available from Alexander Forbes as a top-up cover at a rate of R96 per family. Call Alexander Forbes for more information. 011 269 2690

Q When will my new Discovery contribution be deducted from my monthly salary or monthly pension?

The existing deductions will continue as it is at present

Q Where do I have to pay my premiums if I pay by cash?

The Scheme does not accept cash payments. Please make arrangements for a debit order.

Q If paying by debit order would I need to sign a new form?

No, your previous debit order details will be transferred over. If you need to change your details please contact us on 0860 123 077.

Q Where can I view the Exposition Document on the amalgamation of the two schemes? (Objections can be submitted in writing until 31 May 2010).

The Registrar of Medical Schemes

Hadefields,
Block E, 1267 Pretorius Street, Hatfield, Pretoria
Tel: 012 431 0500
Fax: 012 431 0560

Discovery and Umed

Discovery Service Centre,
16 Fredman Drive, Sandton
Tel: 011 529-2888
Fax: 011 539-5503

8. Closing Remarks:

Umed members for a very long time had the benefit of an in-house medical scheme. Unfortunately it is not sustainable anymore. From the many calls and feedback we received to date, we understand that merging Umed with an open Medical Scheme after being in existence for many years will require some adaption by members. Future member support was mentioned as a concern and we refer you to the Questions and Answers section and the future role of the brokers for more details. Many members have indicated that they understand the position and support the pro-active approach the Board has taken to secure a long term membership at reasonable cost to members with a reputable and willing open medical scheme.

Thank you to all our members for the positive approach so far through the process to secure medical care for us all into the future.

Kind regards.



**CHAIRMAN
POTTIE POTGIETER**



**PRINCIPAL OFFICER
FAAN LOUW**

155 West Street, Sandton, PO Box 652506 Benmore, 2010, Emergency 0850 999 911,
Client Services 0860 11 8633 or 082 234 9488;

Fax (011) 539-7275; www.discovery.co.za; cfmcustomer@discovery.co.za

Umed Medical Scheme is governed by a Board of Trustees: Chairperson HD Du P Potgieter, Principal Officer SA Louw.

A list of the other Trustees is available from the Scheme.

Umed Medical Scheme registration number: 1434

Umed Medical Scheme is an authorized Quartz service provider and administers the Umed Medical Scheme.





19 March 2010

Attention: Mr. Jacques van der Merwe
The Principal Officer
Denel Medical Benefit Trust
Private Bag X21
Brooklyn Square 0075

Dear Mr. Van der Merwe

UMED AMALGAMATION WITH DHMS: DMBT SUBSIDY POLICY

Our telephonic conversation earlier today refers.

The Board of Trustees of Umed Medical Scheme ("Umed") approved the amalgamation of the Scheme with Discovery Health Medical Scheme ("DHMS"). The transaction is subject to certain conditions.

We embarked on a communication process with Umed members to inform them about the planned amalgamation and to complete the member voting process. One of the questions that are frequently being asked by pensioner members in particular is how the policy of Denel and the DMBT will be applied when the amalgamation with DHMS is implemented in view of the various options that will become available to members within the DHMS environment.

Due to the different options available the situation will arise where some pensioners choose cheaper and others more expensive options than the current Umed options. The way the policy has been applied the last 10 years or more was that 2/3 (or 15% in the case of Denpen pensioners) of pensioner members contribution to Umed are being subsidised by Denel through the DMBT regardless of which one of the two Umed options were chosen.

Can we assume that the policy would be applied in the same fashion when the amalgamation with DHMS is concluded, it is 2/3 (or 15% in the case of Denpen pensioners) of the contribution, regardless of which DHMS option are chosen?

Your response at your earliest convenience will be appreciated as we need to be able to provide informed answers to the questions asked by pensioner members.

Kind regards,

H D Du P Potgieter

CHAIRPERSON: UMED BOARD OF TRUSTEES.

155 West Street, Sandton; PO Box 652509, Benmore, 2010; Emergency 0860 999 911
Client Services 0860 11 8633 or 082 234 9476.

Fax (011) 539-7276; www.discovery.co.za; service@discovery.co.za

Umed Medical Scheme is governed by a Board of Trustees: Chairperson HD DuP Potgieter; Principal Officer SA Louw
A list of the other Trustees is available from the Scheme



MEDICAL BENEFIT TRUST

Mr HD Du P Potgieter
Chairperson: Umed Board of Trustees
P O Box 652509
BENMORE
2010

29 March 2010

Dear Mr Potgieter

UMED AMALGAMATION: SUBSIDY POLICY OF THE TRUST

I refer to your letter dated 19 March 2010 and wish to confirm that the Trust's current subsidy policy applicable to pensioners (i.e. DENRET 2/3 and DENPEN 15%) will be maintained until otherwise decided.

Kind regards

A handwritten signature in black ink, appearing to read 'P. J. van der Merwe', is written over a light blue horizontal line.

P J VAN DER MERWE
PRINCIPAL OFFICER

Tel: 012 452 7173
Fax: 012 452 7769
E-mail: jaquesvdm@refunds.co.za

U:\Lubber\RIA\Denel Med Benefit Trust\Potgieter- HDDuP 2010 03.doc

A large, stylized handwritten signature in black ink, likely belonging to P J Van der Merwe, is written in the bottom right corner of the page.



Dear Member

PROPOSED AMALGAMATION OF UMED MEDICAL SCHEME WITH DISCOVERY HEALTH MEDICAL SCHEME

1. PURPOSE

The purpose of this letter is to:

- Update the members of Umed Medical Scheme (Umed) on the progress made with the amalgamation process with Discovery Health Medical Scheme (DHMS)
- To inform Umed members about the process and actions the Board of Trustees (Board) and members need to follow to conclude an amalgamation with Discovery Health Medical Scheme. The letter also informs Umed members about the important voting process by members and provides information to ensure a smooth transfer of members from Umed to Discovery Health Medical Scheme.

2. BACKGROUND

In the member communiqués dated 25 May 2009 and 5 October 2009, the strategic options considered by the Board of Umed to ensure long-term sustainability of medical scheme care for members and the process followed were elaborated on. In the 5 October 2009 communiqué we informed members that we made progress in finding a solution to ensure long-term sustainability. Members can refer to these communiqués if necessary.

Members will recall that the demographic profile of Umed with the emphasis on the high average age of the members is the main reason for the deterioration of the financial position of the Scheme. The demographics profile of the Scheme changed over the years as a result of low appointment figures and corporate actions by the Principal Employers. As a result of the changing and diminishing business activities of the main participating employers more younger active members, left employment of the entities and other had to retire before the age of 65. This had a negative impact on the demographics of Umed in total and continuation members in particular and consequently it impacted negatively on the claim patterns of it resulted in the deterioration of the financial position of Umed. Such deterioration can only be countered with higher than market contribution increases or lower benefits which are not in the interest of members. This would discourage younger members with lower claims profile from joining the Scheme and is clearly not a sustainable solution.

Although the financial reserve position, expressed as the solvency ratio of Umed is still better than statutory requirements, the Scheme suffered deficits over the last number of years. This resulted in a deterioration of the solvency ratio at an alarming rate. The deterioration of Umed's financial position over the last two years is evident from salient figures in the financial statements.

A handwritten signature in black ink, located in the bottom right corner of the page.

Continued financial losses are clearly unsustainable and in direct contravention of the Medical Schemes Act, and have continuously weakened the Scheme's solvency margin.

During the budgetary processes for the 2009 and 2010 year, the Board decided to institute rule amendments; firstly, to ensure that no drastic further deterioration of the Scheme's financial position continue, and secondly, to take cognisance of the concerns and needs of members but keep the benefits and contributions within the medical scheme industry norms.

The proposed amalgamation of the Scheme has become inevitable and is a positive step that will serve members' best interests.

Umed is still being managed under strict actuarial supervision; its demographic profile, claim patterns and financial performance are therefore monitored on a monthly basis. The medium-term actuarial projections still indicate that the Scheme will, despite of a 14.5% contribution increase for 2010, no longer be able to meet the minimum statutory solvency requirements (25%) towards end of 2011.

The Board in late 2007 started a process with the objective of amalgamating Umed with a major open medical scheme after following a comprehensive process in terms of which various strategic options were investigated.

The Board considered **five strategic options**:

- Dissolution of the Scheme.
- Conversion to an open Scheme.
- Conversion to a restricted membership scheme.
- Remain as is.
- Amalgamation with an open scheme.

All options were analyzed and evaluated with the assistance of consultants that are experts in this field. After further consultation with the Registrar and on the basis of legal and other expert opinion, the Board came to the conclusion that an orderly amalgamation with a **willing open** medical scheme was the best (only viable) option open to the Scheme. The Board is of the firm opinion that such a solution is in the best interest of both Scheme's members and participating employers. It is also highly preferable to an uncertain and protracted dispute with Authorities and/or recipient schemes under a dissolution scenario. The Board then decided that an amalgamation of the Scheme in terms of section 63 of the Medical Schemes Act is the preferred option to be recommended to Scheme's members for approval.

One of the important criteria in the value system used by the Board was aimed at minimising the negative impact of any changes on members. Discovery Health Medical Scheme was identified as the preferred Scheme to amalgamate with Umed.

The Board conditionally approved the amalgamation in October 2009, as reported in the communiqué of 5 October 2009.

One pre-condition for the amalgamation set by Discovery Health Medical Scheme is that the Principal Employers make cash contributions in addition to the reserves of Umed to partly compensate for the negative age demographic profile. Members will recall from previous communiqués that this was previously a major stumbling block. However, as was reported in the October 2009 communiqué, the revised offer from Discovery Health Medical Scheme required a much more reasonable cash injection. Danel, as the largest principal employer by far, provided Discovery Health Medical Scheme with an undertaking to investigate the funding of their portion of the additional cash injection, subject to final approval.



Following this, the Board of Trustees of Discovery Health Medical Scheme approved the transaction whereby Umed will be incorporated into their open medical aid scheme under specific conditions. Discovery Health Medical Scheme also obtained approval for the transaction from their members on 21 January 2010.

It gives me pleasure to inform members that the Board advanced with the process up to the stage where the statutory voting process of members and other activities determined by Law and/or Scheme rules will be followed.

An amalgamation of Umed and Discovery Health Medical Scheme means that Umed, with all its financial assets and liabilities including its membership, will be carried over and incorporated into the Discovery Health Medical Scheme as from an agreed date. The target date for the transaction is 1 July 2010 subject to receiving the outstanding approvals.

The aim of the amalgamation is to ensure a long-term security and continued medical scheme cover for all Umed members. The Board will ensure that the process for the amalgamation with Discovery Health Medical Scheme is successful.

3. BOARD'S RESPONSIBILITY

The Boards of Umed and Discovery Health Medical Scheme will now proceed with the process by following the prescribed rules in terms of the Medical Schemes Act and the Rules of the two Schemes.

On 21 January 2010 on a Special General Meeting of members of Discovery Health Medical Scheme, members have voted in favour of an amalgamation of Umed with Discovery Health Medical Scheme under specific conditions.

4. MEMBER'S RESPONSIBILITY: VOTING ON THE AMALGAMATION

You must read this communication carefully. Make your opinion heard and please respond to us.

GENERAL INFORMATION

Umed operations in the months of 2010 until date of amalgamation

For the months of January to June 2010, Umed will continue to operate as normal. The 2010 benefits and contributions have already taken effect from 1 January 2010.

When the amalgamation will happen

If the amalgamation is approved by members through the voting process, the Competition Authority and the Council for Medical Schemes, all options, benefits and contributions of the Discovery Health Medical Scheme will then apply from 1 July 2010.

A summary of the Discovery Health Plans and Default Options

We have included a summary of all the Discovery Health Medical Scheme plans so you can compare the benefits that each plan offers and choose the option most suitable to your requirements



It has been agreed that Umed members on the Umed Classic Option will be defaulted to the Essential Comprehensive option of Discovery Health Medical Scheme and the members of Umed on the Value Option will be defaulted to the KeyCare Plus Option of Discovery Health Medical Scheme. That means that the above options will be allocated to members in the event of them not choosing a specific option.

6. MEMBER VOTING

Every Umed member's voice is important. The only way to make yourself heard is to participate in the **VOTING** process – either **in favour of** or **against** the amalgamation with the Discovery Health Medical Scheme. The Board relies on **the willing and active participation of members to VOTE** by no later than **15 April 2010**.

The Ballot paper (Annexure A) is enclosed.

7. WHY IT IS IMPORTANT FOR MEMBERS TO VOTE

Before the amalgamation process can be approved, at least 50% of Umed members are required to participate in the voting process to indicate whether they vote **for** OR **against** a proposed amalgamation.

If the majority of members (at least 50% of the votes) vote **FOR** the change, the amalgamation will continue subject to the approval of the Council for Medical Schemes. We will advise Umed members of what the outcome of the voting process is. If the majority of members (at least 50% of the votes) vote **AGAINST** the change, the amalgamation with Discovery Health Medical Scheme will not continue. This means the Board will have to re-visit the other options stated in our previous communiqués or the Scheme will have to continue with its members financing shortfalls through above market contribution increases in years to come. The latter option will only be possible should the Registrar of Medical Schemes allow Umed to carry on with business under the particular circumstances.

8. HOW TO VOTE

Please complete the enclosed ballot paper and return it to us by using the free post envelope enclosed. You can also return your votes to your relevant HR departments who will then send it to the Scheme's Auditor's.

9. WE WILL LET YOU KNOW WHAT THE OUTCOME IS

As soon as we have counted the votes and completed the auditing process, we will let you know what the outcome of the voting and amalgamation process is.

10. QUESTIONS AND ANSWERS

Why do I have to vote?

The voting process is in terms of Section 63 of the Medical Schemes Act 131 of 1998 (as amended). Herewith the relevant extract:



"The Scheme may, subject to the provisions of section 63 of the Act, amalgamate with, transfer its assets and liabilities to, or take transfer of the assets and liabilities of any other medical scheme or person, in which event the Board shall arrange for all members to decide by ballot whether or not the proposed amalgamation or transfer should proceed."

Who can I contact for more information or support?

For more information as assistance, you can:

Phone Alexander Forbes Helpline – 011 269 2690 during office hours (7:30 -17:00)
SMS "medical aid" to 31768 (at a cost of R1.50) and your contact telephone or cell number. Alexander Forbes will then phone you back within 24 hours to assist with any further questions, queries you may have on benefits and or contributions.

E-mail: hccclientservices@aforbes.co.za with your enquiry **OR**

Log onto: <https://extranet.alexanderforbes.com/hcc2010/umed/Main/Default.asp>

However, if you studied the Discovery Plans Summary and you consider joining any one of the other Discovery plans available you may do so. In this case please contact Alexander Forbes.

When can I change options when I am a member of the Discovery Health Medical Scheme?

You may change to a plan that offers fewer benefits (downgrade) at any time of the year.

If you want to move to a plan that offers more benefits (upgrade) or that does not offer cover in a network or that does not have a deductible or co-payment, you can only do this during the year end revision process. This takes place during the last three months of the year. The new plan choice is effective from 1 January the following year.

What Medical Savings Account amount will I start off with on 1 July 2010?

If you choose a Discovery Health Plan that has a Medical Savings Account you will be allocated a pro-rated amount for the remaining six months of 2010.

What will my company subsidy be if I transfer across to the Discovery Health Medical Scheme?

The subsidy policy at the time of the change over will be as is at the present moment.. The amalgamation merely means that Discovery Health Medical Scheme becomes the scheme of choice in the place of Umed.





11. DISCOVERY HEALTH MEDICAL SCHEME PLANS

Choosing your Discovery Health Medical Scheme plan with effect from 1 July 2010

We have included a summary of the Discovery Health Medical Scheme plans to which members will be defaulted to. The contribution tables show the full 100% contribution payable to the Scheme for each main member, adult or child dependant registered.

Information sessions have been arranged for pensioners for the end of March 2010 and a separate communication have been mailed to all pensioners in this regard. Active members can contact their Human Resources Department for assistance.

We trust you will now be in a position to make an informed decision about your future medical scheme cover for yourself and your dependants.
Kind regards

H D Du P Potgieter
Chairperson: Umed Board of Trustees

S A Louw
Principal Officer

"PB3"

THE DENEL RETIRED EMPLOYEES MEDICAL SCHEME FORUM

17 October 2011

Mr. Talib Sadik
Group Chief Executive Officer
Denel (Pty) Ltd
PO Box 8322
0046 Centurion

Dear Mr Sadik

DENEL POST-RETIREMENT MEDICAL CONTRIBUTION SUBSIDY OBLIGATION

We refer to our letter dated 3 May 2011 addressed to you.

Our letter was intended to propose for your consideration a solution to Denel that would remove the obligation to fund the post-retirement medical contribution subsidy from Denel's balance sheet. The letter was written in a positive spirit aimed at arriving at a mutually beneficial situation to both Denel and the beneficiaries of the Denel Medical Benefit Trust (DMBT), i.e. pensioners and future pensioners.

We were initially encouraged by your prompt acknowledgement of receipt on 5 May 2011, in which we were informed the matter had been referred to Mr Themba Zwellbanzi and Ms Patience Mushungwa, who would respond to us in due course.

The inordinately long delay of five months for a response from the two officials gave cause for concern. Although we finally received a letter from Ms Mushungwa on 23 September 2011, she touched on some of the non-strategic matters we had outlined to her in our letter of 6 April 2011, but failed to address the important issue we had raised with you, besides other key matters we wanted resolved.

In keeping with our original intention to discuss with you on a strategic level, I'll not burden you with operational details. Suffice it to say a measure of mistrust has developed in our interaction and communication with Denel's Human Resources and Transformation (HR) department. This was not helped by an unexpected and unilateral capping of Denel's subsidy contributions, made retroactive, and which resulted in an acrimonious debate among pensioners. Discovery Health's attempts on three occasions to recover so-called "arrears owed" by pensioners, probably at the behest of Denel, caused great anxiety and in some cases real hardship.

We therefore feel obliged to re-engage with you to help resolve the seemingly intractable situation.

At this juncture I want to state unequivocally that our Forum wants to work constructively with Denel, and that we have as much interest as your organisation to preserve the solvency and sustainability of the Denel Medical Benefit Trust (DMBT).

Chairman: PR Botha. Forum officials: Dr TJ van Reenen, SA Louw, HD du P Potgieter,
J Swart, F Naude, JJ van Wyk, T Reuling. Co-opted member: SJ Basch



THE DENEL RETIRED EMPLOYEES MEDICAL SCHEME FORUM

However, it has increasingly become clear that our viewpoint on key issues is not given sufficient credence and that we likewise do not share Denel's assumptions on these issues. Moreover, our request for sufficient information to make informed decisions is ignored.

With that in mind we request your intervention to ensure a more meaningful process with the Denel HR department than the one we've experienced thus far. We attach our latest letter to the Group Executive: Human Resources and Transformation for your background and with a view to enable you to intervene in a meaningful way.

Sadly our mistrust has now spilled over into the sphere of the management of the Trust. We as a Forum are convinced the Trustees of the DMBT often fail to keep the interests of all the beneficiaries in mind when decisions are taken. The Trustees have on occasion shown a distinct lack of understanding or were not properly informed when dealing with the medical scheme benefits - perhaps because they are not in a position to do so.

We believe this lack of trust and the lack of information could be addressed simultaneously by giving the Forum direct representation on the DMBT Board of Trustees. Surely we as beneficiaries of the DMBT have a very pertinent interest in its management and good fortunes. It would also be in line with generally accepted corporate governance principles. At the risk of repeating myself: we take a responsible view to preserve the long-term funding levels and the integrity of the Trust.

Therefore we kindly request your urgent attention to giving our Forum direct representation on the DMBT to enhance communication and to provide input on pensioner beneficiary interest in a constructive way.

We reiterate our offer to jointly work together to find mutually beneficial solutions to the different issues we face.

Kind regards,

PAUL BOTHA
CHAIRMAN

Chairman: PR Botha. Forum officials: Dr TJ van Reenen, SA Louw, H D du P Potgieter,
J Swart, F Naude, JJ van Wyk, T Reuling. Co-opted member: SJ Basch



“PB4”

**THE DENEL RETIRED EMPLOYEES²⁴ MEDICAL SCHEME
FORUM**

23 November 2011

Mr. Talib Sadik
Group Chief Executive Officer
Denel (Pty) Ltd

By email

Dear Mr Sadik

DENEL RETIRED EMPLOYEES MEDICAL SCHEME FORUM

It is a matter of grave concern that our letters of 17 October 2011 addressed to both yourself and Denel's Group Executive: HR and Transformation have gone unanswered.

We have not even had the courtesy of an acknowledgement of receipt.

In our last letter to you, I pointed out that a measure of distrust existed with the Group Executive HR, and requested your intervention to resolve the issues we have raised in the past. These issues impact negatively on many of our members on a daily basis.

At the same time we requested direct representation on the DMBT Board of Trustees in light of our very real and pertinent interest in the Trust's management and financial status. This would align with accepted corporate governance principles and ensure pensioner beneficiary interests are constructively maintained.

I trust you will attend to these matters at your earliest convenience and hope to receive a suitable reply from you shortly.

