**THE SUPREME COURT OF APPEAL**
**REPUBLIC OF SOUTH AFRICA**

# JUDGMENT

Case No: 56/09

RAJWANTHA SOOKHDEO MUNGAL Appellant

and

OLD MUTUAL LIFE ASSURANCE CO SA LTD Respondent

TREVOR VERNON FREEMAN Appellant

and

OLD MUTUAL LIFE ASSURANCE CO SA LTD Respondent

**Neutral citation:** *Mungal v Old Mutual* (56/09) [2009] ZASCA 141 (20 November 2009)

**Coram:** STREICHER, NUGENT, MAYA, SNYDERS JJA and LEACH AJA

**Heard:** 6 NOVEMBER 2009

**Delivered:** 20 NOVEMBER 2009

**Summary:** **Determination made by Pension Funds Adjudicator – whether adjudicator had jurisdiction to consider the complaint – endowment policy issued by an insurer - value upon early termination.**

**ORDER**

On appeal from: High Court at Durban (Sishi J sitting as court of first instance)

The appeal in each case is dismissed.

**JUDGMENT**

NUGENT JA (STREICHER, MAYA, SNYDERS JJA and LEACH AJA concurring)

[1] Chapter VA of the Pension Funds Act 24 of 1956 creates the office of the pension funds adjudicator, whose function is to dispose of complaints relating to pension funds in a 'procedurally fair, economical and expeditious manner'.[1] After investigating a complaint the adjudicator may 'make the order which any court of law may make', which is 'deemed to be a civil judgment'.[2] Any party who feels aggrieved by a determination of the adjudicator may apply to an appropriate high court for relief in which event the high court 'may consider the merits of the complaint . . . and may make any order it deems fit'.[3] It also follows from s 30P(3) that in considering the matter the court may take further evidence.

[1] Section 30D.
[2] Section 30E read with s 30O.
[3] Section 30P.

[2] In this case Mr Mungal, who was a member of the Protektor Preservation Provident Fund, and Mr Freeman, who was a member of The South African Retirement Annuity Fund, both of which are ‘pension fund organizations’ as contemplated by the Act, lodged separate complaints with the adjudicator that were directed at Old Mutual Life Assurance Company (South Africa) Limited. The complaints had much in common and the adjudicator dealt with them together. After considering the complaints the adjudicator made certain orders against Old Mutual and in particular he ordered Old Mutual to pay to Mungal the sum of R29 592 and to Freeman the sum of R46 635.

[3] Old Mutual was aggrieved by the determinations. Invoking the provisions of s 30P it applied in each case to the high court at Durban for orders setting aside the respective determinations and for further declaratory relief. The two applications were heard together by Sishi J and both succeeded. Mungal and Freeman now appeal with the leave of the court below.

[4] The funds are designed to accommodate employees to whom a benefit has become payable in consequence of terminating their membership of another provident fund. They are ‘underwritten funds’ by which is meant that their only assets are claims under long-term insurance contracts. When a person joins the fund the moneys that he or she received from the earlier fund will be used to pay the premium on an insurance policy taken out by the fund. The parties to the policy will be the fund and the insurer and the member will be the ‘life assured’. Benefits that accrue under the policy are

paid by the insurer to the fund and the moneys are then available to pay to the member the benefits to which he or she is entitled under the Rules. The policies that were taken out when Mungal and Freeman joined their respective funds were both issued by Old Mutual.

[5] Old Mutual is also the administrator of each of the funds. While the funds are under the overall control of boards of trustees the responsibility for their administration was assigned by the trustees to Old Mutual under what was called a Fund Administration and Trustee Services Contract. The agreement requires, and authorises, Old Mutual to perform all the functions that generally attach to the administration of such a fund, which are specified in some detail in an annexure to the agreement.

[6] In these proceedings Old Mutual says at the outset that the adjudicator was not entitled to make any orders against it because the complaints by Mungal and Freeman do not fall within the definition of a 'complaint' in the Act. If there was to be a complaint at all, it was submitted on behalf of Old Mutual, it ought properly to have been directed to the Ombudsman for Long-term Insurance.[4] That objection was not raised when the matter came before the adjudicator but that is not material. If the adjudicator had no jurisdiction in the matter then that is a sufficient and proper basis upon which to set aside his determination.