Yours sincerely



**PAUL BOTHA
CHAIRMAN**

Chairman: PR Botha. Forum officials: Dr TJ van Reenen, SA Louw, H D du P Potgieter, J Swart, F Naude, JJ van Wyk, T Reuling. Co-opted member: SJ Basch



D E N E L

DENEL GROUP

Tel: +27 12 671 2899
Fax: +27 12 671 2786
Email: thembax@denel.co.za
Ref: Ltr/MrBotha/9Mar12

9 March 2012

Mr P Botha
Chairman
The Forum Denel Retired Employees
Medical Scheme Forum

Dear Mr Botha

DENEL RETIRED EMPLOYEES MEDICAL SCHEME FORUM

With reference to your letter dated 27 January 2012 and my subsequent response in a letter dated 5 February 2012, thank you for acceding me time to familiarise myself with the matter at hand.

I have been briefed on the nature and the objective of the Denel Medical Benefit Trust (DMBT) and specifically that it was formed to manage the funds set aside by Denel to meet Denel's post-employment medical subsidies obligation in respect of certain beneficiaries. The liability for any shortfall in DMBT is solely that of Denel.

According to information at my disposal, the board of Umed consulted members of the scheme regarding the amalgamation and championed the process to its completion with the advice of experts. The board consulted members in a number of ways and members voted on the process to enable the board to proceed with the amalgamation. In light of the above I respond to your proposal as follows:

1. Direct representation on the Board of Trustees of the DMBT

DMBT is a discretionary Trust and unlike a pension or provident fund where the employer and employees jointly contribute to the fund, employees did not contribute to the trust, making Denel solely liable for funding any deficit that could occur on the trust. Therefore, there is no requirement for employee representation or appointment of additional members on the board of Trustees of the DMBT.

2. Insight into DMBT financial statements

The trust is Denel's vehicle to meet its obligation regarding the post-employment medical subsidies. The liability for post-employment medical subsidy lies with Denel and not the trust. Suffice to say that Denel is satisfied that the Trust is in a financially sound position to meet its obligation. Denel further receives assurance from its auditors regarding its obligation that is funded through the trust. I want to assure you that there are no concerns regarding Denel's ability to meet its obligation in this regard.

Denel believes that above is sufficient assurance that it will meet its post-employment medical obligation.

3. Insight into actuarial report on the DMBT's current funding levels

The actuarial report is an internal document used to monitor Denel's liability and contains privileged information. Therefore, it will not be prudent to provide it to any third party.

4. Reversal of Denel's unilateral cap on the subsidisation of child dependants who are full time students and handicapped children

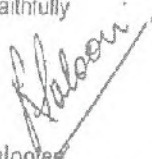
I have gathered that Denel has not made unilateral changes to the subsidy scheme but applies the policy within the prevailing rules applicable to Discovery. Denel pays the subsidies in proportion to the premium paid by a member and subsidies are capped at the Essential Comprehensive option. The amalgamation of Umed was concluded by the Board of Umed in consultation with members and it would not be prudent for Denel to enter into new negotiations post the amalgamation.

5. Details of Denel's actuarial investigation on the impact of the higher subsidy option

Any investigation conducted by Denel in this regard to assess its exposure is privileged information and is for the sole use of Denel. I have been advised that Denel has no intention to pay subsidies on options higher than the Essential Comprehensive. Therefore, information relating to affordability to pay subsidies on higher options is not relevant in this regard.

Considering that there has been a series of interactions between you and Denel pertaining to the abovementioned issues in the past, I hope that my response concludes the matter.

Yours faithfully



Riaz Saloojee
GROUP CHIEF EXECUTIVE OFFICER

cc: M Ngidi - Acting Group Executive HR & Transformation



**THE DENEL RETIRED EMPLOYEES
MEDICAL SCHEME FORUM**

MEETING OF FORUM OFFICIALS ON 22 NOVEMBER 2012

1. Purpose of the meeting.
2. Feedback on meeting between PP and Themba Zwelibanzi and Mike Ngidi from Denel on 16 November 2012.
3. Objectives of Denel with remaining post retirement obligation:
 - 3.1. To get rid of the obligation on its balance sheet
 - 3.2. To access the surplus in the DMBT
 - 3.3. To demonstrate progress at financial year-end (31 March 2013).
4. Opinion expressed by/position of the two officials:
 - 4.1. They realize the benefit of cooperating with an organised group like the Forum;
 - 4.2. They realize that the representatives from the Forum need to be involved at an early stage of the process;
 - 4.3. They did not disagree when it was put to them that somebody independent needed to facilitate exploring of new options;
 - 4.4. They agreed that a formal process such as the recent Densup process needs to be followed;
 - 4.5. First meeting with Forum representatives scheduled for 5 December 2012.
5. Proposal to Forum:
 - 5.1. Two delegates to represent the Forum in the early stages of the process,
 - 5.2. Review representation continually;
 - 5.3. Feedback to Forum officials after each meeting with Denel or when key findings are arrived at.
 - 5.4. Broad mandate that needs to be reviewed at regular intervals.
6. Proposed mandate:

To cooperate with Denel representatives towards a position of redeeming of the Denel obligation towards beneficiaries on the basis of:

 - Fair and equitable situation (gain sharing)
 - Investigation into alternative solutions needs to be done by an independent competent skilled person (eg, Anthony Lester from Towers Watson)
 - Process to allow for regular consultation with beneficiaries
 - Resources need to be available for the above
7. Resolutions by Forum Officials:
 - 7.1. Nomination of delegates;
 - 7.2. Approval of Mandate
8. Communication:
 - 8.1. With Western Cape and other involved beneficiaries (when and by whom?),
 - 8.2. With Forum members (Propose that it be synchronized with the Denel interaction)
9. Other Matters:
 - 9.1. .
 - 9.2. .



"PB7"

From: Paul Botha <paultjie@gmail.com>
Sent: 05 December 2012 03:47 PM
To: Potgieter, Pottie; Faan Louw; Sam J Basch; Tommy van Reenen; Swart Kobus;
ziervogelnaude@mweb.co.za
Subject: Gesprek Denel

Middag Julle

Pottie en ek het die gesprek met Themba en Mike gevoer. Dit het baie positief verloop en Hulle twee is verbind tot n gesamentlike proses met ons om oplossings te ontwikkel. Hulle beseft dat net n verdere uitkoopaksie nie sal werk nie

Die beginsel op ooreengekom is dat daar n "gainshare" vir Denel en ons lede moet wees. Die detail sal later met behulp van n konsultant in die vorm van verskillende moontlike opsies voorgelê word

Die konsultant deur Pottie voorgestel is Anthony Lester. Hulle sal hom ondersoek

Pottie sal n konsep opdrag aan die konsultant vir Themba opstel

Pottie sal met die Kaapse groep praat en hul inlig en hoor waar hulle staan

Themba sou graag gerusgestel word oor ons ledelede en of daar ander groepe is wat sou aanspraak maak dat hul of deel van so n proses moet wees of dat hulle soortgelyke inspraak sou wou he

Denel wil vinnig beweeg


n Opvolggesprek sal gereel word vir Januarie na almal terug is van vakansie. Voorlopig sal die twee van hulle en Pottie en ek die "Komitee" vorm

Lede sal in kennis gestel word van die aanvang van en later die verloop van die proses. Hiervoor sal ons waarskynlik na n "roadshow" of twee kyk

Die proses se kostes behoort nie hoog te wees nie en Themba sal met Jacques bevestig dat die Trust daarvoor instaan

Groete

Paul



“PB8”

From: Rene Potgieter <potties@iafrica.com>
Sent: 12 January 2013 10:02 AM
To: potties@iafrica.com
Subject: FW: DMBT-Matters
Attachments: Scope of work-Advisor.docx

From: Themba B. Zwelibanzi [mailto:thembaz@denel.co.za]
Sent: 11 January 2013 04:13 PM
To: potties@iafrica.com
Cc: paultjie@gmail.com; Michael Ngidi
Subject: FW: DMBT-Matters

Dear Pottie

Complements of the season.

We only returned from leave on 9 January 2013. Just to keep you up to date: Mike is working on the matter and will get back to you in due course.

Regards

From: Potgieter, Pottie [mailto:Pottie.Potgieter@bigenafrica.com]
Sent: 07 January 2013 03:04 PM
To: Themba B. Zwelibanzi; Michael Ngidi (Mike.Ngidi@deneldynamics.co.za)
Cc: Paul Botha (paultjie@gmail.com)
Subject: DMBT-Matters

Dear Mike and Themba,



Trust you had a wonderful festive season. May you experience joy and peace in 2013.

Thank you for the very constructive meeting early in December 2012.

Unfortunately I had a lot of other commitments to attend to before the start of my leave period and hence did not complete the draft SOW for the proposed advisor on the date as promised. However, please find the draft attached hereto.

As far as the mandate given by our Forum management group is concerned, I promised to provide you the wording electronically. It reads as follows:

"6. Proposed mandate:

To cooperate with Denel representatives towards a position of redeeming of the Denel obligation towards beneficiaries on the basis of:

- Fair and equitable situation (gain sharing)
- Investigation into alternative solutions needs to be done by an independent competent skilled person (eg. Anthony Lester from Towers Watson)
- Process to allow for regular consultation with beneficiaries
- Resources need to be available for the above"

Kind regards,

Pottie Potgieter

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Matthew Scorgie

From: Sam J Basch <sam@koisan.co.za>
Sent: 07 August 2013 08:25 AM
To: Paul Botha (paultjie@gmail.com)
Cc: Swart Kobus; Faan Louw (saamslouw@iburst.co.za); Freek Naude (ziervogelnaude@mweb.co.za); Tommy Van Reenen; Jacob van Wyk (vanwykj@iafrica.com); Brian Tucker; Potgieter, Pottie
Subject: DMBT

Goeie dag

Pottie Potgieter en ekself, Sam Basch, het as Forum-bestuursverteenwoordigers op Maandag, 5 Augustus 2013 met Denel gesprek gevoer. Van Denel se kant was aanvanklik Themba Zwelibanze, Gawie van Zyl en Ayanda Mkatini teenwoordig (laasgenoemde van die 'Human Resources'-afdeling wat nou onder bestuur van Natasha Davis staan). Fikile Mhlonlo, die CFO, het heelwat later aangesluit, en onmiddellik pertinent die dringendheid van die saak beklemtoon.

Denel het 'n sogenaamde vars opsie op die tafel gesit, wat neerkom op 'n hoër annuïteitbetaling vir die eerste 10 jaar maar met 'n mindere waarborg daarna. Die koste vir Denel is dieselfde as die huidige Momentum-opsie. In wese is daar dus nie veel verskil van die vorige uitkoopopsie nie, behalwe dat beide op huidige tariewe gebaseer is. Hulle standpunt, soos deur Themba verduidelik, is dat Denel om twee redes nie ver buite die raamwerk van die vorige opsie kan beweeg nie. Eerstens het SARS die bedeling goedgekeur en tweedens kan Denel kritiek op die lyf loop as 'n omvangryker opsie as die voriges aan lede aangebied word.

Dit is duidelik aan Denel gestel dat hulle "twee" opsies nie entoesiasies ontvang sal word nie. Ons het toe die opsie van oornome van die Trust met afteken van die Denel-waorborg in terme van die diensvoorwaardes op die tafel gesit.

Denel het kennis geneem van ons voorstel vir hierdie alternatiewe opsie. Hulle het toe die punt gemaak dat 'n wesenlike deel van die surplus toegeskryf kan word aan die effektiewe uitkoopaksies wat reeds uitgevoer is en dat daardie gedeelte van die surplus Denel toekom. Ons reaksie was dat 'n aktuaris die somme moet maak sodat ons dit kan evalueer.

Naas Denel se twee opsies, sal hierdie 3de opsie intern oorweeg word, en die Forum behoort binne die volgende twee weke 'n antwoord van Denel te ontvang.

Indien die Forum se Opsie 3 deur Denel as 'n alternatief aanvaar word, sal die proses vorentoe bepaal word. Dit sal 'n 'Road show' insluit om die 3 voorstelle aan lede voor te hou.

Ons sien dit as 'n positiewe verwikkeling wat hopelik binne die kalenderjaar konseptueel gefinaliseer kan word.

Beste groete

Sam J Basch
sam@koisan.co.za
(+27) 82 881 3696



"PB10"

From: Themba B. Zwelibanzi <thembaz@denel.co.za>
Sent: 11 June 2014 03:27 PM
To: Pottie.Potgieter@bigenafrica.com
Cc: Fikile Mhlontlo; Natasha Davies; Gawie Van Zyl; Ayanda Mkatini; paultjie@gmail.com
Subject: FW: Denel medical post retirement

Dear Pottie,

Thanks for the update and pointing out issues that have not been addressed in my email. Our focus was on providing the information required and not a record of the discussions. Denel's response to the questions is as follows:

1. The appointment of a suitably qualified impartial person to assist us all with the process

We understand the importance of the matter and trust that at our next meeting where we will discuss your response regarding the list of assumptions forwarded to you, we will discuss the matter in relation to specific terms of reference.

2. How we plan to deal with those who did not react to the choices of alternative benefits offered

Our intention is to start interacting on default along the current process as discussions on the Trust should give us a leverage in this regard as the Trust was not indicated as a default option in our communication regarding the offer. This will therefore take time.

In light of a number of activities lined up for us, we have prioritised this process as critical and urgent and would like to finalise a programme of action, which is dependent on our next meeting. It would be appreciated if you could give us an indication as to when we should plan for our next meeting. This is very important to ensure that people who are critical for the process from our side are there.

Kind regards
Themba

From: Potgieter, Pottie [mailto:Pottie.Potgieter@bigenafrica.com]
Sent: 11 June 2014 07:00 AM
To: Themba B. Zwelibanzi
Cc: Paul Botha (paultjie@gmail.com)
Subject: Denel medical post retirement

Dear Themba

Thank you for your e-mail and the names and basis for calculation attached thereto as well as your phone call yesterday

At our meeting held at your offices on 27 May 2014 we pointed out that we feel it is necessary to formally obtain a mandate from those who support the Trust option in order to proceed. This would also entail the election of a new management for the Forum representative of those who chose the Trust option. (we believe we will be able to ensure continuity which we know is a concern to you.) Now that we have the names we are attending to this. We have a meeting this afternoon and will discuss the insistence of Denel-Rheinmetall regarding representation)

The new management could then respond to your request for a reaction to your e-mail and the information supplied

In your e-mail you make no mention of two points we covered at the meeting

1. The appointment of a suitably qualified impartial person to assist us all with the process and
2. How you plan to deal with those who did not react to the choices of alternative benefits offered (At the meeting you indicated they would be defaulted to the Trust option)

Although the above may take some time we feel it is essential for all concerned to be able to handle the



process in a professional way that would reduce any later liability risks to individuals involved in the process.

We would appreciate your response on the abovementioned points.

Kind regards

H. D. du P. (Pottie) Potgieter
Bigen Africa Services (Pty) Ltd
Tel: +27 (0)12 843 9036
Fax: +27 (0)12 842 8850
Mobile: +27 (0) 83 675 1338
Pottie.potgieter@bignafrica.com
Physical Address:
Allan Cormack Str
The Innovation Hub
Persequor, Pretoria
Postal Address:
PO Box 29
The Innovation Hub
Pretoria, 0087

Please consider the
environment before
printing this email

A handwritten signature in black ink, appearing to be 'H. D. du P. (Pottie) Potgieter', located in the bottom right corner of the page.

"PB11"

DENEL MEDICAL BENEFIT TRUST

SCOPE OF WORK IN REDEEMING DENEL OBLIGATION/REACHING AGREEMENT WITH REMAINING BENEFICIARIES

1. Background

Denel has an obligation that arose from employment contracts signed before 1 April 2000 for qualifying retired employees, to pay a monthly medical subsidy of 2/3rds for retired employees who were/are Denel Retirement Fund (Denret) members and 15% for (Denel Pension Fund (Denpen) in respect of their membership contributions to an employer prescribed medical scheme (currently Discovery Health Medical Scheme). The subsidy for dependent children is paid until the age of 21 or up to 25 for dependent students. Spouses and children with disabilities are subsidized for the rest of their lives after the death of the principal member.

This obligation is fully funded by the employer through funds deposited over time and housed in a trust, Denel Medical Benefit Trust, and is governed through a Trust Deed. The Trust is managed by employer appointed trustees who prepare annual actuarial reports to monitor trust activities and prepare annual financial statements. The current funding level of the trust is sufficient to pay the obligation without Denel having to pay any additional funds.

On 18 September 2006, the Denel Board resolved that the open-ended liability risk relating to this scheme be terminated and Denel opted to make voluntary alternative settlement offers to qualifying members as follows:

- (a) Transferring the benefits of active employee beneficiaries who accepted the offer to Denret;
- (b) Paying the benefits for non-Denel Retirement Fund members accepting the offer in cash; and
- (c) Purchasing annuities for pensioner beneficiaries accepting the offer.

Originally there were 5 486 (2 772 pensioners plus 2 714 actives employees) qualifying members and to date

To date 82% or 4468 of the beneficiaries accepted Denel's offer. Of the remaining members 461 indicated preferences for an Employee-only managed Trust and about 557 either did not respond or did not accept the offer. Denel's intentions are to default the remaining beneficiaries to either Denret for active members or CPI annuity for pensioners. However, it is desirable that they are defaulted to an Employee only managed Trust.

2. Termination of the obligation

Denel would like to terminate this obligation equitably based on sound and fair assumptions commensurate to the risk and profile of the beneficiaries. Denel seeks an outcome that would be acceptable to the majority of the remaining members which will:



- a) Remove the subsidy obligation and administrative burden from Denel while
- b) Ensure the Employee Beneficiaries are not prejudiced

3. Terms of reference

Representatives of the remaining beneficiaries and Denel have been in discussions regarding the best way to exit the current arrangement. There is a common position that this arrangement should be exited and the interests of both Denel and the beneficiaries are served. Amongst others it is necessary that the parties should have a common understanding of the assumptions used to calculate the current settlement offer and the implications thereon. Consequently the representatives of the beneficiaries have requested the appointment of an expert, independent from those used by Denel, to act as an advisor to the parties in the process. This is viewed as critical considering that the trust is becoming a member-only trust. Thus the expert is required to:

- (a) Advise on reasonable assumptions to be used to calculate the settlement offer considering the existing rights and position of the remaining beneficiaries that would include inter alia:
 - (i) Investment return in excess of medical inflation;
 - (ii) Medical inflation in excess of CPI;
 - (iii) Mortality post-retirement;
 - (iv) Marital status assumption;
 - (v) CPI; and
 - (vi) Sweetener in view of the guarantee of Denel being removed (no more liability).
 - (vii) Current tax position regarding contributions
 - (viii) Existing security position of beneficiaries
 - (ix) Longevity risk
- (b) Provide guidance on the best possible way of structuring the benefits
- (c) Provide input regarding legal documentation for final agreed upon solution(s).
- (d) Provide input on the structuring of the trust and investment policy

4. LIMITATIONS

This appointment is limited to the activities articulated in 3 above and the expert will report to the representatives of the beneficiaries and Denel.

5. ACCEPTANCE OF SCOPE

On behalf of Denel



Full names Signature

Date

On behalf of employee beneficiaries.....

Full names Signature.....

Date.....

A handwritten signature in black ink, located in the bottom right corner of the page. The signature is stylized and appears to consist of several overlapping loops and lines.

Memo

Date: 31 October 2014

To: Denel Retired Members Medical Aid Forum

From: Ant Lester and Maretha de Kock

Subject: Terms of reference

Dear
Forum
members

In our view it is essential that Towers Watson gets our terms of reference agreed at the outset and the purpose of this note is to set out our understanding of these terms.

Towers Watson is to act as an independent expert to the Forum without favour to either Denel or the members. As such we will provide all correspondence to both parties and will not meet with either party without the consent of the other party. In reality we would strongly prefer to attend meetings of the Forum where both Parties are present.

Our understanding is that Towers Watson must advise the Forum on the amount of money that should be retained in the Trust (or its successor-in-title) in order to *reasonably and fairly secure the existing rights of members*. Specifically, the word "reasonably" means that there is high probability (estimated at around 70% to 80%) that the amount we suggest will be sufficient to cover the existing rights of members but we cannot guarantee that it will be sufficient.

There are definitely possible future scenarios where the amount we propose will not be sufficient (e.g. if medical inflation is 6% p.a. higher than normal inflation over the long term, medical advances improve the life expectancy of pensioners by 30%, changes in the tax dispensation etc.) and hence the need for the parties to agree that the amount is a reasonable one and not one that guarantees the existing rights of members.

It is also important to define what the existing rights of members are. In their correspondence the member group indicate the following:

- The Denel subsidy is for the member, spouse and dependent children – we understand this to mean that there is no subsidy for any other dependents. It is important that parties agree what constitutes a dependent child – for example, a child aged 30 that stays at home and who does not have a job is presumably not eligible to be counted as a dependent.
- Denel has undertaken to increase the subsidy annually in line with the contribution increase of the Discovery Health Essential Comprehensive Plan. The members have suggested that the subsidy should possibly be based on the Classic Comprehensive option. The benefit option on which the subsidy is based is a matter that runs to the heart of what the implied contract between the parties is and if there is a dispute here it would need to be dealt with by a labour lawyer

We will not be able to determine the suggested quantum of the Trust assets unless the two Parties agree on which benefit plan such amount should be determined or indeed whether this plan could be varied in future. Our strong preference would be to get this issue resolved at the outset as this allows us to make a firm recommendation. Alternatively we could do the calculations on both bases, but this approach runs



the risk that the applicable benefit option becomes the dispute point rather than the quantum that should be retained in the Trust.

We also need confirmation that Denel is also of the view that they have given a firm undertaking to increase the subsidy each year in line with the increase in the Discovery Health Essential Comprehensive Plan (or the Classic Comprehensive Plan if they have so agreed).

- The subsidy paid from the Denel Medical Benefit Trust is currently not taxable in the hands of the beneficiary based on a tax directive provided by SARS. This is a tax issue and will only apply for as long as the current legislation remains. It is possible that tax legislation could change in future and our suggested quantum of the Trust could not reasonably allow for such changes as it would be speculative to contemplate the nature of such changes.

In summary we need both Parties to confirm the following

- Towers Watson will propose the amount of money that should be retained in the Trust (or its successor-in-title) in order to *reasonably and fairly secure the existing rights of members*. Specifically, the word "reasonably" means that there is high probability, estimated at around 70% to 80% that the amount we suggest will be sufficient.
- Members are only entitled to a subsidy in respect of the former Denel employee, his or her spouse and dependent children. We suggest that a dependent child be defined as a child under the age of 18 or in the case of full time study up to the age of 24 or a child that is disabled to such an extent that they will always be dependent.
- The amount that should be retained in the Trust should be based on the Discovery Health Essential Comprehensive Plan or the Classic Comprehensive Plan as the Parties instruct. Alternatively we can do the calculations on both plans but this is not our recommended route.
- Denel should confirm that they have accepted their obligation to increase the subsidy each year in line with the increase in the Discovery Health Essential Comprehensive Plan (or the Classic Comprehensive Plan if so agreed). If Denel has a different view of their undertaking this should be set out and the Parties would need to agree on what Denel's obligation is before we do the calculations.
- Our calculation will be based on the assumption that the current tax dispensation remains in place. Another way of stating the above is that Denel has not provided any undertaking that the subsidy will be tax-free and if the law changes in future to make the subsidy taxable this will be for the member's account

We would appreciate written confirmation from the Forum that we can proceed on the basis set out above with specific guidance on whether the calculated amount for the Trust should be based on the Essential Comprehensive Plan or the Classic Comprehensive Plan (or both bases are required).



We really look forward to working with the Forum. Given the nature of the mandate we believe it is important to disclose that Ant Lester no longer works as an actuary. Although Ant qualified as an actuary in 1989 and worked in the actuarial industry until three years ago, he now focuses on investment consulting work. Ant is comfortable that he has the necessary expertise and experience to advise the Forum on this matter, but it is important that the parties are aware of his position.

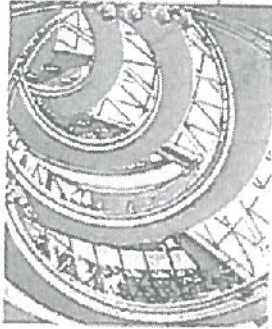
To the extent that any of the work requires actuarial calculations Towers Watson will ensure that this work is reviewed and signed off by one of its senior practising actuaries.

A handwritten signature in black ink, appearing to be 'Ant Lester', located in the bottom right corner of the page.

"PB13"

- In front below
- R 267. + 5?

3/12/2016



Denel Medical Benefit Trust

Securing post-retirement
medical aid subsidies

November 2014

Ant Sester
 Munters de Groot
 Paul Bollen
 P. de
 Thema Grootenboer
 Grooten
 Grooten
 Grooten
 Natasha

Fikale

Zoo Justice Optima

TOWERS WATSON

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Section 1: Introduction

Towers Watson has been appointed by the Denel Retired Employees Medical Forum to provide an expert opinion on the quantum of the assets that should be retained in the Denel Medical Benefit Trust to meet its future obligation of subsidising the medical aid contributions of the Trust membership. Hereafter the quantum so calculated is referred to as the "Initial Amount".

As an expert advisor we provide this advice to the Forum without favour to any party. Accordingly, we express an opinion as to the Initial Amount we believe fair to all stakeholders that should either be retained in the Trust or transferred to a new Trust.

Please note that any reference to Denel means Denel and its associated or subsidiary companies.

Disclaimer

Towers Watson has prepared this report for the Denel Retired Employees Medical Forum solely for their use, for the specific purpose indicated.

The calculations shown in this report are based on a set of assumptions chosen from a reasonable range. Any changes to any of the assumptions used would influence the results. The assumptions have been derived by Towers Watson through a blend of economic theory and historical analysis. They inevitably contain an element of subjective judgement. It should be noted that no set of assumptions could be expected to perfectly capture future uncertainty, particularly the risk of extreme events.

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Section 2: Background information

Categories of members

There are three categories of members that remain members of the Trust, namely:

- Members that did not return an option form (no response members)
- Members that elected that the status quo continue
- Members that elected that a new Trust be established offering members the same benefits as the existing Trust, but with Denel no longer participating in the Trust

The table below shows the key statistics in relation to the three categories:

Category	In-service members	Pensioners
New Trust		
Number of members	137	328
Average age	58 years, 7 months	68 years, 9 months
No response		
Number of members	11	418
Average age	53 years, 11 months	69 years, 5 months
Status quo		
Number of members	26	30
Average age	56 years, 9 months	69 years, 5 months

We have performed the calculations separately for the "New Trust" members only and for the total remaining membership.

Handwritten notes: 174, 776, 995, 557, 568

Data

The data used in the calculations was supplied by Momentum. We have accepted the static data (i.e. the member's date of birth, spouse's date of birth, gender and percentage subsidy) as correct. For some members the Rand amount of the subsidy supplied was higher than that implied by the percentage subsidy. In these cases we assumed the percentage subsidy to be correct and adjusted the Rand amount subsidy downwards.

We would advise that if an Initial Amount is agreed, the correctness of the associated member data be verified at the time

Handwritten signature

Subsidy policy

Based on the data supplied it is clear that the current subsidy policy is based on the contributions paid to the Discovery Health Essential Comprehensive option (including the full contribution to the medical savings account).

For most members the subsidy is $2/3^{\text{rd}}$ of the above contribution although there are a few members receiving a lower subsidy of 15%. Members also have the option to choose a cheaper medical aid option and in this case the subsidy is based on the lower contribution rate.


The employee constituency of the Forum believes that there is a case that the subsidy should be based on the Discovery Health Classic Comprehensive option, but the parties have agreed that Towers Watson do their calculations based on the Essential Comprehensive option.



Section 3: Basis of calculation

Assumptions required

In order to determine the Initial Amount in relation to a subsidy policy based on the Discovery Health Essential Comprehensive Plan the most important assumptions ranked more or less in order from most important to least important are:

- Medical aid inflation
- The level of investment returns
- The longevity of the members and their dependents 
- The rate at which in-service members will retire on the basis of ill-health, early retirement and on reaching normal retirement age; this rate would be affected by any retrenchment programme Denel may implement over the next few years
- The dependency status of members in-service, at retirement and in retirement
- The mortality and resignation rate of members in service
- The rate at which members may resign from the Trust (and in so doing forfeit their subsidy) simply because they cannot afford their share of the medical aid contribution. Alternatively members may elect a cheaper benefit option than the Essential Comprehensive Plan
- The level of future expenses that the Trust should provide for.

It is useful to think of the assumptions as a budget of what may reasonably be expected in the future. Inevitably the actual experience will differ from that budgeted for but the parties need to be comfortable that the proposed is both fair and reasonable.

Principles used in setting the basis

Setting of the above assumptions is far more difficult than would be the case if Denel were to underwrite the benefits. The central difference is, of course, that the Trust *would not be able to rely on any employer support* if its actual experience were worse from that budgeted for. Absent Denel, in the case of a future adverse scenario, the only remedy that the Trust would have would be to reduce the subsidy.

The above argues that the assumptions used for determining the Initial Amount should be set conservatively, but there is a limit as to the degree of conservatism that can be adopted. As the assumptions become more conservative the fair criticism becomes "you are speculating and bring in with certainty scenarios that in practice only have a very small chance of happening and if these events do not arise then the Initial Amount is much too high".



Our assumptions do take into account the fact that there is no employer support for the Trust. However, we strongly emphasise that our calculated Initial Amount will not be sufficient to maintain the current subsidy under all scenarios. Listed below for illustrative purposes are two scenarios under which the Initial Amount almost certainly would not be sufficient to maintain the existing subsidy policy:

- If Denel were to implement a retrenchment scheme early next year in terms of which all in-service members aged 50 and older could early retire immediately with the 2/3rd medical aid subsidy.
- A development of medical science over the next ten years that increases the life expectancy of members by five years.

There are, of course, many other scenarios under which the Initial Amount will be insufficient such a partial government default on its inflation linked debt and medical inflation being much higher than budgeted for.

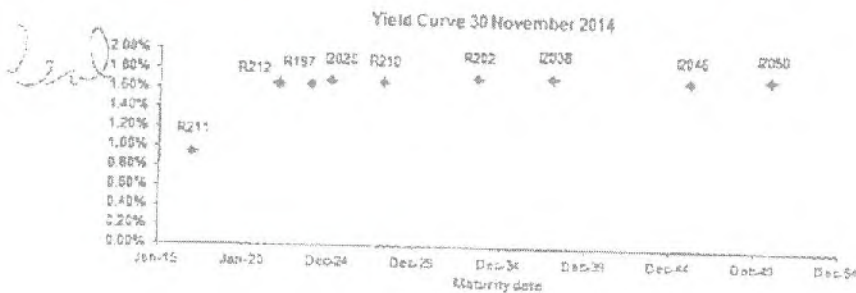
We highlight that if members elect to join the new trust they must do so on the clear understanding that there is a possibility that their subsidy can be reduced; of course in the event of good outcomes (i.e. the actual experience is better than budget) the subsidy could be increased.

The final point we make is that the proposed Initial Amount should proxy the market competitive price a third party would charge for taking over the liability. There is unfortunately not a competitive market for the buy-out of post-retirement medical aid obligations, but where possible we have used market pricing.

Investment return assumption

In order to meet its obligation to members with a very high degree of certainty, the Trust should structure its assets to meet the nature and term of its liabilities with minimal investment risk. The ideal asset class, if it existed, would be a government issued *medical inflation linked bond* – of course there is no such instrument, but the government does issue inflation linked bonds.

The chart below shows the term structure of the yield to maturity of such inflation linked bonds (abbreviated to ILB) as at 30 November 2014 – at the longest duration ILB's offer a real return of just below to 1.8% p.a.




Importantly there is no need to assume the future level of investment return – one can get this directly from the market pricing of ILBs.

However, in order to match the liabilities more closely one needs a more complete universe of ILB's by duration. The Bond Exchange of South Africa has constructed an ILB yield curve which proxies at real return at each duration using the government issued ILB's as the reference point and so it is possible to discount the monthly future post-retirement medical aid subsidy amounts at the appropriate yield to maturity.

In doing so one needs to reduce the yield slightly to allow for the slight mismatch arising from having to use the ILBs in issue, implementation risk and investment manager fees. Our estimate of this allowance is a reduction of 0.25% p.a. which is slightly lower than the 0.3% p.a. permitted in terms of Board Notice 270 issued by Registrar of Pension Funds Act for a materially similar purpose.

Accordingly in estimating the Initial Amount the investment return will be taken from the inflation linked bond yield curve as at 30 November 2014 reduced by 0.25% p.a. across the maturity spectrum.

Medical aid contribution inflation

circled This assumption is a very important one and requires us to estimate the long term relationship between medical inflation and general inflation.

The first point to make is that medical inflation is different in concept to how inflation is widely understood. This is best demonstrated by way of a simple example: - assume a patient visits his General Practitioner (GP) five times a year and the cost per consultation is R400; the member thus incurs GP costs of R2 000. In the next year the GP only increases his tariff by 5% to R420 per consultation, but the patient visits the GP 6 times, then the cost is R2 520. This represents a staggering increase of 26% compared to the previous year.

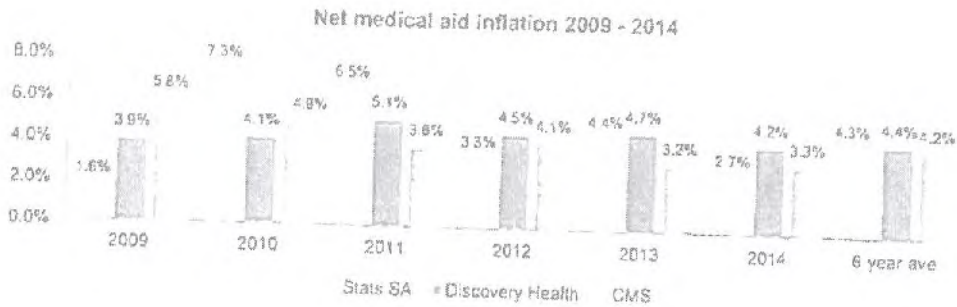
So whilst the GP has kept his tariff increase under control, medical aid inflation has increased sharply because of a change in utilisation. *So, changes in medical aid inflation are driven by not just tariff increases but also changes in utilisation.* In fact the main driver of medical aid inflation in South Africa in the past has been an increase in utilisation rather than tariff increases, a point we return to overleaf

It is common to refer to the so-called "net inflation rate" which is the excess of the increase in medical aid contributions over normal inflation. We have three sources of this net rate for the period 2009 to 2014:

- The figure provided by Statistics South Africa as per the chart below
- Information provided by Discovery Health in relation to their scheme
- The annual report of the Council of Medical Schemes (CMS)



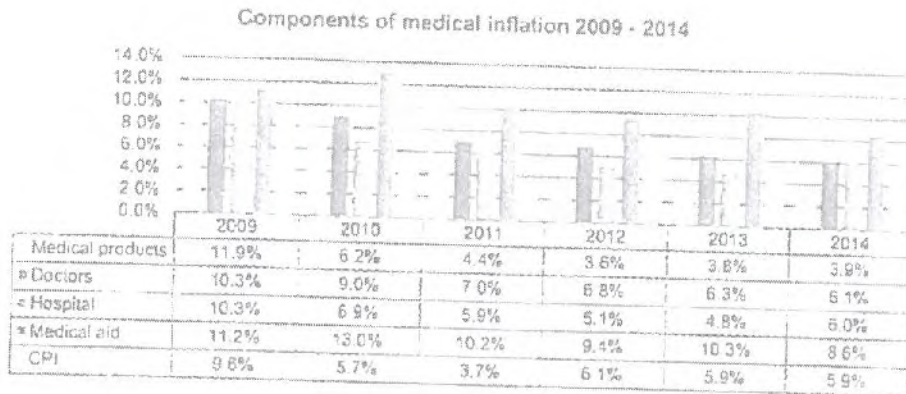
The statistic for each of the calendar years 2009 to 2014 as well as the average net rate over the last six years is shown in the chart below – please note the CMS net inflation rate for 2014 has been estimated:



Sources: http://beta2.statssa.gov.za/wp-content/uploads/2014/03/CPI-graph_1.png; Discovery Health: <https://www.medicalschemes.com/Publications.aspx>

Over the six year measurement period the three sources show a remarkably similar level of net inflation. Based on the above information a reasonable starting point for the assumption of medical aid inflation would be to assume that it will be 4.25% p.a. higher than normal inflation. This assumption would however need to be assessed against likely future tariff inflation and utilisation rates before the final assumption can be set.

The chart below shows the annual increase medical product, doctors and hospital costs and medical aid premiums as determined by Statistics South Africa for the period 2009 to 2014. We also show the increase in the official consumer price index (CPI).



Source: http://beta2.statssa.gov.za/wp-content/uploads/2014/03/CPI-graph_1.png

the developed world longevity has been increasing by an astonishing 2.5 years every 10 years (Source: Vaupel JW. *Biodemography of human ageing*, Nature, 2010; 464: 536-542)

We believe it is reasonable to assume that more expensive options like the Discovery Health Essential Comprehensive option will tend to have a greater proportion of higher income members and so improving longevity is likely to drive medical inflation higher. (The 2014 Essential Comprehensive contribution for a member plus one adult dependent is R6 318 per month versus the market average contribution rate as per the Council of Medical Schemes of R3 418 per month.)

The ageing effect is unlikely to last forever and so one should allow for a gradual tapering of this factor.

- The disease burden – advances in medical science have resulted in treatment protocols that not only extend life expectancy but also improve the quality of life. These improvements naturally come at a high costs initially – in time the cost of this treatment reduces. However, over the long term, the innovation needed to stimulate the development of new drugs and treatment protocols will keep prices high. We believe this force of innovation will be a permanent driver of medical inflation especially as people will pay much more to be healthy
- Anti-selection – legislation in South Africa requires medical schemes to charge members the same contribution rate irrespective of their age and health status.

An individual can join a medical scheme at any age, but if this person has not been a member of a medical aid before the scheme may restrict benefits for a period of up to two years. Where the individual joins the scheme as a consequence of his or her employment, these restricts are typically not applied. Subject the above a member of a medical scheme can move between the benefit options without any limitation of benefits.

There is almost certainly some anti-selective effect in South African medical schemes as members who know that they are in ill-health can move to benefit options that offer more benefits. Such anti-selection will also contribute to higher medical inflation albeit not with the same force as the disease burden

The net inflation assumption

Based on the above analysis our firm view is that medical aid inflation will exceed general inflation over the long term by a significant margin for the following reasons:

- Tariffs will go up by an estimated 1% to 1.5% p.a. in excess of general inflation to reflect fair remuneration of doctors and demand for private hospitals
- There will always be innovation in health care as human nature is to pay more to be healthier. Incentives drive innovation and it is fair and reasonable to expect that such innovation comes at cost in excess of general inflation



- Advances in medical science and innovation will have the effect of people living longer and in so doing increase the demand for health care. However, the ageing effect is likely to taper in the future.
- It is highly unlikely that South Africa will be able to afford a good national health system in the next 10 to 15 years that would alleviate the cost push on medical aids

Counteracting these forces will be processes to measure that medical treatment is effective (i.e. limit over-servicing) and benefit design that nudges members greater health consciousness. Taking the above into account we believe it is reasonable to assume that medical aid inflation will exceed general inflation according to the following scale

Period	Excess medical inflation
Next 5 years	4.25%
Years 6 to 10	4.00%
Years 11 to 15	3.50%
After year 16 to 20	3.00%
After 20 years	2.50%

In effect we are allowing for the ageing effect to reduce in impact over the next 20 years. Actuaries have sometimes argued that it is unreasonable to assume such high medical inflation on two grounds:

- Such high medical inflation will result in medical aids becoming unaffordable – we would agree except that we would reason that members will switch to a lower cost benefit option first before giving up their medical aid membership. As such member demand for health care is unlikely to reduce.
- If medical aid inflation is so much higher than general inflation then eventually health care will make up a very large part of the economy. This argument is flawed in that it does not take into account that health care is largely consumed and to the extent that this happens, it does not contribute to an increasing share of the economy.

Longevity of pensioners and their dependents

It is possible to insure pensioner longevity by entering into a mortality swap arrangement. The counterparty to such an arrangement will look to gather evidence of the general health of the membership via a simple health questionnaire. If the parties wanted an observable price for pensioner longevity we could arrange for an insurer to quote this.

In the absence of such an observable price the next best approach is to estimate the mortality assumption embedded in the insurer pricing on non-profit life annuities. We understand that a typical table is the so-called PA(90) table rated down by 3 years with an allowance for mortality to improve at rate of 0.5% p.a. which is the assumption that we have used.

Early retirement rates

The rate of early retirement is very difficult to estimate as the experience can vary significantly over time. Early retirement rates are generally higher when the Employer's business is struggling and lower in good times. We understand that the normal retirement age for most members is 65. In the absence of specific information we have used a general early retirement scale as set out in the table below:

Age	% of members retiring
55	5.0%
56	5.0%
57	5.0%
58	10.0%
59	10.0%
60	30.0%
61	10.0%
62	10.0%
63	10.0%
64	10.0%
65	100.0%

A higher rate is generally observed at age 60, especially in cases where the normal retirement age has been increased from 60 to 65.

We have not make any explicit allowance for a retrenchment programme in the above rates – we propose to add a piecemeal loading to allow for this contingency (see further discussion below).

In-service resignation, mortality and ill-health retirement rates

Consistent with the actuary's assumptions we have assumed in-service member mortality in line with the SA85-90 (light) table and used the same resignation scale as that adopted in the valuation of the liability. In addition we have used a general ill-health retirement scale to budget for the acceleration of the payment of the subsidy on such an event. The assumed average rate of mortality and ill-health retirement between the stated ages is set out in the table below:

Age band	Resignation rate	Mortality rate	Ill-health rate
30 – 34	12.5%	0.17%	0.19%
35 – 39	7.5%	0.21%	0.32%
40 – 44	2.5%	0.28%	0.70%
45 – 49	0.0%	0.40%	1.72%
50 – 54	0.0%	0.58%	0.00%
55 – 59	0.0%	0.83%	0.00%
60 – 64	0.0%	1.19%	0.00%



Member subsidy

We have done the calculations on assumed that all in-service members will receive a 66.7% subsidy based on the Discovery Health Essential Comprehensive Plan.