[7] A 'complaint' is defined in the Act to mean, amongst other things

'a complaint … relating to the administration of a fund … and alleging-

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[4] The office of the Ombudsman for Long-term Insurance has been created pursuant to the Financial Services Ombud Schemes Act 37 of 2004.

(a) that a decision of the fund or any person purportedly taken in terms of the rules was … an improper exercise of its powers;

(b) that the complainant has sustained or may sustain prejudice in consequence of the maladministration of the fund by the fund or any person, whether by act or omission;

(c) that a dispute of fact or law has arisen in relation to a fund between the fund or any person and the complainant; or

(d) …

but shall not include a complaint which does not relate to a specific complainant;'

[8] The complaints in this case were conveyed to the adjudicator in letters written by Mungal and Freeman. Needless to say they were not framed in the language of the definition but I do not think the form in which a complaint is made is critical. Chapter VA clearly contemplates complaints being made by lay persons who are not expected to have studied the definition with legal expertise and to have framed their complaints accordingly. More important than the form in which the complaint is expressed is the substance of the complaint. If the various elements of the definition are inherent in the complaint that seems to me to sufficiently bring it within the terms of the definition notwithstanding that they have not been expressed in those terms.

[9] The complaints were that Old Mutual refuses to pay moneys that are said to be due to the respective funds under the policies. But they might just as well have been couched as complaints that Old Mutual refuses to claim the moneys on behalf of the funds. Because the corollary of its refusal, as insurer, to acknowledge the validity of the claims, is a refusal, as administrator, to perform its duty to take steps to recover the claims. And for so long as moneys that are due to the funds are not claimed the right of its

members under the Rules to be paid pension benefits will be thwarted because the members have no independent legal rights against the insurer under the policies. If moneys are payable under the policies I do not see why the members should be told to forego the pension benefits that will accrue to them if the moneys are paid and to confine themselves to complaints against the insurer to the Ombudsman for Long-term Life Assurance.[5]

[10] Seen in that context the complaints against Old Mutual are quite capable of being construed as complaints 'relating to the administration of the funds'. Clearly the complainants will be prejudiced if the moneys are due but are not recovered. It also seems to me that the refusal of the administrator to acknowledge the validity of the claims and to take the necessary steps to pursue them is capable of constituting 'maladministration of the fund'. The disputes in these cases are certainly 'in relation to the fund' and are between the complainants and the administrator of the funds as much as between them and the insurer. Those allegations were not made in terms in the letters that were written to the adjudicator but they are all inherent in the nature of the complaint.[6]

[11] On that approach it might be that the order made by the adjudicator ought to have been directed at compelling Old Mutual, as administrator of the funds, to acknowledge that the claims are valid and to press for their recovery, but that relates to the nature of the orders that were made rather than to the nature of the complaints. Where the insurer is not also the

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[5] Although the members are not contracting parties complaints may be made to the Ombudsman for Long-term Insurance by the life assured under the policy.

[6] We were referred in argument to the analysis of the definition by Josman AJ in *Armaments Development and Production Corporation of SA Ltd v Murphy* 1999 (4) SA 755 (C) but I do not think that analysis is helpful on the facts of this case.

administrator there might be no purpose served by considering a complaint of this nature if the insurer is not willing to submit to the conclusions reached by the adjudicator. But where the insurer is also the administrator those conclusions could hardly be altogether ignored, particularly if they were to be confirmed by a court in proceedings under s 30P. Those are matters, however, that relate to whether an order is capable of being made that will be effective in resolving the complaint, and not to whether the adjudicator has jurisdiction to consider the complaint. In my view there is no merit in the objection and I turn to the merits of the complaint.

[12] There is no need to visit the Rules of the respective funds. The complaint is directed at the collection of moneys that are alleged to be due to the funds. Whether those moneys are indeed payable depends upon the construction of the relevant policies.