For pensioners we used a lower subsidy where the member has elected a lower cost benefit option. We have assumed that in future no pensioner will elect a lower cost benefit option, nor will any pensioner resign from the medical scheme

Piecemeal adjustment

We have loaded the calculated in-service member liabilities by 5% to make provision for the possibility of retrenchments and in so doing have added some R10 million to the Initial Amount. Subject piecemeal loadings are necessarily subjective.

Other assumptions

The other assumptions we made are:

- We assumed that 75% of in-service members would be married at retirement; this percentage is in line with the current in-service member proportion married.
- We have made no allowance for any children's benefit – this understates the liability slightly as on death in service and early retirement it is likely that there are dependent children and the data shows a few dependent children for current pensioners



Section 4: Results

Calculation date

A calculation date of 1 December 2014 has been used. The calculation would need to be refreshed at the actual settlement date using up to date data and the inflation-linked bond yield curve at that date.

Results per category

Using the assumptions set out in section 3 the Initial Amount for members per category before an expense allowance is shown in the table below:

Election	Category	Number of members	Initial Amount R'm
New Trust	In-service members	137	158.6
	Pensioners	328	270.1
No Response	In-service members	11	13.0
	Pensioners	418	257.5
Status Quo	In-service members	26	30.5
	Pensioners	31	22.5
Grand total		951	752.2

If we assume a total expense of R100 per member per month and allow for expenses to escalate in line with inflation the estimated value of future expenses is some R15 million. Thus the total initial amount increases to R767.2 million.

Section 5: Summary and conclusion

We have estimated the so-called Initial Amount for the remaining in-service and pensioners of the Denel Medical Benefit Trust as at 1 December 2014.

The calculation requires us to make a large number of assumptions, the most important of which is the budgeted future medical inflation, investment returns, pensioner longevity and the rate of early retirement. The level of future investment returns can be determined directly from the yield on government issued inflation linked bonds and one can get a market price for pensioner longevity leaving only future medical inflation and early retirement rates to be estimated.

For the purposes of calculation we have used the yield on government issued inflation linked bonds as at 30 November 2014 and estimated the other parameters. In setting our assumptions we have aimed to maintain a balance between reasonableness and conservatism. Importantly we have not made full allowance for possible low probability events that could increase the liability significantly (e.g. an extensive retrenchment programme, major medical advances).

The Initial Amount calculated can only be considered as a reasonable estimate and certainly no guarantee can be made it will be sufficient to cover the future obligations of the Trust. Accordingly members would need to be aware that there subsidy would need to be reduced if the actual experience is worse than that budgeted for; there is also the possibility that the subsidy could be increased in the actual experience is better than assumed.

The estimated Initial Amount is set out in the table below:

Election	Category	Number of members	Initial Amount R'm
New Trust	In-service members	137	158.6
	Pensioners	328	270.1
No Response	In-service members	11	13.0
	Pensioners	418	257.5
Status Quo	In-service members	26	30.5
	Pensioners	31	22.5
Grand total		951	752.2

This amount should be increased by some R15 million to allow for the capitalised value of future expenses.



"PB14"

From: paultjie@gmail.com
Sent: 21 January 2015 01:50 PM
To: Swart Kobus; Potgieter, Pottie; ziervogelnaude@mweb.co.za; Faan Louw; Sam J Basch; louis Visagie L (Louis.Visagie@rheinmetall-denelmunition.com); roderick keyser; Jacob van Wyk; 'Flip Mostert' (flip.mostert@rheinmetall-denelmunition.com)
Subject: Re: Vergadering met Denel

Dankie vir jou baie volledige terugvoering Kobus en ook aan julle ander wat reeds gereageer het. Denel se probleem is die antwoord (totale bedrag benodig) waarmee Ant uitgekome het. Ek sal in die volgende dag of so meer volledige terugvoering gee sodra ek n kans gehad het om met Pottie sienings te vergelyk Groete Paul
Sent via my BlackBerry from Vodacom - let your email find you!

From: Swart Kobus <Kobus5@retfunds.co.za>
Date: Wed, 21 Jan 2015 11:13:57 +0000
To: Paul Botha<paultjie@gmail.com>; Pottie Potgieter<Pottie.Potgieter@bigenafrica.com>; ziervogelnaude@mweb.co.za<ziervogelnaude@mweb.co.za>; Faan Louw<saamslouw@iburst.co.za>; Sam J Basch<sam@koisan.co.za>; Louis Visagie L (Louis.Visagie@rheinmetall-denelmunition.com)<Louis.Visagie@rheinmetall-denelmunition.com>; roderick keyser<Roderick.Keyser@rheinmetall-denelmunition.com>; Jacob van Wyk<vanwykj@iafrica.com>; 'Flip Mostert' (flip.mostert@rheinmetall-denelmunition.com)<flip.mostert@rheinmetall-denelmunition.com>
Subject: RE: Vergadering met Denel

Middag Paul

Dankie vir die terugvoer na julle vergadering vanmôre.

Ek sou graag wou weet hoekom Fikile nie Ant Lester se aanbevelings kan oorweeg nie. Betwyfel hy Ant se onpartydigheid of sy aannames/berekenings of is hy ongelukkig omdat Ant se aanbevelings nie in hulle guns is nie. Hoekom het ons tot 'n onpartydige Konsultant ingestem. Anders kon ons mos sommer Momentum se "eensydige en onbetroubare" syfers as vertrekpunt aanvaar het, wat ons wel gedoen het en dus die Trust opsie gekies het.

Dit is my siening (en ek glo die meeste van ons s'n) dat ek by twee geleenthede gekies het om lid van die DMBT te bly en my derde/laaste keuse was om in die DMBT of 'n soortgelyke Trust te bly waar ons nie swakker as die huidige Trust sal wees nie.

Ek ondersteun dus die standpunt dat Ant se aanbevelings (plus 'n sweetner) die vertrekpunt moet wees en bly want 'n verdere uitkoopaksie van min of meer die voriges is tydmors. Ons moet onthou dat ons lede gekies het om lid van 'n Trust te bly vanweë bepaalde voordele wat hulle uit die Trust geniet. Ek betwyfel dit of ons lede in enige iets anders as 'n Trust sou belangstel.

Groete

Kobus

Kobus Swart
Direct tel : (012) 452-7154
Direct fax : (012) 425-4016
Switchboard : (012) 452-7000
Physical Address: 1st Floor - Steven House, Brooklyn Bridge, 570 Fehrsen Street, Brooklyn
Postal Address: Private Bag X21, Brooklyn Square, 0075
E-mail : kobuss@retfunds.co.za

From: Paul Botha [mailto:paultjie@gmail.com]
Sent: 21 January 2015 11:23 AM



To: Pottie Potgieter; ziervogelnaude@mweb.co.za; Faan Louw; Sam J Basch; Swart Kobus; Louis Visagiel
(Louis.Visagiel@rheinmetall-denelmunition.com); rodrick.keyser; Jacob van Wyk; 'Flip Mostert'
(flip.mostert@rheinmetall-denelmunition.com)
Subject: Vergadering met Denel

Pottie en ek het vanoggend met Denel byeengekom. Fikile, Themba en Ayanda het Denel verteenwoordig.

Fikile het beklemtoon dat Denel nie kan oorweeg om Ant Lester se aanbeveling tov die bedrag benodig vir die Trust te aanvaar nie. Ons het aangedui dat ons vertrekpunt Ant Lester se bedrag MOET wees en dat ons nog addisioneel hiertoe n sweetener sou wou he

Dit was dus duidelik dat ons nie tot n vergelyk op hierdiue basis sou kon kom nie

Dit gese is daar punte van ooreenstemming en beide partye wil graag die saak tot n punt bring.

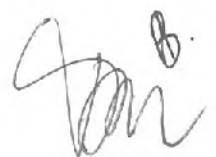
Denel sal kyk na n verdere uitkoopaanbod maar moontlik met verdere nuwe opsies (bv kontantaanbod). Hul voel egter dat n nuwe annuiteit maar net dieselfde sou kon wees as vorige annuiteite omdat hulle nie gessien wil word om af te wyk van wat reeds aangebied en aanvaar is nie. Van ons kant moet ons dink oor alternatiewe wat oorweeg kan word en weer met Denel konsulteer

Ons sal binnekort verder toelig

Groete

Paul

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<http://www.alexanderforbes.co.za/layouts/AFOSTSITE/EmailLegalNotice.htm>. Should you not have Web access, send an email to legalnotice@aforbes.co.za and a copy will be sent to you.



"PB15"

THE DENEL RETIRED⁹ EMPLOYEES MEDICAL SCHEME FORUM

27 January 2015

Attention: Mr Fikile Mhlontlo

The Group Chief Financial Officer
Denel (Pty) Ltd
By e-mail

Dear Fikile

RESPONSE ON DISCUSSIONS WITH DENEL REGARDING PROPOSED ALTERNATIVE TO THE CURRENT POST RETIREMENT MEDICAL

With reference to the discussions held on 21 January 2015 between representatives of Denel and

the Forum regarding the establishment of a "new" trust to take the place of the current obligation of Denel to fund post-retirement medical contribution subsidy (which obligation is currently discharged through the DMBT) we feel it necessary to summarize the current position as the Forum Management view it.

When the latest Denel buy-out offers were made a new option was included being the "Trust" option. This was intended to allow the beneficiaries the option of taking over the DMBT or to establish a new trust consisting of and managed by beneficiaries with no involvement of or guarantee responsibilities for Denel.

The immediate question was what would be the quantum required by this "new" trust in order to ensure that beneficiaries would not be prejudiced compared to their existing position.

Denel agreed to the Forum's request that an independent suitably qualified expert should be appointed to do the necessary research and calculations to quantify the existing position. We further agreed on certain candidates and a scope of work to guide the advisor's research.

Ant Lester from Towers Watson was subsequently appointed and has now, based on the agreed scope of work provided his well-motivated findings on the amount required by the "new" trust.

Although we as the Forum have certain reservations regarding the recommendation made (the calculations were based on the premise that subsidies would remain capped at the Discovery Essential Comprehensive option level and no provision was made for any compensation to members for the loss of the Denel "guarantee or our position as capital beneficiaries of a well-funded trust with very specific provisions that trust funds could only be used for payment of subsidies to members) our Forum management decided to accept the Advisor's findings subject to a 5% compensation for the loss of the guarantee. The principle of a compensation or "sweetener" is a generally accepted principle in buy-out offers as compensation for the loss of the company "guarantee" and increase in risk to the individual.

Chairman: FR Botha. Forum officials: SA Louw, H D du P Potgieter, J Swart, F Nalude, JP van Wyk, SJ Basch. Co-opted members: DL Visagie, R Keyzer, F Mostert



THE DENEL RETIRED⁵⁰ EMPLOYEES MEDICAL SCHEME FORUM

This position of the Forum Management was conveyed to Denel on Wednesday 21 January 2015. At the said meeting however you advised us that the amount as per the report of the Advisor was not acceptable to Denel as it was too high.

This, unfortunately, leaves us with no room to manoeuvre. We simply cannot recommend to our members that they accept a settlement which provides less than their current position. We consequently cannot make any counter-proposal as requested by you in the said meeting.

We would therefore like to propose that you as representative of Denel inform and motivate to us where you differ from the assumptions from the Advisor in order for it to be quantified in an orderly fashion. That is the only way we will be able to motivate it to our members. You are of course free to make other offers as well but please bear in mind the very detailed and well considered arguments set out by Ant Lester.

We appreciate the spirit of cooperation thus far and trust that we can move forward to arrive at a mutually beneficial solution.

Kind regards,



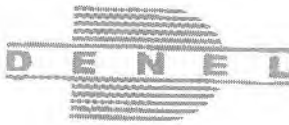
For: PAUL BOTHA: CHAIRMAN

Copies: Mr Themba Zwelibanzi

Chairman: PR Botha. Forum officials: SA Louw, H D du P Potgieter,
J Swart, F Naude, JP van Wyk, SJ Basch. Co-opted members: DL Visagie, R Keyzer, F Mostert



"PB16"



DENEL GROUP

Tel: +27 12 671 2781
Fax: +27 12 671 2833
Email: ETkileM@denel.co.za
Ref: Ltr/PostRetirement/4Feb15

4 February 2015

Mr Paul Botha
Chairman of Post Medical Retirement Forum

Email: paultjie@gmail.com
Pottie.Potgieter@bigenafrica.com

Dear Paul,

**PROPOSED ALTERNATIVE TO THE CURRENT POST RETIREMENT MEDICAL OFFER:
EMPLOYEE ONLY TRUST**

Thank you for your letter dated 27 January 2015 in respect of the above.

We wish to re-iterate significant points we raised at our meeting of 3 December 2014, where the Towers Watson report was presented and during the follow-up meeting of 21 January 2015. Denel has serious concerns regarding the recommendation of the report to almost double the current settlement offer. This is exacerbated by your stated position that the recommended amounts plus additional risk compensation would be the minimum position that your members will be willing to accept. This is despite the fact that the Towers Watson Report is an advisory document.

We believe the amounts per the report to be too conservative and materially out of line with our independent valuation of the liability. In addition, this will not be fair to members who accepted the previous alternative offers as more than a third of the original asset base would be set aside for the last 18% of the beneficiaries if this proposal were accepted. This goes beyond compensating for the related risk and is in our view not fair to both Denel and other beneficiaries will potentially expose Denel to liabilities. Based on the current position of the Forum, it is regrettable that we advise that Denel will not pursue the proposal further.

Denel remains committed to concluding the process considering that commitment was given to members that they will be given the opportunity to once again choose an alternative benefit on concluding this process with the Forum. Denel will further explore avenues that represent acceptable alternative benefits for the members including but not limited to restructuring the DMBT with Denel remaining the underwriter, offering annuity insurance to pensioners currently receiving medical subsidies, lump sum payments to active Denret members to be transferred to Denret and cash payments those that are not members of Denel's retirement fund. Denel will send the necessary communication to members in due course.

Denel SOC Ltd, Reg No 1992/001337/30, Nelmaplus Drive, Irene
P O Box 8322, Centurion, 0046, South Africa. Tel: +27 (0)12 671 2700, Fax: +27 (0)12 671 2751
Directors: Ms M J Janse van Rensburg (Acting Chairman), Mr R Saloojee¹ (Group Chief Executive Officer), Adv G Badela,
Dr G C Cruywagen, Ms Z B Mathenjwa, Mr Z Mhlonlo¹, Mr N J Maiseki, Mr M Msimang, Mr B F Ngwenya, Prof S M Nkomo,
Adv M S Nshikile, Mr M V Ratshimbani

¹Executive Director
Group Company Secretary: Ms E M Africa

A handwritten signature in black ink, appearing to be "M. B.", located in the bottom right corner of the page.

I wish to take this opportunity to thank you and the Forum for your efforts with regard to the employee-only trust proposal.

Please feel free to contact me for any clarification in this regard.



Fikile Mhiontlo
GROUP FINANCIAL DIRECTOR

cc. Themba Zwelibanzi - Denel
Gawie van Zyl - Denel



“PB17”

**THE DENEL RETIRED EMPLOYEES
MEDICAL
SCHEME FORUM**

5 March 2015

Attention: Mr Fikile Mhiontlo

Group Financial Director
Denel (Pty) Ltd
By e-mail

Dear Fikile

PROPOSED ALTERNATIVE TO THE CURRENT POST-RETIREMENT MEDICAL

Thank you for your letter dated 4 February 2015. Our late reply is due to consultation with the members of our management team.

Firstly we would like to thank you for the friendly spirit in which the discussions had taken place up to now and the truly consultative nature of these interactions. When we reached agreement on the appointment of the independent advisor as well as the terms of reference we really believed that the gap between our respective positions was narrowed and that we were close to achieving a mutually acceptable agreement.

We had hoped that the appointment of an independent and qualified consultant acting on a clear and agreed scope of work would help to overcome the problem of vested interests on the two sides, but following your response it seems that this effort has not provided the desired result.

Besides the apparent abrupt termination of negotiations as evident in your letter, we were also rather surprised by the large difference between your figure (which you term an "independent valuation") and the figure calculated by Towers Watson as being required to maintain the beneficiaries' status quo. We can only surmise this is as a result of differing departure points or the advisors not basing their calculations on the same considerations. As was also requested in our letter dated 27 January 2015 could you please confirm in which respects the scope of work provided to Towers Watson and the conclusions arrived at by its advisor deviate from the considerations and assumptions used in the "independent valuation of the liability" to which you refer.

Analysing and considering such differences could possibly significantly reduce the gap between our current positions and perhaps allow a continuation of negotiations

Yours faithfully,



A handwritten signature in black ink, appearing to read 'Paul Botha', written in a cursive style.

PAUL BOTHA: CHAIRMAN

A handwritten signature in black ink, appearing to read 'Paul Botha', written in a cursive style.

"PB18"



Tel: +27 12 671 2899
Fax: +27 12 671 2833
Email: ThembaZ@denel.co.za
Ref: Ltr/PostRetirement/26May15

26 May 2015

Mr Pottie Potgieter
Representative of Post Medical Retirement Forum

Email: Pottie.Potgieter@bigenafrica.com

Dear Pottie,

**PROPOSED ALTERNATIVE TO THE CURRENT POST RETIREMENT MEDICAL OFFER:
EMPLOYEE ONLY TRUST**

I refer to our meeting of 21 May 2015 attended by you and Mr Sam Basch on behalf of the Pensioner Forum. I wish to thank you for engaging with Denel rekindling consultations regarding the employee-only post-employment medical benefit trust proposal following Denel's letter dated 4 February 2015. This spirit of constructive consultation has ensured that we formulate, what we believe, is an acceptable proposal.

As was presented to you at our meeting of 21 May 2015 for consideration by the forum, Denel's offers have been based on industry assumptions applied by the independent actuary that calculates Denel's liability for publishing in annual financial statements. Denel considered and compared assumptions applied by two different companies, Towers Watson and NMG, which are tabulated below:

	Towers Watson	NMG
CPI	6.2%*	6.2%
HCCI	9.5%*	7.7%
DR	7.8%*	8.0%
Post-retirement Mortality		PA(90)

* Estimated as not explicitly stated in report

The major assumptions applied by both Towers Watson and the NMG are materially aligned except for the Health Care Consumer Inflation (HCCI) as Towers Watson estimates medical aid contributions increasing by 3% in excess of normal inflation over 30 years, whilst the NMG estimates an increase in the region of 1.5%. We feel that increases in medical aid contributions cannot exceed normal inflation by 3% per annum over the long term (30+ years) as such increases cannot be sustainable. If HCCI was to grow at a 3% real rate for 30 years, it is unlikely that medical aids will be able to continue as they are currently structured.

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Directors: Ms M J Janse van Rensburg (Acting Chairman), Mr R Sebojee¹ (Group Chief Executive Officer), Adv G Badela,
Dr G C Cruywagen, Ms Z B Mathenjwa, Mr Z Mhiondo¹, Mr N J Motseki, Mr M Maimang, Mr B F Ngwenya, Prof S M Nkomo,
Adv M S Ntshikla, Mr M V Ratshimbani

¹Executive Director
Group Company Secretary: Ms E M Africa

Having considered the above, Denel has been persuaded that the assumptions applied by NMG are appropriate, and the amount of assets set aside to cater for the future liabilities is fair. Denel also considered the fact that the way previous offers enjoyed reputable insurance companies' guarantees and in the case of the employee-only managed trust beneficiaries are taking the risk on their own. Denel has carefully evaluated this risk as well as the potential negative impact of future inflation changes and investment returns and concluded that an enhancement of 10% of the liability would sufficiently cover those risks that will be in the employees' hands. Denel has also considered that the envisaged employee-only managed trust will adopt a sound investment strategy that takes into account risk, inflation and investment returns.

The Denel proposal provides the new fund with the flexibility to adopt an appropriate conservative investment strategy to effectively mitigate the risk of higher than anticipated HCCI. Examples of such conservative investment strategies would be the investment mandate of the Conservative Portfolio and Secure Portfolio in the Denel Pension fund that returned inflation plus 5.2% and 5.9% respectively over the last 11 years. These funds have an investment strategy that target an inflation plus 3.5% return. The assets to be migrated to service the future liability, including the risk premium are estimated to be as follows:

	Number	Total Service Liabilities (R'm)	10% Enhancement (R'm)	New Trust Offer (R'm)
Actives	112	91.0	9.1	100.1
Pensioners	343	183.9	18.4	202.3
Total	455	274.9	27.5	302.4

Denel is committed to concluding the process considering our undertaking that members will be given an opportunity to once again choose an alternative benefit on concluding this process with the Forum. Denel is aware of and will endeavour to find a suitable tax position for this transaction including the verification of membership and agree a process with the Forum once the position of the Forum has been confirmed in this regard.

We look forward to your response confirming the acceptability of our in principle thoughts on this matter. Please feel free to contact me for any clarification in this regard.


Fikile Mhlontlo
GROUP FINANCIAL DIRECTOR

cc Themba Zwelibanzi - Denel
 Gawie van Zyl - Denel



"PB19"

THE DENEL RETIRED EMPLOYEES MEDICAL SCHEME FORUM

12 June 2015

Attention: Mr Fikile Mhlontlo

**The Group Chief Financial Officer
Denel (Pty) Ltd
By e-mail**

Dear Fikile

PROPOSED ALTERNATIVE TO THE CURRENT POST-RETIREMENT MEDICAL OFFER: EMPLOYEE ONLY TRUST

Thank you for the meeting at your offices on 21 May 2015 and your letter of clarification dated 26 May 2015. Our belated reply is due to some of us being out of town and the requirement from our side to consult with the members of our Forum management team on the outcome of the meeting and the content of your letter.

The management team applied its collective mind to the content of your letter of clarification as well as the feedback from our members who attended the meeting of 21 May 2015. The team is encouraged in certain respects, e.g. the willingness to take the income tax impact into consideration in the future structure of the proposed "Employee Only Trust". We are furthermore amenable to considering an alternative offer providing that the quanta of the existing rights of our members are not negatively affected.

However, following the involvement of an independent advisor (Ant Lester from Towers Watson who is an expert in this field) who arrived at certain recommendations, the Forum's management team has difficulty in accepting an alternative (lower) offer and still be sure that the existing rights of members are not negatively affected. At the same time we note the comments in your letter that the assumptions of the NMG actuaries differ from the findings of Towers Watson.

To deal with the above situation the Forum management team resolved to kindly request you to (simultaneously) involve both NMG and Ant Lester with a request to obtain a joint report and ideally a joint recommendation. If they cannot agree on a single recommendation they should indicate the main differences in their assumptions, reasons for those and the financial impact thereof. Such a report may then be used by the Forum management team to motivate their recommendation for deviating from the recommendations in the initial report prepared by Ant Lester.

Such a comparison need not pay attention to non-significant matters. In comparing a previous NMG actuarial report at our disposal with the Ant Lester report the only significant matters to consider and report on are the following:

Chairman: PR Botha, Forum officials: SA Louw, H D du P Potgieter,
J Swart, F Naude, JP van Wyk, SJ Basch, . Co-opted members: DL Visagie, R Keyzer, F Mostert



Item	NMG Assumption	Towers Watson Assumption
HCCI	7.7%	9.5%
Post-retirement mortality	PA(90)	PA(90)-3
Level of investment returns	3.5% above inflation	0.25% below the inflation linked bond rate

Jan

Administration cost Not clear

R 15 m provided for

In addition to the above and the matter of efficient income tax structuring, we also need clarity on are the following additional matters with a lesser significant impact:

In instances where beneficiaries are currently on lower options than the Essential Comprehensive, calculations for the calculated amount should provide for Essential Comprehensive as the beneficiaries have the option to move to a higher option at any time;

Clarity on the actuarial assumptions on spouses.

We are convinced that the combined report as proposed above could go a long way towards reaching agreement on the matter.

Yours faithfully,



For: PAUL BOTHA: CHAIRMAN

Copies: Mr Themba Zwelibanzi



"PB20"

D E N E L

24 June 2015

Tel: +27 12 671 2869
Fax: +27 12 671 2860
Email: ThembaZ@denel.co.za
Ref: Ltr/DMBT/24Jun15

Mr. Paul Botha
Chairman
Denel Retirement Employees Medical Scheme Forum

paultjie@gmail.com

Dear Paul

**PROPOSED ALTERNATIVE TO THE CURRENT POST-RETIREMENT MEDICAL OFFER:
EMPLOYEE ONLY TRUST**

We are responding to your letter dated 12 June 2015 in respect of the above.

Denel has considered your response to the proposal regarding the possible employee only trust set out in our letter dated 26 May 2015. In previous engagements, you indicated that the critical outstanding issue was reconciling our position to the Watson report for consideration by the Forum and such information was duly included in our previous correspondence. Based on our observation during the last meeting, we believed we were beginning to gain traction. We are disappointed that we have not found each other and the Forum is still using the Towers Watson report as its sole point of reference.

We do not support facilitating a joint report by MNG and Towers Watson as the assumptions, as well as Denel's view on those assumptions is well articulated in the correspondence between ourselves. The Forum is, however, at liberty to contact MNG (DMBT actuaries for purposes of the financial statements) and Towers Watson, should you require additional information and clarification to formulate a position. We wish to remind the Forum that it will not be possible for Denel to implement proposals that are not in line with the principles of the buyout process thus far.

We believe that Denel's proposal is reasonable and fair as it was informed by various actuarial reports as well as various discussions with the Forum resulting in Denel proposing to adjust the offers. We have come a long way and the proposal is fair with Denel having ensured that offers are attractive.

In order to provide all respondents with adequate time to consider their offers and respond appropriately, we have planned to communicate the offers in July 2015 and will appreciate your response to our letter of 26 May 2015 by no later than 29 June 2015.

Yours faithfully,


Pikile Mhlongo
GROUP FINANCIAL DIRECTOR

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St G C Cruywagen, Ms Z B Matherijwa, Mr Z Mhlongo, Mr N J Motseki, Mr M Msimang, Mr B F Ngwenya, Prof S M Nkomo,
Adv N S Nshikila, Mr M V Ratshimbilani

Executive Director
Group Company Secretary: Ms E M Africa



"PB21"

From: Fikile Mhlontlo <FikileM@denel.co.za>
Sent: 25 June 2015 08:16 PM
To: Paul Botha; thembaz@denel.co.za; Potgieter, Portie
Subject: Re: PROPOSED ALTERNATIVE TO THE CURRENT POST-RETIREMENT MEDICAL OFFER: EMPLOYEE ONLY TRUST

Dear Paul,

I note your email and its contents.

We support the Forum following a due process as it deems appropriate. Whilst this is the case, we have stated our position that we will not be part of NMG and Watson interaction as requested by the Forum. We believe we have adequately articulated areas of differences and pointed our position for consideration by the Forum. We will however alert NMG or any other party that the Forum seeks to engage them. Themba will liaise with you in this regard.

It is unfortunate that you refer to our plan to distribute offer letters in July 2015 as an arbitrary deadline. We wish to remind that the plan was to close this matter way back in December 2014. As a carrying company, we certainly will not keep this matter opened endlessly. We made undertakings to issue offer letters within a reasonable timeframe following engagement with the Forum - the expected time has long passed?

Kind Regards,
Fikile

From: Paul Botha
Sent: Thursday 25 June 2015 15:05
To: Fikile Mhlontlo;
Thembaz @denel.co.za;
Pottie Potgieter
Subject: PROPOSED ALTERNATIVE TO THE CURRENT POST-RETIREMENT MEDICAL OFFER: EMPLOYEE ONLY TRUST

Dear Fikile

Your letter dated 24 June 2015 refers

To our mind the issue of the widely divergent views expressed by Towers Watson and Denel remains. To address this we accept your proposal to communicate with NMG and request you to kindly arrange such a meeting through the DMBT. You are welcome to have Denel and or DMBT representatives attend same.

We note your desire to bring this matter to finality and to communicate new offers in July. Although from our side we would also like to reach agreement sooner rather than later we cannot accept an arbitrary deadline. Also we trust that your comment that you cannot deviate from previous buy out offers does not mean that we cannot through following due process find common ground

Kind Regards
Paul Botha

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**THE DENEL RETIRED EMPLOYEES
MEDICAL
SCHEME FORUM**

19 May 2017

Attention: Mr Themba Zwelibanzi
Mr Gawie van Zyl

By e-mail

Dear Themba/Gawie,

**PROPOSED ENHANCEMENT OF BENEFITS TO BENEFICIARIES
CONSIDERING FAVOURABLE FUNDING LEVEL OF THE DENEL MEDICAL
BENEFIT TRUST ("THE DMBT")**

Thank you for the brief but constructive meeting the first week of April 2017. Apologies for only responding now but I went on leave shortly after our meeting and have been playing catch-up with my other commitments since returning.

My opinion of what I believe will provide sufficient comfort to the majority of the remaining member-beneficiaries to secure their post-retirement medical aid subsidies should Denel wants to get rid of the obligation on its balance sheet (and what the Forum should be able to motivate to its constituency) can be summarized as follows:

1. Supported by Professional opinions and Acceptance of Offer by individual beneficiaries:

Although there is a host of experience and knowledge in the individuals comprising the Forum Management, any proposal for a settlement needs to be supported by professional opinions. The reasons being that we are not registered financial advisors and need to be assured that we will not be liable for any future claim from aggrieved beneficiaries and secondly to be able to motivate it properly to beneficiaries for acceptance. In that regard we propose the following:

Utilizing the basic assumptions of the Towers Watson report of November 2014 with adjustments/deviations that can be motivated (see 2 below);

Appointing an independent actuary to do the individual calculations for the current beneficiaries using these assumptions and agreed upon deviations as well as the current supporting information such as contribution rates. Please take note that the proposal is for calculations per individual. (For example we cannot use

general assumptions for age of spouses);

Any acceptable proposal arrived at should still be signed off by individual beneficiaries;

Obtaining of professional advice by Denel, the DMBT and beneficiaries on the implementation, legal compliance and any amended structure

2. Proposed Basis of calculation the Quantum of Allocation from the current Trust



THE DENEL RETIRED EMPLOYEES MEDICAL SCHEME FORUM

Assets:

Using the Towers Watson report as point of departure the proposed most important assumptions should be as follows:

2.1. Medical aid inflation

The conclusions in the Towers Watson Report providing for both higher medical inflation and higher utilization were as follows:

Period	Excess Medical Inflation
Next 5 years	4.25%
Years 6 to 10	4.00%
Years 11 to 15	3.50%
After year 16 to 20	3.00%
After 20 years	2.50%

The excess medical inflation the Towers Watson report arrived at above proved the last two years to be quite realistic considering increases in contributions by the majority of medical aid schemes. However, the Towers Watson report raised the following:

In effect we are allowing for the ageing effect to reduce in impact over the next 20 years. Actuaries have sometimes argued that it is unreasonable to assume such high medical inflation on two grounds:

Such high medical inflation will result in medical aids becoming unaffordable — we would agree except that we would reason that members will switch to a lower cost benefit option first before giving up their medical aid membership. As such member demand for health care is unlikely to reduce.

If medical aid inflation is so much higher than general inflation then eventually health care will make up a very large part of the economy. This argument is flawed in that it does not take into account that health care is largely consumed and to the extent that this happens, it does not contribute to an increasing share of the economy.

In the light of that we believe that a straight 3% above CPI would be a reasonable assumption to use.

2.2. The level of investment returns

In view of the amended age demographics of the remaining beneficiaries it will become increasingly difficult to go for high risk and return and to match cash flow and return.

An investment return of 2.5% above inflation seems realistic less 0.25% to allow for investment manager fees, ie 2.25% net.

2.3. The longevity of the beneficiaries and their dependants:

As per the Towers Watson report the PA(90) table rated down by 3 years with an allowance for mortality to improve at rate of 0.5% p.a. should be used

2.4. Early retirement Rate of In-service

beneficiaries: As per the Towers Watson report

2.5. In-Service resignation, mortality and ill-health retirement rates:

As per the Towers Watson report

2.6. The dependency status of members in-service, at retirement and in retirement

The actual situation should be used for dependent spouses and children's benefits.

2.7. The rate at which members may resign from the Trust (and in so doing forfeit their subsidy)

This should be set at zero

2.8. The level of future expenses that the Trust should provide for.

In view of critical mass that is being lost due to dwindling number of beneficiaries a figure of R150 per member per month escalated by inflation plus 1.5% should be allowed for.

3. Enhancement of benefit to compensate beneficiaries for removal of the Denel underwriting:

A figure of at least 15% is market related and should be offered on top of the calculations in 2 above.

4. Tax dispensation:

Any change must be structured in such a way that the beneficiaries retain the current income tax dispensation.

5. Structure for accommodating the beneficiaries:

The ideal situation would be to retain the existing Trust for the remaining beneficiaries and to create a vehicle for extracting surpluses allocated to Denel per agreement.

6. Legal Position of the DMBT, Denel's obligation and to execute the proposed scheme without legal risks.

There remains questions in my mind about the possibility of executing any agreed settlement between Denel and the remaining beneficiaries and achieving the objectives of all the parties given the wording of the Trust Deed and the stipulations of AS19.

I have even questions in my mind if the previous buy-outs with the Momentum Annuity as vehicle really removed the obligation from Denel's balance sheet as it retains the structure of a Group scheme.

Proper legal and other professional investigations with advice is necessary before significant time is spent on the matter. In that regard I would like to propose that a process is started involving the Forum Management, the DMBT and Denel to arrive at a mutually beneficially situation for Denel and the beneficiaries that would also enable the DMBT Trustees to fulfil their fiduciary responsibilities. Due to the latter it may also be possible to utilize DMBT funds for such studies.

Kind regards,

HDD (POTTIE) POTGIETER



"PB23"

**THE DENEL RETIRED EMPLOYEES
MEDICAL
SCHEME FORUM**

22 July 2019

Attention: Mr Gawie van Zyl

Acting Group

CFO Denel

SOC

By e-mail

Dear Gawie,

**DENEL OBLIGATION TOWARDS POST-RETIREMENT FUNDING: PROPOSED
PROCESS TO ARRIVE AT A MUTUALLY BENEFICIAL POSITION FOR
BENEFICIARIES OF THE DENEL MEDICAL BENEFIT TRUST ("THE DMBT") AND
THE COMPANY**

Thank you for the constructive meeting on 5 July 2019.

Apologies for the time we took to put our formal proposal in writing. This was due to us having to first consult extensively with our Forum Management to ensure that we embark on crafting a solution that can be motivated to the remaining member-beneficiaries. All of these beneficiaries need to have their post-retirement medical aid subsidies secured and importantly, have sufficient comfort with Denel being released of its future obligation.

1. Updated Professional opinion/Legal Assistance:

As stated previously, any proposal for a settlement needs to be supported by a credible professional opinion(s) to be able to motivate it properly to beneficiaries for acceptance. In that regard we propose the following:

Enlist the services of Towers Watson (Ant Lester) to provide an updated report;

We believe it would be prudent and sensible to use Ant Lester as he has the credibility and is *au fait* with the basic assumptions of the Towers Watson report of November 2014, of which adjustments/deviations/updates will form a good basis;

Obtain calculations from an independent actuary (if that cannot be done by Ant Lester himself) to determine the individual calculations for the current beneficiaries using the assumptions as per the forthcoming updated Ant Lester report (and agreed upon deviations as well as the current supporting information such as contribution rates). Please take note that the proposal is for calculations per individual. (We cannot for example use general assumptions for age of spouses);

Professional legal assistance will be required before and during implementation;



Involving credible financial institutions later in the process to determine feasibility of underwriting and a sustainable management structure.

2. Proposed review of assumptions:

Without limiting the professional report of Ant Lester/Actuary, we are of the opinion that the following should be addressed:

2.1. The calculation of the obligation should be based on the Essential Comprehensive option for all beneficiaries. This will be a huge motivation to some beneficiaries currently on lower options due to affordability problems, to accept the settlement;

2.2. Using the Towers Watson report as a point of departure; the proposed most important change in assumptions should be as follows:

2.2.1. The level of investment returns:

In view of the changing age demographics of the remaining beneficiaries it will become increasingly difficult to go for high risk and return and to match cash flow and return. However, we agree that the 2014 Ant Lester report was on the conservative side.

2.2.2. Early retirement rate of in-service

beneficiaries: This should be set at zero.

2.2.3. In-service resignation, mortality and ill-health retirement

rates: This should be set at zero.

2.2.4. The dependency status of members in-service, at retirement and in retirement:

The actual situation should be used for dependent spouses and children's benefits.

2.2.5. The rate at which members may resign from the Trust (and in so doing forfeit their subsidy):

This should be set at zero.

2.2.6. The level of future expenses that the Trust should provide for:

In view of critical mass that is being lost due to the dwindling number of beneficiaries a figure of R200 per member per month escalated by inflation plus

1.5% should be allowed for.

Enhancement of benefit to compensate beneficiaries for removal of the Denel underwriting:

This should be offered on top of the calculations and form part of final negotiations.

3. Tax dispensation:

Any change must preferably be structured in such a way that the beneficiaries retain the current income tax dispensation.

4. Future structure for accommodating the beneficiaries:

The ideal situation would be to retain the existing Trust for the remaining beneficiaries and to create a vehicle for extracting surpluses allocated to Denel per agreement. However, in the process of amending the Trust Deed we need to allow more flexibility to the application of benefits to beneficiaries as well as an underwriting structure by a credible financial institution including a long term sustainable management structure.

I trust this outline will be favourably considered and we hope to further engage Denel in fruitful discussions.

Kind regards,

A handwritten signature in black ink, appearing to read 'Paul Botha', with a stylized, cursive script.

PAUL BOTHA
CHAIRMAN

A handwritten signature in black ink, appearing to read 'Paul Botha', with a stylized, cursive script.

“PB24”

WillisTowersWatson

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25 October 2019

Mr. Gawie van Zyl
Head of Corporate Finance and Group Treasurer
Denel SOC Ltd
P.O. Box 8322
Centurion
0046

By e-mail: Gawiev@denel.co.za

Dear Gawie

Statement of Work

Thank you for the opportunity to provide consulting services to the Denel SOC. This statement of work sets out the terms of engagement of Towers Watson (Pty) Ltd (“Willis Towers Watson”, “we”, “our” or “us”) by the Denel SOC (“you”) to provide the requisite actuarial services.

Terms and Conditions of Engagement

The services described below will be provided subject to the terms set out in this Statement of Work and Attachments 1 and 2.

Scope of Services

Willis Towers Watson will provide the services described in Attachment 1 to this statement of work. Where necessary, the advice and assistance to be provided will be described in more detail in further communications between you and us.

Any variations to the scope of the services to be provided must be set out in writing between you and us.

Other Services

We recognise that you may also ask us, from time to time, to provide other services.

For incidental additional services we would usually provide those services without the need for an additional signed statement of work but simply to let you have an indication of the scope of the further services that we propose to provide and any changes to the existing fee arrangements. The work undertaken in those cases will be undertaken under the terms of this statement of work.

Executive Chairman: R Omar
Executive Director: A Leslie
Non-Executive Directors: ZB Ebrahim, E Francis*
* British

Reg No: 1998/001765/07. Towers Watson (Pty) Ltd is an authorized Financial Services Provider

Willis Towers Watson I.P.I.L.L

In the case of more substantial projects or pieces of advice we reserve the right to issue further, separate, statements of work setting out in full the terms upon which we would be willing to undertake the project, or provide the advice, in question.

Timetable

We will agree with you timetables for the work that we are to undertake. Our ability to meet any such timetable is dependent on the you and your other service providers fulfilling their obligations in respect of any assignment forming part of the services.

Willis Towers Watson Team

Ant Lester will be the lead consultant for this project. He will be assisted by Andre Bezuidenhout who is an actuary. Other Willis Towers Watson personnel may assist with the services as needed.

Fees and Expenses

In consideration for rendering the services described in Attachment 1 to this statement of work, the Trust will pay Willis Towers Watson on an hourly fee basis as per the table below.

Individual	Hourly rate excluding VAT
Ant Lester	R5 250
Andre Bezuidenhout (actuary)	R4 000
Actuarial support	R2 300

Clause 2 of the Terms & Conditions in Attachment 2 sets out our standard approach to calculating fees for services where those fees have not otherwise been set or agreed.

Invoicing and Payment

We will bill you quarterly by way of an invoice, which will set out the services we have provided. If you have any questions about any of our invoices, you must notify us within 30 days from the date of the invoice.

Limitation of Liability

We draw your attention to clause 7 of the Terms & Conditions in Attachment 2, which sets out provisions limiting our liability in respect of this engagement. For the purposes of this statement of work, our liability to you will be limited to 20 times our fees.

FAIS Disclosures

Willis Towers Watson is registered as an authorised financial services provider under the Financial Advisory and Intermediary Services Act No. 37 of 2002. Accordingly, we have provided the necessary statutory disclosures as Attachment 3



Willis Towers Watson Limited

Acceptance

If this statement of work accurately describes the terms of our engagement, please have an authorised representative of the Trust countersign below and where indicated in the Terms & Conditions in Attachment 2. Willis Towers Watson appreciates the opportunity to be of service you. Should you have any questions now or during our engagement, please contact me.

Yours sincerely



Towers Watson (Pty) Ltd

Enc: Attachment 1 (Scope of Services)

Attachment 2 (Terms & Conditions)

Attachment 3 FAIS Disclosure Annexure

On behalf of Denel SOC, I confirm my agreement to this statement of work, including the Scope of Services in Attachment 1 and the Terms & Conditions in Attachment 2:

Signed:

Name:

Date:



Scope of services

Willis Towers Watson shall provide the following services to the Denel Medical Benefits Trust (the Trust) on behalf of Denel SOC:

1. Perform actuarial calculations to determine the interest of each beneficiary member of the Denel Medical Benefit Trust;
2. Determine the aggregate actuarial liability allowing for different scenarios based on investment returns, medical aid inflation, longevity and other assumptions;
3. Consider the alternatives that may best meet the needs of the Denel Medical Benefits Trust members including the possible outsourcing of the liability to an insurer. In providing such advice we will have regard to the tax structuring of the alternatives.
4. Should the advice be to retain the Trust we will advise the Trustees on possible amendments required to the trust deed, setting up a sustainable management structure and investment strategy

An advice we provide will be in a written format. Please note Willis Towers Watson is not a specialist legal and tax firm and sometimes it will be appropriate for the Trust to obtain such specialist legal and tax advice, particularly in relation to any restructuring of the Trust Deed. Whilst we will work with the legal firm providing such advice, Willis Towers Watson cannot accept responsibility for any of the legal and/or tax advice so provided. Denel SOC will be required to pay the costs associated with such legal advice.