[13] The policies that were issued to the respective funds were both endowment policies with Mungal and Freeman respectively being the ‘life assured’. The nature of an endowment policy is that in return for a premium the insurer undertakes to pay to the policyholder a sum of money on a fixed date in the future or a sum of money (not necessarily the same amount) upon death of the life assured. In effect it is a fixed investment.

[14] Affidavits were deposed to by two actuaries explaining the actuarial and investment principles upon which policies of that nature are modelled. Needless to say the rights and obligations of the parties to a policy are determined by the terms of the particular policy and not upon the model on which it purports to be founded. But that evidence is nonetheless helpful to

understanding the various provisions of the policies. On matters of actuarial and investment principle there is no material difference between the actuaries. Such differences as there are between them are attributable to the construction that each places upon the policies.

[15] Endowment policies are linked directly or indirectly to a particular portfolio of investment assets. The premium is invested in the portfolio and the returns on the investment accrue to the benefit of the policyholder.

[16] Some policies are linked directly to the portfolio in that the value of the portfolio is attributed directly to the value of the policy. The benefits that accrue to the policyholder are thus determined by the value of the portfolio at that time. The drawback of such a policy is that the value of the portfolio will fluctuate from day to day according to the state of the market and it is uncertain what its value will be at the date the benefit accrues. The policyholder is in much the same position as an owner of shares who sets a date upon which the shares must be sold irrespective of their market value on that date.

[17] Insurers counter that drawback by offering 'smoothed bonus' policies. Policies of that kind are only indirectly linked to the value of the investment portfolio. The policies are managed in such a way that fluctuations in the value of the investment portfolio are smoothed out when that value is attributed to the value of the policies. In that way the value of a policy on the date that the benefits accrue can be predicted with some degree of certainty. The aim of such a policy is to ensure that there is a positive return on the

policy even if the value of the portfolio is depressed at the time the benefit accrues.

[18] Smoothing the effects of fluctuations in the value of the portfolio is achieved by allocating to the policies during periods of growth in the value of the portfolio only a portion of that growth and allocating the balance to a reserve account (sometimes called a 'stabilisation reserve account'). The reserve may then be drawn upon to allocate past growth to the policies at times when there is little or negative growth in the value of the portfolio. In that way the value of the policies will follow the trend of the portfolio rather than its fluctuations.

[19] The manner in which growth in the value of the investment portfolio is allocated to the policies is by periodically declaring 'bonuses'. It is usual for such declarations to be made annually in arrear, though provisional interim bonuses might be declared periodically through the course of the year.

[20] The allocation of growth to the policies is an exercise in accounting and does not involve the realisation of assets. A bonus that has been declared and credited to the policies is thus capable of being revoked merely by reversing the relevant accounting entries. To assure policyholders that that will not occur before the benefits under the policies accrue to the policyholders insurers usually undertake that at least a portion of a bonus that has been declared will not be revoked. The portion that may not be revoked is commonly called a 'vesting bonus' and the portion that may be revoked is called a 'claim bonus'. An insurer might offer even greater

certainty by guaranteeing that the policies will have a certain minimum value at the time the benefits accrue. Where that is done the insurer is effectively guaranteeing that bonuses will be declared over the life of the policies in amounts that are sufficient to maintain a minimum level of growth.

[21] That process of attributing the growth of the portfolio to the policies is managed through an account for each policy that is usually known as an 'accumulation account'. The accumulation account will be credited with the premium (or premiums) and with bonuses as and when they are declared, and will be debited with fees and charges that become due to the insurer. The balance on the accumulation account at any time (which will always be a credit when there is a single premium) represents the value of the policy at that time.

[22] The two policies that are now in issue, so far as their provisions are now material, are substantially the same, but they differ in some of their detail (though the differences are mainly confined to terminology). For convenience I will confine myself first to the Mungal policy.

[23] The commencement date of the policy was 1 January 1998 and it was to endure until 1 January 2010 (the maturity date). A single premium of R193 560.05 was payable on commencement. The 'glossary of terms' in Part 2 of the policy records, under the heading 'Accumulation Account', that

'[e]ach policy is administered through its Accumulation Account which is increased by premiums and investment returns, and reduced by expenses and benefit charges'.

The 'investment returns' that are referred to are the bonuses that are declared from time to time, representing that portion of the growth in value of the portfolio that has been attributed to the policy. The 'expenses and charges' that may be debited to the account are specified elsewhere in the policy.

[24] The general provisions in Part 3 record that

'Old Mutual will declare annual vesting and claim bonuses, which will be added to the balance in the Accumulation Account'. The vesting bonuses, once declared, can never be removed in respect of maturity and death claims. The claim bonus may be reduced or removed altogether at any time before it becomes due as part of a benefit payable under this policy'.

The policy guarantees

'an average … growth rate of 0.35% per month … up to the date of any maturity, death or disablement claim'.

The guaranteed value of the policy upon maturity is expressed in monetary terms to be the sum of R319 076. The guaranteed value upon death or disablement (the latter event is not relevant for present purposes) is naturally not capable of being calculated in advance but is calculable once the event has occurred.

[25] The dispute in this case arose because Mungal elected to terminate the policy before it had run its full course (which is colloquially called 'surrendering' the policy) after being informed of the amount he could expect to receive if he surrendered it (he was given contradictory figures at various times but that is not material). At that time the credit balance on the accumulation account was R295 730.71. Old Mutual paid R266 157.64 to the fund – which was 90% of the credit balance – and the balance of that amount after deducting tax was paid by the fund to Mungal.

[26] The reason that the value of the policy as reflected in the accumulation account was reduced by 10% requires brief explanation. By the nature of 'smoothed bonus' policies their value as reflected in the accumulation accounts will seldom correspond with the market value of the portfolio. When the market for the portfolio is buoyant the value of the policies might be lower than the value of the portfolio and the converse might occur when the market is depressed. To pay the full value of a policy when it exceeds the related value of the portfolio is necessarily detrimental to the remaining policyholders because that excess will need to be recovered ultimately from future growth in the portfolio. Payment of the full value of a policy when it is lower than the related value of the portfolio will have the opposite effect on the body of policyholders. Maintaining bonuses and the reserve at an appropriate level serves in the ordinary course to balance those relative gains and losses. But it is self evident that an insurer is able to maintain the appropriate balance only if the time at which benefits will become payable under the pool of policies is capable of being predicted.

[27] Where the value of a policy exceeds the related value of the portfolio, and the policy is terminated before it has run its term, it is common for insurers to pay to the policyholder only the true value of the policy, so as to ensure that the early termination is not detrimental to the general body of policyholders.[7] The tool that they use to evaluate its true value at the time of termination is a factor that they call a 'market adjuster'. A market adjuster is merely a percentage by which the value of the policy as reflected in the

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[7] Where the situation is reversed the value of the policy as reflected in the accumulation account will ordinarily be paid and the difference between that and the related value of the portfolio will accrue to the benefit of the remaining policyholders.

accumulation account will be reduced so as to bring it in line with the value of the portfolio. The percentage that will be applied is actuarially calculated with reference to the current value of the portfolio and will fluctuate from time to time according to the state of the market. At the time the Mungal policy was terminated the market adjuster that was being applied by Old Mutual stood at 10% and the balance on the accumulation account was reduced accordingly.

[28] The reduction of the value of the policy was the source of Mungal's complaint. He said that the policy had no provision specifically allowing for the application of a market adjuster and Old Mutual was thus obliged to pay him the full credit balance on the accumulation account. The adjudicator approached the matter in the same way and searched the policy to see if it contained such a provision. Having found none he declared that Old Mutual was 'not entitled to apply the market level [adjuster] to reduce the complainant's benefit' and on that basis ordered the deducted portion of the value to be paid.

[29] That approach was also adopted in the opinions expressed in the affidavit deposed to on behalf of Mungal by his attorney, in the opinions expressed by his actuary, and in the submissions that were made on his behalf before us, but it misdirects the enquiry. It assumes a priori that the policyholder is ordinarily entitled to the benefits of the policy – the credit balance on the accumulation account – without interrogating whether that assumption is correct.