Willis Towers Watson and Denel SOC
Terms & Conditions

1. **Parties and Application.** These terms and conditions ("terms") cover all services, advice, work product and other deliverables (collectively, the "services") provided by the Willis Towers Watson entity identified below or any of its affiliates ("Willis Towers Watson", "we", "our" or "us") to the entity identified below or any of its affiliates ("you" or "your").

The scope of our services for each project (the "statement of work") will be agreed by you and us in written communications and shall, unless provided otherwise, incorporate these terms.

2. **Fees.** Unless otherwise specified, our fees will be calculated by reference to any agreed assumptions, the time spent on, the importance, complexity and urgency of each project. Any fees or rates quoted or estimated are exclusive of any applicable sales taxes, Value-Added Tax, or similar taxes. Expenses are charged in addition.

Unless otherwise agreed, we will submit invoices for the services provided and expenses incurred on a quarterly basis. Invoices are payable within 30 days of receipt. In the event that invoices are not paid within that time, we shall be entitled to charge interest on the outstanding amount at an interest rate equal to the lesser of 1.0% per month or the maximum rate allowed by law.

3. **Our responsibilities.** We shall provide the services in a professional manner with reasonable skill and care. We will assign to the project team members of our staff with adequate education, training and experience to perform the tasks assigned to them. We will use reasonable endeavour to meet any timetable that we may agree with you.

The work product we deliver to you in connection with the performance of the services will not infringe any intellectual property right of any third party. Unless otherwise expressly agreed in writing, we do not accept any fiduciary or trust responsibilities or related liability in connection with the performance of the services. We do not provide legal, accounting or tax advice.

4. **Your responsibilities.** You will provide us in a timely manner with the documentation, information, access to your personnel and cooperation we reasonably require to provide the services. Any delay or failure to provide materials, information or cooperation may result in a revision to any agreed timetable and/or, if we need to do additional work as a result, in additional fees being charged. We will rely on the documentation and information provided to us by you or your representatives and do not take responsibility for verifying the accuracy or completeness of it. You may rely only upon our final work product and not on any drafts or oral statements made by us in the course of providing the services.

5. **Intellectual Property Rights and Work Product.** You shall retain ownership of all original data and materials, and the intellectual property rights in that data, provided to us by you or your representatives. You will have the right to use, reproduce and adapt the copies of the work product delivered to you for internal purposes within your organisation. We shall retain the intellectual property rights in such work product, and the skills, know-how and methodologies used or acquired by us during the course of providing any services.

The services we perform, including the work product we deliver to you, are provided solely for the intended purpose, and may not be referenced or distributed to any other party without our prior written consent. You may distribute our work product to your affiliates, provided that you ensure that each such affiliate complies with these terms and the applicable statement of work as if it were a party to them, and you remain responsible for such compliance.

You shall not refer to us or include any of our work product in any shareholder communication or in any offering materials (or fairness opinion provided by your professional advisers) prepared in



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connection with the public offering or private placement of any security, unless otherwise agreed in writing.

6. **Confidentiality and Data Privacy.** Each party shall protect all confidential information which the other party provides to it (whether orally, in writing or in any other form) using the same standards as the recipient applies to its own comparable confidential information, but in no event less than reasonable measures.

Each party's confidentiality obligations will not apply to information: (i) already known to it at the time of disclosure; (ii) in the public domain or publicly available; (iii) provided to it by a third party who is under no such obligation of confidentiality; or (iv) independently developed by it. Each party may disclose confidential information to its legal advisers to protect its own legitimate interests and to comply with any legal or regulatory requirements. If any court, regulatory authority, governmental agency, professional body or legal process requires the recipient to disclose information covered by this confidentiality obligation, then the recipient may make any such disclosure; provided that the recipient will, if permitted by law, advise the other party promptly of any such requirement and cooperate, at such other party's expense, in responding to it.

We are a global business and in performing the services we may pass individually identifiable personal information ("Personal Data") within our global network of offices and to our affiliates and to providers of IT outsourcing who will be subject to appropriate data protection standards. Irrespective of where we receive or hold Personal Data on your behalf, we confirm that, acting as data processor we will take appropriate technical, physical and organisational / administrative measures to protect that Personal Data against accidental or unlawful destruction or accidental loss or unauthorised alteration, disclosure or access. We will only use the Personal Data for the purposes of providing services to you or for other reasonable purposes which are related to the services we provide, unless you instruct us otherwise. You and Willis Towers Watson shall each comply with the provisions and obligations imposed on each of us by applicable data privacy legislation and regulations.

7. **Limitation of Liability.** If our services do not conform to the requirements agreed between you and us, please notify us promptly and we shall re-perform any non-conforming services at no additional charge or, at our option, refund the portion of the fees paid with respect to such services.

If re-performance of the services or refund of the applicable fees would not provide an adequate remedy for damages actually suffered by you, the aggregate liability of Willis Towers Watson and its employees, directors, officers, agents and subcontractors (the "related persons") to you whether in contract, delict (including negligence and gross negligence), breach of statutory duty or otherwise for any losses arising from or in any way connected with each statement of work or the services provided under that statement of work shall not exceed in aggregate twenty times our total fees.

Nothing in these terms shall exclude or limit the liability of Willis Towers Watson or our related persons in the case of: (a) death or personal injury resulting from our or our related person's negligence; (b) wilful misconduct; (c) fraud; or (d) other liability to the extent that the same may not be excluded or limited as a matter of law. In no event shall we or any of our related persons be liable for any incidental, special, punitive, or consequential damages of any kind (including, without limitation, loss of income, loss of profits, or other pecuniary loss).

Where we are jointly liable to you with another party, we shall to the extent permitted by law only be liable for those losses that correspond directly with our share of responsibility for the losses in question.

8. **Third Parties.** These terms only create rights enforceable by you and do not create any rights enforceable by any other party.

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We accept no responsibility for any consequences arising from any third party relying on our work product. If we agree to provide our work product to a third party, it shall be on the terms specified by us.

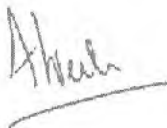
You agree to reimburse us for all costs (including reasonable legal fees) that we incur in responding to any requests or demands from third parties, pursuant to legal process or otherwise, for data or information related to the services provided to you.

9. **Termination.** Either party may terminate a project on 30 days' written notice to the other party. We shall be entitled to be paid our fees for services rendered up to the date of any such termination, and for expenses incurred. Any of these terms that would be reasonably intended to apply after termination will do so.
10. **Miscellaneous.** These terms, together with the statement of work, set out the entire agreement between you and us concerning the provision of the services. Any modifications of or amendments to these terms or a change to the services must be in writing and agreed by the parties. Should any of these terms be declared void, illegal or otherwise unenforceable, the remainder shall survive unaffected.

Neither party may assign or delegate any of its rights or obligations to any third party without the prior written consent of the other party. Notwithstanding the foregoing either party may assign or delegate any of its rights and obligations to an affiliate. We reserve the right to employ subcontractors to assist us in providing services and to pass to them any information and materials they need to perform their work. Where we use affiliates or subcontractors to provide the services to you, we will remain responsible for the provision of the services to you.

11. **Dispute Resolution and Governing Law.** The parties agree that they will work in good faith to resolve any disputes that arise out of or in connection with these terms or any statement of work. If a dispute cannot be resolved by the parties, the matter will be submitted to non-binding mediation before the parties pursue any other remedies. Both parties agree that the exclusive jurisdiction and the proper venue for any action brought hereunder will be the courts of South Africa. Any controversy, dispute or claim of any kind between the parties shall be governed by and interpreted in accordance with the laws of South Africa, without regard to any provisions governing conflicts of laws.

Signed by and on behalf of:
Towers Watson (Proprietary) Limited



Ant Lester

Director

Date: 25 October 2019

Accepted and agreed by and on behalf of: Denel
SOC

By _____



Print Name: _____

Print Title: _____

Date _____

Jim B

WILLIS TOWERS WATSON DISCLOSURE INFORMATION

Company name	Towers Watson (Pty) Ltd ("Towers Watson") operating as Willis Towers Watson
Company Registration No.	1998/001765/07
Address (Head Office)	Level 4, Monte Clare Place, 23 Main Road, Claremont, 7708
Address (Servicing Office)	As above
Contact person Telephone/Fax/Email	Ant Lester Tel. 021-6813701 Fax 021 - 6813800 E-mail ant.lester@willistowerswatson.com
Legal Status of Towers Watson	Willis Towers Watson is an independent consulting company and does not own shares in, or represent, any insurance company. The South African operation of Willis Towers Watson has no contractual relationship with any insurer, other than the mandates in terms of which we are authorised to provide advice on the products of certain product suppliers.
License Details	<p>Towers Watson (Pty) Ltd was issued with License No. 2545 on 29 September 2004, in terms of which Towers Watson (Pty) Ltd is an authorised Financial Services Provider pursuant to the Financial Advisory and Intermediary Services Act No 37, 2002.</p> <p>The license authorizes Towers Watson (Pty) Ltd to carry on business in respect of financial advisory services in the following products:</p> <ul style="list-style-type: none"> • Long-term Insurance: Category A, B, C • Equities • Money Market Instruments • Bank Deposits • Debentures and securitized debt • Bonds • Derivative Instruments • Participatory interests in collective investment schemes • Foreign currency denominated investment instruments • Pension Fund benefits • Health service benefits provided by a medical scheme as defined in section 1 of the Medical Schemes Act, 1998 • Medical Scheme Gap Cover provided via short-term insurance contracts or policies



Willis Towers Watson

Willis Towers Watson is committed to providing its clients with the highest possible quality of service. In the event that a situation was

<p>Complaints Resolution</p>	<p>to arise where the lodging of a formal complaint is considered necessary, this should be addressed, in writing, to the Compliance Officer at our Head Office. Willis Towers Watson's detailed complaints resolution procedures are also available, on request, from the Compliance Officer</p> <p>Willis Towers Watson maintains professional indemnity cover (insurance) of at least twenty times the fees charged to the Trust</p>
<p>Professional Indemnity insurance</p>	<p>Willis Towers Watson has been appointed to strategic consulting services to the Denel Medical Benefits Trust on behalf of DENEL</p>
<p>Services provided by Willis Towers Watson</p>	<p>SOC. The basis of Willis Towers Watson's engagement is set out in the Agreements with the Trust.</p>
<p>Fees payable to Willis Towers Watson</p>	<p>The basis of remuneration for any work undertaken by Willis Towers Watson is set out in the Agreements referred to above amended from time to time as agreed between the parties.</p>
<p>Supplier relationships</p>	<p>Willis Towers Watson receives no commission payments or other forms of remuneration from any service provider representing the Denel SOC.</p> <p>Willis Towers Watson is the sponsor of Retirement Online, an umbrella retirement fund. Retirement Online's Board of Trustees is comprised of three independent trustees and three Willis Towers Watson trustees. Retirement Online contracts with the best service providers for administration, investments and insurance and then governs these contracts. Presently, Futuregrowth Asset Management is a participating employer in Retirement Online.</p> <p>Willis Towers Watson performs professional investment consulting services to Momentum Employee Benefits relating to the Momentum Multi-Manager Guaranteed Fund. This contract is for a fixed fee and Willis Towers Watson is not incentivised in any way to place assets in this product.</p> <p>Other than the parties listed above Willis Towers Watson has no other contractual or professional relationships with any suppliers to the Denel SOC.</p> <p>For the sake of clarity, the above disclosures are made in relation to the South African business of Willis Towers Watson that previously operated under the name of Fifth Quadrant Actuaries & Consultants. Any relationships that may exist with one of Willis Towers Watson's affiliates outside South Africa would be purely coincidental and would not in any way compromise the independence of the advice given to clients in South Africa.</p>
<p>Product supplier details</p>	<p>To the extent that we assist the Trust in establishing any relationship with an investment manager or insurer, Willis Towers Watson will provide details of such financial service providers.</p>

I _____, acknowledge the receipt of disclosure information from Willis Towers Watson (Pty) Ltd by the Denel SOC in terms of disclosure requirements as set out in the FAIS Act and the requirements of the underlying General Code of Conduct for authorised Financial Service Providers and their Representatives.

Signed at _____ on this _____ day of _____ 2019 on behalf of the Denel SOC

who warrants he / she is duly authorized hereto

A handwritten signature in black ink, appearing to be a stylized name with a large initial, located in the bottom right corner of the page.

**THE DENEL RETIRED EMPLOYEES
MEDICAL
SCHEME FORUM**

27 January 2020

Attention: Mr Gawie van Zyl

The Group
CEO Denel
SOC
By e-mail

Dear Gawie,

**DENEL OBLIGATION TOWARDS POST-RETIREMENT FUNDING: PROPOSED
PROCESS TO ARRIVE AT A MUTUALLY BENEFICIAL POSITION FOR
BENEFICIARIES OF THE DENEL MEDICAL BENEFIT TRUST (“THE DMBT”) AND
THE COMPANY**

With reference to our ongoing discussions to find an alternative to the current arrangement regarding subsidies for medical aid contributions and your verbal request to Pottie earlier this month for an indication of what should be acceptable to us we would like to comment as follows:

1. Ant Lester from Willis Towers Watson made some suggestions to us late in November as to what we should get out of a settlement in order not to prejudice the interests and rights of the beneficiaries. We requested him to share these with you as we are all committed to jointly work towards finding a settlement which is equitable and hopefully one with which we would all be happy. To state the obvious, the more favourable the outcome for us the easier it would be for us to motivate same to beneficiaries and get their buy-in.
2. During our meeting with Ant Lester in late November 2019 we requested some amendments/review of certain assumptions and to obtain quotes from financial institutions again on the basis of that. He could only provide us with the revised quotes/figures on 24 January 2020, hence our late response to you.

3. Our Objectives with this proposal:

To make the proposed exercise work for everybody, we set the following objectives:

It is to be fair and equitable;

It needs to have a high probability of being accepted by the majority of beneficiaries;



Risks have to be mitigated for beneficiaries also as far as the long term management of the funding vehicle is concerned

Low reputational risk to Denel;

More flexibility to beneficiaries than the present Trust arrangement to make it more attractive to beneficiaries.

4. Proposal:

The proposal based on our objectives and the input from Ant Lester is as follows:

- 4.1. That the amount earmarked for Beneficiaries be invested with a financial institution (Sanlam and Momentum provided quotes) as suggested by Willis Towers Watson in the individual names of Beneficiaries to provide monthly payments to Discovery (or other medical aid provider) or to the Beneficiary for alternative use should he or she so decide (subject to tax provisions);
- 4.2. Quotes from financial institutions based on:
 - The contributions on Discovery Essential Comprehensive option for all beneficiaries regardless on which option he is currently; Allowance for medical inflation being 4.5% above CPI (average increase for the Discovery Essential Comprehensive option over a ten year period is 4.6% according to Ant Lester report);
- 4.3. We furthermore propose an enhancement of 30% in addition to 4.2 above to allow for the risk of Denel's underwriting being removed as well as an enhancer for beneficiaries to accept the offer;
- 4.4. That in return Beneficiaries absolve Denel from any and all future obligations regarding medical aid contribution subsidies;
- 4.5. That Willis Towers Watson be tasked to implement the above arrangements;
- 4.6. That the Forum assist to present any agreed upon proposed settlement to beneficiaries;

5. Quotes from financial institutions and Reserves:

On the basis as in 4.2 Ant Lester requested Momentum, Old Mutual and Sanlam to quote on the basis that all members were on the Essential Comprehensive Scheme irrespective of the option they had elected and to provide for this premium to increase annually by inflation + 4.5%. The results based on the yield curve as at 31 December

2019 including adding the proposed 30% were as follows:

	CPI+ 4%	CPI + 4.5%
Momemtum	688 253 547	732 144 792
Old Mutual	648 187 654	Not prepared to quote
Sanlam	612 307 441	650 170 899
Lowest	612 307 441	650 170 899
Plus 30% enhancement	795 999 673	845 222 169

The surplus in the scheme as at 1 April 2019 is just over R1 000 million (i.e. R1 billion) and the liabilities were R390 million. If the members received 50% of the surplus the assets available for the buy-out would R890 million. Based on 2 December 2019 pricing one could enhance the pension by some 35% if the members were allocated 50% of the surplus



. We are confident the above will adequately safeguard the interests and rights of Beneficiaries and as well as Denel and we would welcome an opportunity to discuss this further with you and get inputs from you as to what could be acceptable to Denel

We suggest the implementation costs be carried by Denel and these be deducted from the amounts to be received from the DMBT on its dissolution.

I trust this outline will be favourably considered and we hope to further engage Denel in fruitful discussions.

Kind
regards,



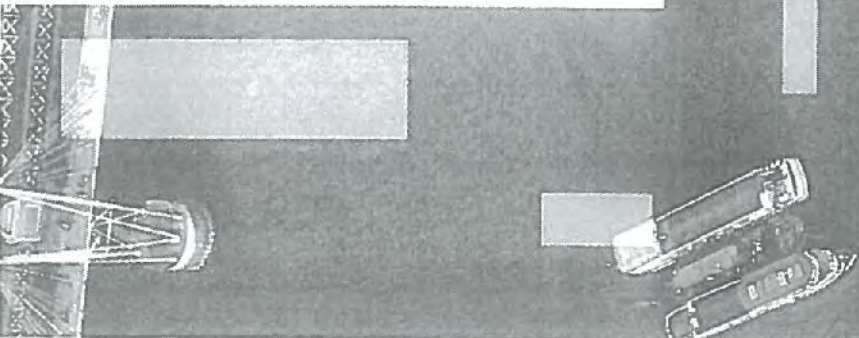
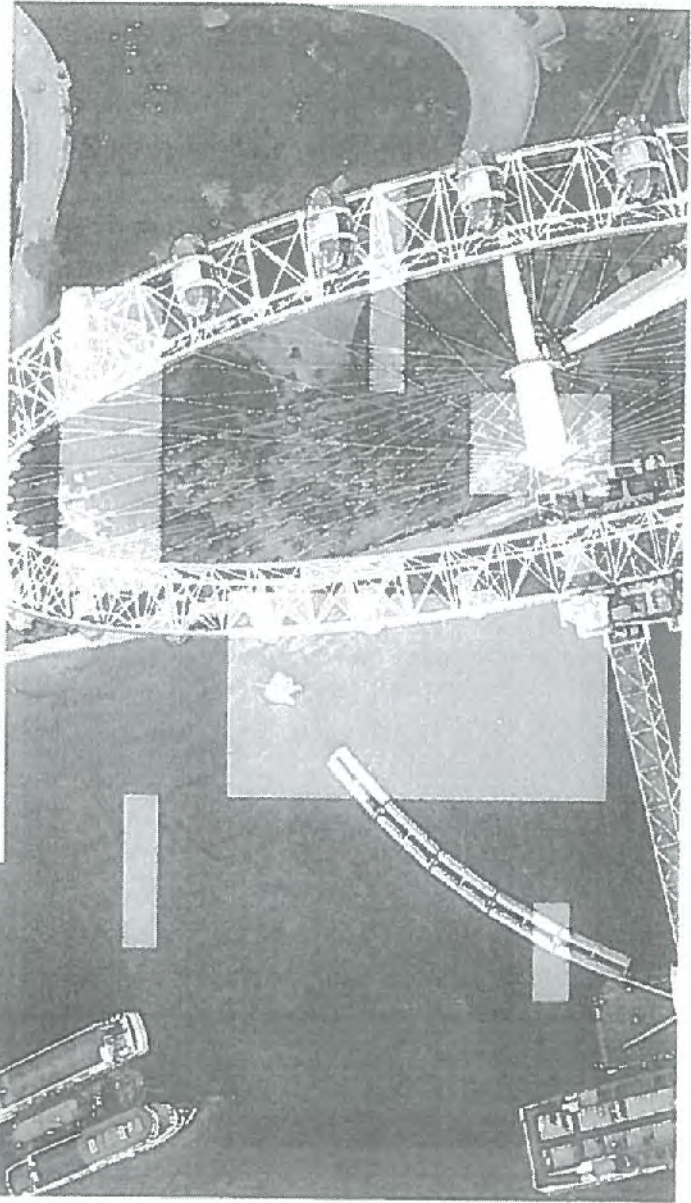
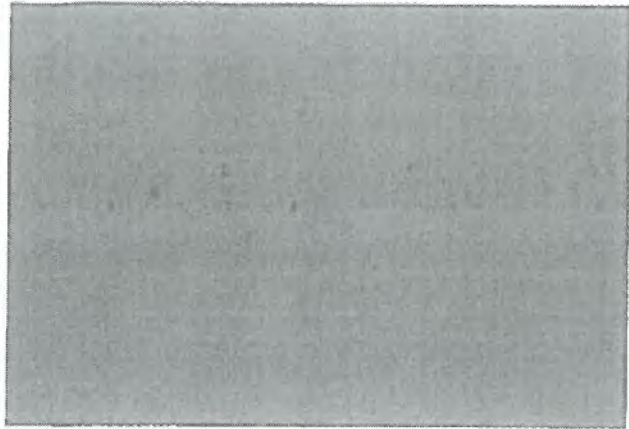
PAUL BOTHA
CHAIRMAN

Chairman: PR Botha. Forum officials: SA Louw, H D du P Potgieter,
J Swart, F Naude, SJ Basch, . Co-opted members: DL Visagie, R Keyzer, F Mostert



"PB26"

Willis Towers Watson I.I.T.I.I



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Denel Medical Benefit Trust

Introduction

Denel and members of the Denel Medical Benefit Trust ("the Trust") are considering coming to an agreement in terms of which the current beneficiaries are outsourced to an insurer.

To this end Willis Towers Watson obtained quotations from Old Mutual, Sanlam and Momentum based on the inflation linked bond yield curve as at the close of business on 6 March 2020. We point out that inflation linked bond yields have increased materially in the subsequent week, which would reduce the cost of buying out the beneficiaries.

Basis of quotation

We requested the insurer to quote on the following basis:

- All beneficiaries are entitled to a subsidy based on the cost of belonging to the Discovery Health Essential Comprehensive option.
- Provision should be made for the subsidy to increase by inflation plus 4% p.a.; alternatively, inflation plus 4.5% p.a. Such a level of pension and annual increases must be guaranteed by the Insurer.
- The child's subsidy would be paid to age 25 except for disabled children where the subsidy would continue lifelong.
- The subsidy would only be paid to the spouse to whom the beneficiary was married at the time of the outsource (i.e. no provision is made for subsequent marriage or remarriage).
- In the event that there was deflation the increase would be 4% (or 4.5%), but to the extent that inflation arose subsequently increases would be clawed back.
- The quotes should be provided on a commission free basis.

Old Mutual indicated that they are only prepared to quote on the CPI + 4% p.a. basis.

Taxation issues

All the Insurers indicated that there should not be any adverse tax consequences for the Pensioners if the arrangement is outsourced. In providing their comment the Insurers relied on the provisions of the Binding Class Ruling (BCR 008) issued by SARS in October 2009.

This ruling provides that:

- The proceeds of the life annuity policy paid to the Pensioner will constitute a taxable fringe benefit in the hands of the Pensioners. However, to the extent that the Pensioner applies the policy proceeds to pay contributions to a medical aid scheme, a nil value will be placed on such amount. This means that should the life annuity benefit exceed the amount paid to the medical aid scheme such excess will be taxable.



• The annuity issued by the life insurer must comply with the following conditions:

- a) The policy will not allow the Employer to benefit under the policy; nor will it confer rights on the Employer.
- b) The policy will only be enforceable against the Insurer by the Pensioner;

The policy benefits will be payable to an approved medical aid scheme ("MAS") for as long as a Pensioner remains a member of such MAS. Any excess of the policy benefit above the contribution payable to the approved MAS will be payable directly to the Pensioner and will be taxable.
- d) The policy benefits will only be payable directly to the Pensioner in full if the Pensioner ceases to be a member of an approved MAS.
- e) The Pensioner's rights under the annuity policy will not be capable of surrender, commutation or assignment, or of being pledged as security for any loan.
- f) The Pensioner will not be entitled to a cash payment, other than in circumstances set out in clauses c) and d) above.
- g) The annuity will be paid for the life of the Pensioner and/or the Pensioner's dependants.
- h) The Pensioner and the Employer will not be entitled to cancel the transaction.

Please note that to the extent that the Pensioner makes additional contributions to the MAS (e.g. their share of the contribution or to fund medical benefits not paid by the scheme) they will qualify for the tax rebate as provided for in section 6A, and if applicable, an additional medical expenses tax credit in terms of section 6B of the Income Tax Act. The same tax dispensation applies to such contributions currently made by the Pensioners.

The above applies to future Pensioners but there is no equivalent tax dispensation for in-service members. The issue is that if an in-service member is issued with a policy which is payable immediately replicating the benefits paid by the Trust, he or she never "retires" and so the tax neutral dispensation that applies to Pensioners never comes into effect. Accordingly, the arrangement has adverse tax consequences for in-service members.

Proposed legal structure

We recommend the following approach:

1. The Trust should invest in a policy with an Insurer in terms of which the Insurer guarantees the current subsidy based on the Essential Comprehensive scheme premiums plus an enhancement
2. Pensioners will have the choice to opt out of the Trust and elect to receive the pension in their own name. This opt-out must be structured as a settlement so that the provisions of BCR 008 apply. The Trust will need to get specialist tax and legal advice to facilitate this option.
3. Alternatively, the Pensioner may elect to remain a member of Trust. In this case the Trust will pay the lesser of the pension paid by the Insurer (subsidy based on Essential Comprehensive option plus the enhancement) and the total medical scheme contribution for the option the



member has elected to the medical scheme since the Trust cannot make a payment directly to the Pensioner.

4. Existing in-service members will remain members of the Trust. Again, the Trust will pay the lesser of the pension paid by the Insurer and the total medical scheme contribution for the option the member has elected to the medical scheme. Once the in-service member retires, he or she will have the choice to opt out of the Trust and become a Pensioner of the Insurer as a settlement in terms of BCR 008.

5. The Trust Deed needs to be amended to allow the surplus allocated to the Employer to be paid out.

At the same time the Deed should be changed to provide that the Trust's liability is limited to the amount received from the Insurer in respect of a particular. In this way, the Trust can continue even if there is no participating employer

The major impediment to implementing the above is whether approval can be obtained to change the Trust Deed to allow for the Employer to be a beneficiary and receive its share of the surplus. We are unsure of the legal hurdles that need to be crossed and whether or not beneficiary consent is required to change the Deed. We would be pleased to assist the Trust in engaging with specialist legal advice on these matters.

Quotations received

The table below sets out the quotations received from the Insurers based on the yield curve as at 6 March

2020. These are the "raw" quotes and we have not engaged in any negotiation around the prices. We would expect to reduce the price following this process

Table 1: Insurer quotes – all figures are R'm

Purchase basis	Momentum	Old Mutual	Sanlam
CPI + 4.0% p.a.			
In-service members	95.5	88.1	87.1
Pensioners	605.6	580.4	604.0
Total	701.1	668.5	691.1
CPI + 4.5% p.a.			
In-service members	105.0	n/a	98.3
Pensioners	644.9	n/a	643.5
Total	749.9	n/a	741.8

The Old Mutual pricing is the most favourable by a considerable margin, noting that they are not prepared to offer the CPI + 4.5% p.a. buy-out option. The difference between the 4.0% and 4.5% basis is a loading of some 7%, which can form part of the enhancement provided to beneficiaries.

Enhancement to settlement values

The key risks faced by the beneficiaries following this settlement offer are:

- (a) Medical aid inflation could be higher than the CPI + 4% p.a. (or CPI + 4.5% p.a.) provided for Table 2 below shows the increases in the Discovery Health Essential Comprehensive option over the past 10 years:

Table 2: Discovery Essential Comprehensive increases versus inflation

Year	Premium increase	Previous Year Inflation
2011	8.0%	3.5%
2012	9.0%	6.1%
2013	11.8%	5.7%
2014	8.9%	5.4%
2015	9.9%	5.3%
2016	9.0%	5.2%
2017	11.9%	6.8%
2018	8.3%	4.7%
2019	9.9%	4.5%
2020	11.0%	4.0%
Average over 10 years	9.8%	5.1%

Thus, medical aid inflation has exceeded price inflation by 4.6% p.a. over the past 10 years. This observed difference is the reason why we requested quotations on the CPI + 4.5% p.a. basis. However, as pointed out above, a 7% enhancement to the CPI + 4% p.a. basis gets one to the same point.

- (b) The beneficiaries are fully exposed to SA inflation risk as determined by the government – one has observed in many countries that governments have a bias towards understating inflation to reduce their funding costs (i.e. there is a material moral hazard). Discovery are going to set their premiums relative to actual health care inflation and in an environment where government has a bias towards understating inflation, medical premium inflation could exceed the CPI +4% p.a. (or 4.5% p.a.) allowed for.
- (c) The Insurer could get into financial difficulty and so may not pay the full pension. It is important to highlight in this regard that the Pensioners will not be able to change Insurer and so they are entering into a long term contract (in many cases of 20+ years) with no flexibility to exit. Pensioners need to be compensated for this lack of flexibility / liquidity.
- (d) National Health Insurance may push up the cost of private health care significantly and this may be reflected in the increase in the Essential Comprehensive premiums.
- (e) The Insurers will back their guarantee by investing a good proportion of the assets in government issued inflation linked bonds. To the extent that government defaults on this debt, the Insurers are going to struggle to meet their contractual obligation. We think a government default is very unlikely; more likely is that government will understate inflation, which is covered in (b) above.
- (f) The beneficiaries take on demographic risk to the extent that the only dependants covered by the Insurer are those that are on record as at the settlement date. For example, the future spouse of a beneficiary who is currently single, but who marries after the settlement date, will not be covered. Presumably had the Trust continued such a future spouse would have been covered.

There is no hard science to answer the question of what fair compensation would be for the above risks. However, our sense is that the Solvency Assessment Methodology (SAM) which regulators use to set capital requirements for insurers would result in a loading of some 30% to 35% for the CPI + 4% p.a. basis.

Apportionment of the assets

We have been provided with the market value of the Trust's assets as at 31 January 2020 (R1 485.7 million). We note that these assets are invested almost entirely in equities and so we have reduced the market value by 10% to allow for the estimated market movement to 6 March 2020.

The table below sets out the estimated apportionment of the assets between the beneficiaries and Denel as at 6 March 2020:

Table 3: Estimated apportionment of the assets as at 6 March 2020 – all figures are R'm

Item	R'm
Base liability (CPI + 4% p.a.)	668.5
Proposed 30% enhancement	200.6
Total liability	869.1
Market value of assets	1 338.1
Denel share	469.0

Unfortunately, equity markets have declined significantly since 6 March 2020. Whilst the cost of the settlement offer will reduce because inflation linked bond yields have increased (we estimate the price reduction to be some 3% to 4%), this is insufficient to offset the decline in the market value of the portfolio.

Way
forward

Our view is that Denel is unlikely to proceed with the settlement offer based on current market conditions.

However, in our opinion, it makes sense to enter into a policy with an Insurer which provides for the current

subsidy together with guaranteed increases of inflation plus 4% p.a. or 4.5% p.a. (i.e. excluding the enhancement), with this investment being staged over the next six to nine months. This would result in some R668.5 million (or 50%) of the Trust's assets being invested in inflation linked bonds based on current market levels.

Our counsel is based on the following considerations:

- The Trust is currently running a very large mismatched position investing in equities to meet inflation-linked bond type liabilities. The Deed currently precludes Denel from receiving any benefit from the Trust, so they have no interest in running a mismatched position. Furthermore, our reading of clause 5 of the Trust Deed precludes the Trustees from increasing the benefits without Denel's consent. Accordingly, it is unclear to us what the motivation may be for running such a large mismatched position.
- The Trust is extremely well funded and so it can run a mismatched position. However, the current strategy is relatively undiversified and, in an extreme event, the sustainability of the current benefit expectations of the beneficiaries could come under pressure. We point out that this is a very low probability, but if this were to occur the Trustees will have a tough time in explaining the rationale for the investment strategy, especially given the previous bullet point.

The intervening period could also be used to firm up all the legal issues, with the focus being on amending the Trust Deed to permit the Trustees to distribute excess assets to Denel and for the Trust to be liquidated. We would be happy to work with your legal specialists around such a revision.

Disc
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B.


Willis Towers Watson has prepared this report for Denel as part of a strategy to settle its post-retirement medical aid obligation.

The analysis in this report is based on the information received from Old Mutual, Sanlam and Momentum and the data used is based on that previously supplied by the Denel Medical Benefit Trust updated with known data changes. There are a number of complex legal and tax issues associated with this settlement offer on which Willis Towers Watson is unable to provide advice. Accordingly, Denel should seek expert legal and tax advice on these matters.

This report is based on information available to Willis Towers Watson as at date of this report and takes no account of subsequent developments after that date. It may not be modified by the client, nor may it be disclosed by the client to any other party without Willis Towers Watson's prior written permission, except as may be required by law. In the absence of its express written agreement to the contrary, Willis Towers Watson accepts no responsibility for any consequences arising from any third party relying on this report or the opinions expressed. This report is not intended by Willis Towers Watson to form a basis of any decision by a third party to do or omit to do anything.

A handwritten signature in black ink, appearing to be 'A.B. [unclear]', located in the bottom right corner of the page.

From: Paul Botha <paultjie@gmail.com>
Sent: 18 June 2020 09:07 AM
To: Potgieter
Subject: Fwd: Meeting tomorrow
Attachments: image002.png

----- Forwarded message -----

From: Gawie Van Zyl <Gawiev@denel.co.za>
Date: Wed, 17 Jun 2020 14:09
Subject: RE: Meeting tomorrow
To: Lester, Ant (Cape Town) <Ant.Lester@willistowerswatson.com>
Cc: Potgieter, Pottie <Pottie.Potgieter@bigengroup.com>, Paul Botha <paultjie@gmail.com>, Andisa Nqwaba <Andisan@denel.co.za>, Carmen Le Grange <CarmenL@denel.co.za>, Danie Du Toit <DanieD@denel.co.za>, Gawie Van Zyl <Gawiev@denel.co.za>

Dear Ant

Our discussion with the chair of FIC and the actuaries on Monday refer

As a summary

- * Denel were comfortable with the assumptions that was the basis of the quotes received from the insurers
- * Denel will assume the risk on 1) The value of the assets due to market volatility and 2) Changes in the liability quote from insurers due to yield curve etc.
- * Based on the above Denel requested that a risk premium of 15% on top of the insurers quote be proposed to the forum in response to the forum proposal of 25%

The chairperson stressed that Denel remains committed for a speedy resolution with a fair outcome for all, and that the wellbeing of pensioners is of the utmost importance for Denel

Looking forward to your response on the Denel counter proposal

Kind Regards

Gawie van Zyl
Denel Group Head of Corporate Finance
gawiev@denel.co.za
T: 012 671 2932
C: 082 806 9755

From: Lester, Ant (Cape Town) <Ant.Lester@willistowerswatson.com>
Sent: Thursday, 21 May 2020 21:27
To: Gawie Van Zyl <Gawiev@denel.co.za>
Cc: Potgieter, Pottie <Pottie.Potgieter@bigengroup.com>; Paul Botha <paultjie@gmail.com>
Subject: Meeting tomorrow

Dear Gawie

I have obtained updated quotations from Old Mutual, Momentum and Sanlam. These prices are based on the yield curve on Friday 15 May. Once the Insurer provides a quote it is valid for three or five days, so we will need to reprice before implementation. Naturally the price depends on interest rates; higher interest rates reduce the price, whereas lower rate increase the price. Nevertheless the pricing shown below is a good starting point.

Clearly Old Mutual is the lowest cost Insurer. The key terms of their quote are:

- * Pension increases of CPI + 4% p.a
- * Current in-service and pensioner membership cover based on current dependency status (no provision for remarriage or additional dependents)
- * Subsidy based on the Essential Comprehensive option for all members



- * In the event of deflation the minimum increase is 4%
- * The Income Tax Act limits the maximum increase an Insurer may grant for the first five years to 20%; we will look to include a contractual provision that Old Mutual must grant catch-up increases after the expiry of the five years if the increases are capped at this 20%. They have indicated that they are comfortable to include such a clause.
- * No commission payable

We understand that the assets at the end of April were some R1 414.2 million.

My firm advice to the Pensioner Group is that they should seek an enhancement of at least 25%. This enhancement is compensation for the following risks:

1. Medical aid inflation can be higher than the CPI + 4% provided for – the historic increases in the premium rates over the past 10 years has been CPI + 4.5% p.a.
2. The pensioners face the moral hazard of the government understating the inflation rate to reduce their funding cost; such understatement of inflation is observed in many countries and is not unique to South Africa
3. The strategy is fragile to the extent that the pensioner's entire subsidy value is with Old Mutual – thus there are circumstances under which Old Mutual simply cannot afford to pay the pension.

These are not risks that the Pensioners currently need to face as the DMBT has assets which are more than twice the Old Mutual consideration of some R600 million.

Finally there are a few key moving parts here – the value of the assets and the cost of the pensions. I think we need a plan to get this implemented on terms acceptable to the members and Denel as soon as possible. The Old Mutual quote allows the DMBT to be the owner of the policy whilst you are engaging with the members. Once the deal is agreed an individual policy will be issued to each pensioner. Irrespective of whether you proceed with the deal we assess the Old Mutual pricing to be attractive and would be a good asset for the DMBT to hold anyway.

I look forward to our discussion tomorrow.

Kind regards
Ant

Willis Towers Watson

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A handwritten signature in black ink, appearing to be 'G.M.' or similar, located in the bottom right corner of the page.

**THE DENEL RETIRED EMPLOYEES
MEDICAL
SCHEME FORUM**

27 June 2020

Mr Gawie van Zyl
Head of Corporate Finance and Group Treasurer
Denel SOC Ltd
P.O. Box 8322
Centurion
0466

Dear Gawie

SETTLEMENT OF POST-RETIREMENT MEDICAL AID LIABILITY

We refer to the various meetings and discussions we have had in this regard. We understand that Denel is proposing a settlement offer of current subsidy percentage based on the Discovery Health Essential Comprehensive Plan together with inflation plus 4% p.a. and a 15% enhancement. Such a pension would be purchased from an Insurer (the indications are that this will be Old Mutual) and ultimately each Trust beneficiary will be issued with a policy in their own name providing the above. This will extinguish the liability of the Denel Medical Benefit Trust to the current beneficiaries.

We are in agreement with all the terms other than previously we proposed a 25% enhancement, which Denel has counter-offered at 15%. We believe it is important to reach a "win-win" situation and therefore propose that the final enhancement be agreed at 20%. Our request for the 20% enhancement is motivated as per the below:

- *The Essential Comprehensive premium increases have averaged inflation 4.5% p.a. over the last 10 years. We believe it is reasonable to assume that this pattern will continue. Had provision been made for the subsidy to increase at inflation plus 4.5% p.a. as opposed to 4%, the cost would have been an estimated 7% higher.*
- *Medical inflation may, in future, exceed even inflation plus 4.5% p.a. We believe that there should be some compensation for this risk, say 3%*
- *The beneficiaries are entering into a long term contract with an insurer which they cannot exit. Whilst we accept that the risk of an Insurer like Old Mutual getting into financial difficulty is low, this is not an impossible event over say the next 15 years (the duration of the contract for most beneficiaries). Naturally the beneficiaries would face a reduction in their pension under such circumstances. We consider a 5% enhancement to be fair compensation for this risk*

Finally, this is deal that is going to need the support of all the pensioners. A large of the pensioners will look to us to draw comfort that arrangement is fair. We



really would like to be able say "hand over heart" that what Denel is offering is very fair. A further 5% enhancement bringing the total enhancement to 20% gets us there. Naturally we would have preferred the 25% enhancement, but we are comfortable to go with our proposed 20%

Finally, we wish to express our appreciation to Denel is getting the process to this point. We are committed to doing all we can to assist Denel in getting this transaction implemented as this truly represents a "win-win" for the DMBT beneficiaries and the Company.

Yours sincerely



PAUL BOTHA

CHAIRMAN

Chairman: PR Botha. Forum officials: SA Louw, H D du P Potgieter, J Swart, F Naude, SJ Basch, . Co-opted members: DL Visagie, R Keyzer, F Mostert



“PB29”

From: Paul Botha <paultjie@gmail.com>
Sent: 02 July 2020 02:27 PM
To: Potgieter; Frederik Naude; Swart Kobus; At Louw (Destiny4u); Louis Visagie; Flip Mostert; Sam J Basch; Anne-Marie Louw; roderick.keyser
Subject: Medies

Middag Alma!

Pottie en ek het sopas n gesprek met Denel gehad. Die gesprek is gelei deur Gloria Serobe die Voorster van hulle Finansieskomitee. Denel se Aktuarisse was by, so ook Ant Lester, verteenwoordigers van die DMBT Trustees en Denel Direkteure en Topbestuur.

Ons voorstel van die 20% toeslag is aanvaar onderworpe aan Denel se volle Direksie se goedkeuring - wat more byeenkom. Ons verwag dat hulle dit ook sal steun.

Die rol wat die Forum sal en kan speel in die proses is breedvoerig bespreek en daar sal van ons verwag word om aktief betrokke te wees om lede se inkoop te verkry..

Ant en Claire sal die motivering wat aan lede moet uitgaan opstel. In paralel hiermee moet ons ook met lede kommunikeer en ons siening gee. Ant sal n gesprek met Jacques die PO van die DMBT voer om die belegging benodig om lede se polisse te dek te bespreek.

Meer hieroor soos dinge gebeur

Pottie sal jy asb waar nodig uitbrei.

Groete

Paul

Paul



Denel Medical Benefit Trust (DMBT) Letter to pensioners

Background

As former employees of Denel, who were employed prior to 2002, you are contractually entitled to receive subsidies in respect of your medical aid contributions to Discovery Medical Scheme ("Discovery") in retirement.

In 2002, Denel founded the Denel Medical Benefit Trust ("the Trust") of which you became a beneficiary. Denel contributed funds into the Trust and in turn the Trust has been responsible for making the subsidy payments and for safeguarding the assets of the Trust on your behalf. It is noted that Denel still retains the obligation in respect of the subsidisation of your medical aid contributions. The Trust is the vehicle through which payments in lieu of this subsidy are made.

The details of the subsidy which you receive are as follows:

- Members of Denel Retirement fund receive 66.67% of contributions post-retirement for main member and dependents.
- Members of Denel Pension fund receive 15% of contributions post-retirement for main member and dependents.
- The subsidy amount is capped at a maximum of the relevant percentage (66.67% or 15%) of Discovery's Essential Comprehensive plan.

At retirement, your dependents are eligible for a subsidy of their medical contributions if they are a member of Discovery. However, if, for example, your marital status changes during retirement, any new dependents are not eligible for a subsidy of their medical aid contributions.

Future of the Denel Medical Benefit Trust

Discussions with yourselves as beneficiaries of the Trust have taken place regarding the granting of you, as beneficiaries of the Trust, a fair and equitable compensation amount to buy out Denel's obligation with an insurance company in exchange for Denel being relieved of this obligation. This buy-out will be funded from the assets currently held by the Trust. It is proposed that Denel receive the remaining assets in the Trust once the buy-out has been effected.

As per the current Trust Deed, once the buy-out is effected, Denel does not have the right to access any remaining assets in the Trust. The Trust Deed needs to be first amended to allow the Trust to be able to distribute assets to Denel. The Trust Deed can only be amended if this is agreed to by all beneficiaries of the Trust or alternately, amended via a court proceeding. The preferred option is to obtain agreement from every one of you as beneficiaries of the Trust in order to avoid any costly court proceedings.

Proposed Buy-out Transaction

As part of the proposed buy-out, an insurance contract will be purchased from an insurance company using the proposed compensation amount.

The proposed compensation amount will ensure a subsidy of post-retirement medical aid contributions in line with the maximum limit based on the relevant percentage (66.67% or 15%) of Discovery's Essential Comprehensive plan for all beneficiaries of the Trust. In addition, a further enhancement of 20% has been agreed with the beneficiaries of the Trust in order to equitably compensate you for taking on the risks associated with this transaction.



Through this insurance contract you will receive monthly payments which will be directed towards Discovery to meet your medical aid contributions. The contract will have the following terms and conditions:

- The benefits will be paid directly to Discovery for as long you remain a member of Discovery.
 - You will not be liable for any tax on the payments from the insurance contract if they are directed towards Discovery to meet your medical aid contributions in full. However, you may be liable for tax for amounts you receive from the contract in excess of medical aid contribution OR if you directly receive the full payment instead of Discovery.
 - Payments will increase annually at a guaranteed rate of CPI plus 4%.
 - Only current spouses and dependents are covered. New spouses and dependents after the transaction will not be provided for.
 - The child's subsidy amount will cease at age of 25 except for disabled children for whom this will continue for life.
 - In the event of economic deflation, where CPI is less than zero, the minimum increase will be 4% (instead of CPI plus 4%)
 - You will not be able to surrender the contract for any surrender lump sum benefit.
 - Neither you nor Denel will be entitled to cancel the transaction once in effect.
- It is noted that based on quotations received as of 21 May 2020, Old Mutual has provided the most competitive quotation.

Considerations for Beneficiaries in relation to the Buy-out Transaction

We believe that the proposed offer is fair to you as pensioners and beneficiaries for the Trust. It is however noted that there are both potential advantages and disadvantages of this transaction to you that you must consider before making a decision as to agree to the proposed transaction.

The proposed buy-out offer has the following advantages for you:

1. As part of this offer, you will receive a higher subsidy amount than you are currently receiving as a result of the agreed 20% enhancement. Furthermore, the subsidy amount on which the transaction is proposed is based on the Discovery Essential Comprehensive plan which is a further advantage for pensioners who are currently on lower Discovery plan options.
2. There is a potential for you to pay less out of your own pocket for medical aid contributions compared to the amount you are currently meeting in respect of medical contributions. For example, after the transaction, the subsidy amount will be independent of your plan chosen - you will be able to opt for a less expensive medical aid option and receive the same subsidy amount which can reduce your net costs.
3. The transaction will give you more flexibility. You can use the monthly payment amounts for other uses if you need, although this will attract a tax liability. Any amounts received directly to you will be subject to tax.
4. You will no longer be exposed to the risks associated with your benefits being managed by Trust. These risks, for example, may include poor investment performance of assets in the Trust and resulting risk of future reductions in benefits if Denel are unable to make good any shortfall in the Trust. This transaction will guarantee payments based on the Discovery Essential Comprehensive plan and will guaranteed an increase of CPI plus 4% per annum regardless of any investment conditions.

The potential disadvantages of this buy-out are as follows:

1. If medical aid contribution increases are higher than CPI + 4 % you will subsidise a larger share of your medical aid contributions. This risk has been mitigated to an extent by the agreed 20% enhancement.
2. There is a risk of the insurer facing financial difficulty. However, this risk is mitigated to an extent by the presence of Prudential Authority (an extension of the South African Reserve Bank) who regulates and monitors the financial soundness of all insurance companies through capital adequacy requirements.
3. Subsequent spouses and additional dependents who are currently not on record will not be covered. This is however in line with the current subsidisation policy.

Next Steps

The next steps for this buy-out are as follows:

1. To agree to the proposed amendment to the Trust deed and the proposed buy-out we need your individual signature as agreement - *please sign on page x of the attached document by XXX 2020.*
2. Updated quotations will be obtained from Old Mutual to proceed with the buy-out.
3. Once the proposed buy-out has been effected, your subsidy from the Trust will cease and the payments towards your medical aid contribution will be facilitated by Old Mutual in the month following the effective date of the transaction.
4. Application to amend the Trust Deed will be made once agreement has been obtained from all beneficiaries of the Trust.

If you have any questions or queries please contact XXX.

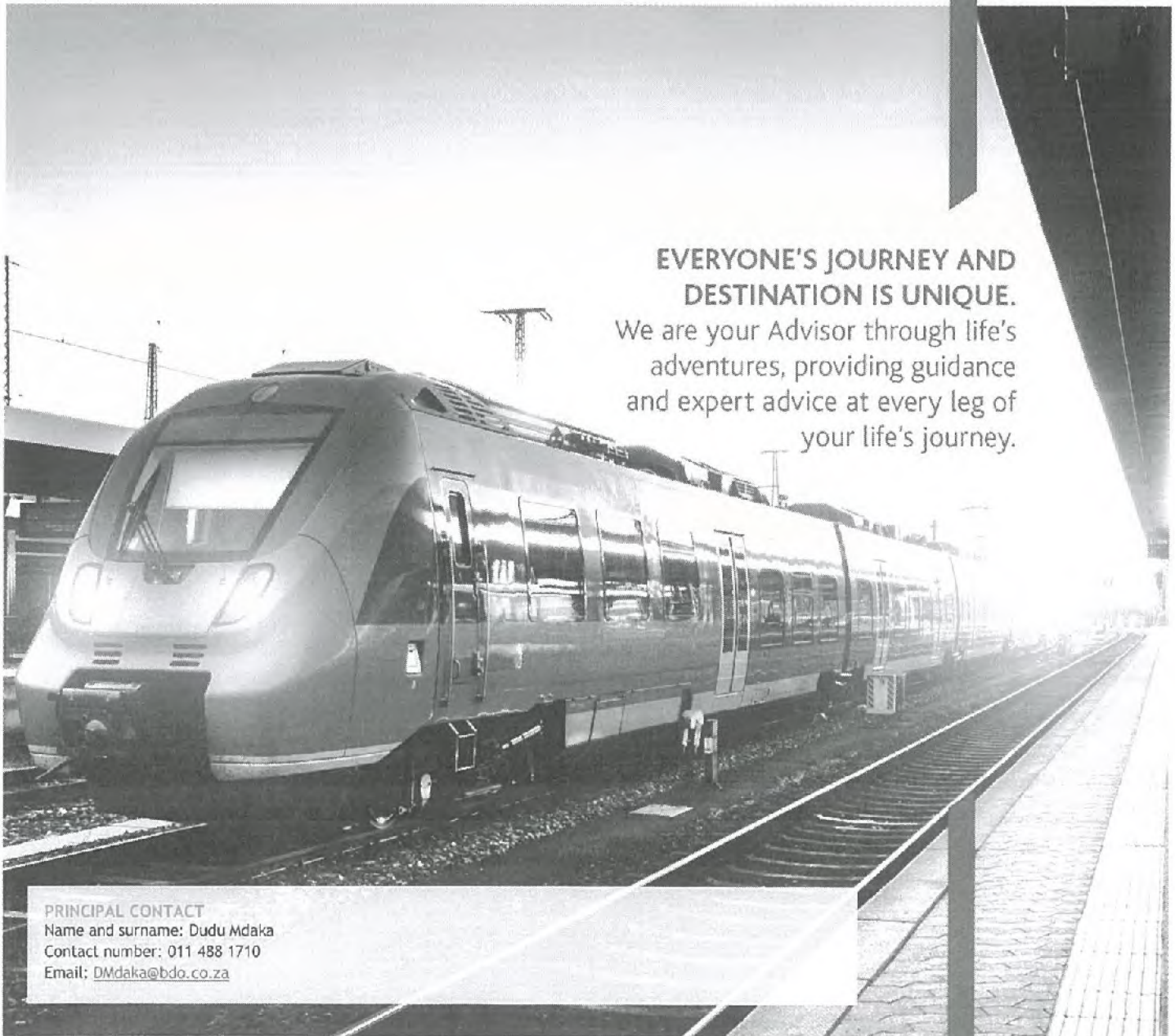
Yours sincerely,

A handwritten signature in black ink, appearing to be 'John B. [unclear]', located in the bottom right corner of the page.



EMPLOYEE BENEFITS

NOVARTIS SANDOZ SA (PTY) LTD EMPLOYEE BENEFIT PLAN



**EVERYONE'S JOURNEY AND
DESTINATION IS UNIQUE.**
We are your Advisor through life's
adventures, providing guidance
and expert advice at every leg of
your life's journey.

PRINCIPAL CONTACT

Name and surname: Dudu Mdaka
Contact number: 011 488 1710
Email: DMdaka@bdo.co.za

INTRODUCTION

At BDO Employee Benefits, we know that your employee benefits can often seem confusing. We also know that the better you understand them, the better you will be able to plan for your retirement, death or disability. That's why we've put together this leaflet for you. In it, you'll find all you need to know about how your benefits work, how you access them - and what a difference they can make in your life.

The increasing complexity of the retirement fund industry requires specialist knowledge and expertise. BDO Employee Benefits (Pty) Ltd have been appointed as the Consultants to the fund and should you require any assistance you may contact them directly.

FUND BENEFIT STRUCTURE

Due to the Retirement Reform, with effect from 01 March 2021 your Retirement fund will have a Provident Fund section and Pension Fund section. Momentum is the Insurer for both the Pension Fund and Provident fund section of your retirement fund.

If you are 55 years or older on 01 March 2021, you will not be affected by this change at all if you remain a member of the same provident fund until retirement date.

If you are below the age of 55 years on 01 March 2021 all contributions plus future growth will remain in the Provident Fund section of your retirement fund. All future contributions and growth with effect from 01 March 2021 will now accrue as pension fund savings in the Pension Fund section of your retirement fund.

Your Retirement fund is with Momentum and your risk benefits are insured with Discovery. You can view your retirement and risk benefits online. Discovery and Momentum Internet guides are available.

ELIGIBILITY

All permanent full-time employees who are between the ages of 18 and 65 years will become members of the provident fund.

CONTRIBUTIONS

The employer contributes to the retirement fund at 9% of your monthly pensionable salary as well as associated risk benefits.

You contribute 7% of your monthly pensionable salary. The Risk and Administration costs are included in the total contribution rate of 16%.

The Dread Disease cost is over and above the 16% contribution rate.

ADDITIONAL CONTRIBUTIONS

You may arrange with your employer to deduct extra contributions from your salary if you wish to add to your Retirement fund and you may contribute up to 27.5% per annum of your gross remuneration and receive a tax deduction, however you may not decrease your contribution rate. This is subject to a maximum of R350 000 per annum.

RETIREMENT AGE

Normal Retirement Age is 65. Employees have the choice however to retire from the age of 55 onwards.

TERMINATION OF SERVICES

Upon resignation or dismissal, your total share of the fund which is made up of total contributions including returns less costs will become payable. This will apply to contributions plus future growth accumulated in both the Provident fund section and the Pension fund section of your retirement fund.

You have the option to take the benefit as a cash lump sum or preserve the full provident fund and pension fund amounts accumulated up to date of termination.

Should you take it in cash, tax will be levied on this as follows:

Lump sum on Termination	Rate of Tax
R0-R25 000	0%
R25 000 - R660 000	18%
R660 001 - R990 000	27%
R990 000 +	36%

RETIREMENT

Provident Fund section - your total share of fund which is made up of total contributions less costs including returns will become payable. This may be taken as a cash lump sum or may be used to purchase a monthly pension from an insurance company.



[Handwritten signature]

Pension Fund section - if your total pension fund savings including growth are R247 500 or less, you will be able to take the full amount in cash. If your total pension fund savings including growth are R247 501 or more then you will only be able to take up to 1 (one) third in cash, the other 2 (two) thirds needs to purchase a pension from an insurance company.

Before retiring from the retirement fund, it is important to seek professional advice before selecting a retirement product. BDO Employee Benefits can assist in this regard.

If you take any money as a cash lump sum the following tax table will apply:

Lump sum on Termination	Rate of Tax
Not exceeding R500 000	0%
R500 001 to R700 000	18% of taxable amount exceeding R500 000
R700 001 - R1 050 000	R36 000 + 27% of taxable amount exceeding R700 000
Exceeding R1050 001	R130 500 + 36% of taxable amount exceeding R1 050 000

Retrenchment tax table aswell

DEATH BENEFIT

In the event of your death whilst still in the employ of Novartis SA (Pty) Ltd, a lump sum benefit equal to four (4) times your annual salary will be paid out to your beneficiaries, as per your Beneficiary Nomination Form.

In addition, your retirement monies (total contributions plus investment returns) will also be paid out to your beneficiaries.

If no beneficiaries have been nominated, the money will be paid to your Estate.

These payments will be subject to taxation.

FUNERAL BENEFIT (MOMENTUM)

Relationship	Amount
Member and Spouse	R20 000
Children aged 14 - 21	R15 000
Infant - 13	R7 500

- Benefit will cease when primary member reaches the age of 70
- The funeral benefit covers 8 people, you the member, up to 2 spouses and up to 5 children.
- All children are covered up to the age of 24, provided they studying/disabled

FUNERAL BENEFIT (DISCOVERY)

Relationship	Amount
Member and Spouse	R20 000
Children aged 15 - 21	R20 000
Children aged 6 - 14	R10 000
Children aged 0 - 5	R6 000
Stillborn (death of a foetus after 26 weeks)	R2 500

- Primary Member and Spouse covered from age 16 to below 65
- The funeral benefit covers 8 people, you the member, up to 2 spouses and up to 5 children.
- All children are covered up to the age of 24, provided they studying/disabled

EDUCATION BENEFIT

This benefit is provided over and above the death benefits listed above. It provides for the cost of your child's education in the event of your death regardless of whether your child is in nursery school or at a tertiary institution. Discovery Life will pay the education costs to the educational institution.

The type of institution attended by your child/children at the time of your death will determine the benefit rate that Discovery Life will apply. This rate covers government and private schooling as well as entrance to specific overseas universities, depending on where your child is being educated.

Benefit payments cover the following years of education:

Education	Maximum amount per child	Maximum period
Pre-school	R4 800 per month	1 year
Primary school	R8 100 per month	7 years
High school	R9 500 per month	5 years
Tertiary education (local)	R65 000 per annum	3 years
Tertiary education (international)*	\$65 000 per annum	3 years (maximum)

* Subject to an approved list set by Discovery Life

To qualify for the benefit, the following requirements must apply:

- The child must be the biological or legally adopted child of the member
- The stepchildren of the member may be covered if the following conditions are met:
 - The member must be married to the stepchild's mother or father before the date of the event giving rise to a claim
 - The member has notified Discovery Group Risk of the existence of the stepchild.
 - If the member divorces the mother or father of the stepchild, the benefit falls away for that stepchild.
- Adoption will only be considered as valid if the date of adoption or the date of application for adoption is before the date of death of the member. Adopted children must be declared to Discovery at the commencement of membership.
- A claim will only be considered if the member has not reached the benefit expiry age at time of claim.
- Discovery Group Risk will not be responsible for fees before grade 0/R.
- From a school with no fees to one with fees: a maximum increase of up to R10 900 per year, applicable for pre-school to primary school, and primary school to high school.
- The benefit payments are made annually, directly to the institution where the child is being educated.

All South African universities are included in this benefit, as well as universities and recognized institutions providing for a trade (such as plumbing or electrical). Benefit payments will cover actual education fees as well as providing an allowance of up to 40% of the fees for university residence and required books, subject to maximums set by Discovery Life from time to time. Benefit payments will not be made if the child does not attend an education facility for any reason whatsoever.

Discovery Life may alter the list of approved overseas universities from time to time. These rates are reviewed annually in accordance with the increase in educational costs.

DISABILITY BENEFITS

If you are disabled as a result of sickness or accident and the insurers of the benefit decide, based on the medical evidence provided, that you are unable to return to the job you worked in immediately prior to you becoming disabled, you will receive a monthly disability income of 75% of your salary, subject to certain maximums.

This benefit will commence three (3) months after you become disabled ("the date of disability") and is subject to certain limitations. The benefit escalates at 5% per annum is payable until you recover, die or reach the age 65.

This benefit covers your own occupation for the first 12 months and your own or similar occupation thereafter. Your contributions to the retirement fund will continue to be paid.

MEDICAL PREMIUM WAIVER

For the first 12 months that you receive a monthly disability benefit, a portion of your medical premiums will be paid by Discovery Life to the applicable Medical Scheme.

For members on Discovery Health, the full medical costs will be paid. The number of children covered by this benefit is not subject to any maximum. Adult Dependents (including children aged 18 years or older) are excluded from this benefit.

The payment allows for payment increases in the same month as at the same rate of increase that the medical aid increases contributions for its members, subject to a maximum of 20% per annum.

For non-Discovery Health members, the monthly payments will be as follows:

	Contribution	MSA	Total
Primary member	R3 339	R1 187	R4 526 per month
Spouse	R2 554	R 852	R3 406 per month
Per child	R1 331	R 504	R1 835 per month

These benefits are payable for a maximum period of 12 months.

SEVERE ILLNESS / DREAD DISEASE BENEFIT

This benefit provides a lump sum if the insured is diagnosed with one of the defined severe illnesses. A severe illness is an illness that affects a person's lifestyle in such a way that his/her ability to function normally is limited. Severe illnesses that are covered include: cancer, nervous system, heart and artery, eye, ear, nose and throat, connective tissue, endocrine and metabolic diseases, advanced AIDS, gastrointestinal, respiratory disease.

The benefit amount is 1 x annual salary up to a maximum of R2.2 million and for the Early Cancer benefit the maximum is R110 000 per life. The benefit is designed so that claim payments are proportional to the severity of the illness itself.

CHILDREN'S DREAD DISEASE BENEFIT

All Children up to the age 18 are covered for this benefit up to a maximum of 10% of the member's sum assured. You can also purchase additional risk cover. Please contact your People and Organisation department.

All risk may be subject to medical underwriting.

INVESTMENTS

The Board of Management, in consultation with BDO Employee Benefits, has put together an investment strategy based on member demographics. The approach followed is age-related - as members get older their needs and risk analysis changes.

As a member, you may contact BDO Employee Benefits regarding your investment options. Your allocated portfolio will be enclosed with your annual benefit statement.

CONCLUSION

It is very important that you monitor your Risk benefits in conjunction with your personal insurance. A Financial Needs analysis should be conducted by you to ensure that the correct cover is in place. You need to understand what can be expected from the risk benefits and make provision for additional risk benefits in your personal capacity if necessary.

You must ensure that Nomination of Beneficiary forms are updated when changes in personal circumstances, such as childbirth or divorce, occur. This is done on an annual basis, but should you wish to amend these forms in the interim you may do so by contacting your P&O department.

IN THE EVENT OF ANY ASSISTANCE OR ADVICE REQUIRED, THE PRINCIPAL CONTACT WILL BE:

- Duduzile Mdaka: Dmdaka@bdo.co.za



This booklet is a summary and not a legal document. In the event of a dispute, the Rules of the Scheme will prevail.

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