[30] The benefits that are conferred by the policy appear from the insuring clause in which Old Mutual 'undertakes to pay the benefits, as set out in Part 1 of this policy document …'. Only two benefits are provided for in that part of the policy.[8] One is a benefit that is contingent upon the policy enduring to its maturity date. The other is a benefit that is contingent upon the death of the life assured. In both cases the benefit that accrues when that contingency occurs is an entitlement to the credit balance on the accumulation account (which is guaranteed to be not less than a specified amount upon maturity, and upon death to be an amount that returns at least 0.35% on average per month until the date the benefit is claimed).[9]

[31] In its terms the policy exists to provide policyholders with the benefits that are to be had from fixed-term investments (the fixed date being maturity or the death of the life assured). It would be most surprising if the returns that are promised on a fixed-term investment were to be payable to investors who terminate the policy before the term has expired. Fixing a date for payment of the benefit, whether that date be maturity or death, would be altogether superfluous. It would also be surprising if an investment scheme that is actuarially modelled upon the predicable termination of policies were to have been intended to apply even to unpredictable early terminations.

[32] What is overlooked by the argument advanced on behalf of the appellants (and by the determination that was made by the adjudicator) is

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[8] The benefits are expressed in Part 1of the policy in the following terms: 'On survival of the Assured to 1 January 2010 the balance in the Accumulation Account is payable, with a guaranteed amount of R319 076. On the death of the Assured before I January 2010 the balance in the Accumulation Account is payable.'
[9] Although not expressed as such in the definition of the benefit that is the effect of the guarantee in the general provisions that there will be 'average … growth of 0.35% per month … up to the date of any … death claim'.

that the entitlement to be paid on early termination is not one of the 'benefits' of the policy. It is no more than a separate entitlement that arises if the undertaking to pay benefits is terminated before the benefits accrue. That is clear from the text of the policy alone, quite apart from the anomalies that would otherwise arise.

[33] While the policy provides in terms for the payment of the credit on the accumulation account (the benefit that the policy promises) upon the occurrence of one of the specified contingencies – maturity or death of the life assured – it provides for what is payable upon early termination in altogether different terms. If that event occurs Old Mutual is obliged to pay the 'surrender value' of the policy. What that means is expressed in the general provisions of the policy as follows:

'The amount of the surrender value will be determined by Old Mutual at the time of surrender and will take into account disinvestment costs, the recovery of unrecouped expenses, any debts against the policy and legal limits in force'.

[34] It was submitted on behalf of Mungal that the proper meaning of that clause is that upon surrender the policyholder is entitled to be paid the full value of the policy as reflected in the balance on the accumulation account, with the deduction only of such disinvestment costs, unrecouped expenses and debts as are determined by Old Mutual (none of those amounts were deducted in this case). Counsel could direct us to nothing in the text of the policy to support that construction of the policy and there is none. The plain meaning of the language is that Old Mutual will determine the value of the policy at the time of termination – not merely the amount of the costs,

unrecouped expenses and debts. Those are stated in terms to be no more than amounts that may be taken into account in determining the value.

[35] It might be that in particular cases Old Mutual will determine that the amount that is payable is the credit on the accumulation account. But then that amount is payable because it is the amount that Old Mutual has determined to be the surrender value. And while the amount payable is usually determined by applying the market adjuster to the credit balance on the accumulation account that is only because the credit balance provides a convenient starting point for making the determination.

[36] In my view the policy means just what it says. Upon early termination the policyholder is entitled to an amount that is determined by Old Mutual at that time (which may or may not equate to the credit on the accumulation account). I might add that we are not called upon to decide whether any determination made by Old Mutual would be open to contestation and judicial scrutiny. It is not disputed that the amount was determined in this case in accordance with general insurance and actuarial practice.

[37] Freeman's appeal can be disposed of rather more briefly. The policy in that case commenced on 1 November 1994. Benefits were payable upon retirement date or death. The selected retirement date was 1 November 2012. The benefits were described in the policy as follows:

'On survival of the Assured to 1 November 2012 the balance in the Accumulation Account, with a minimum guaranteed amount of R908 385, becomes available to purchase an annuity. On the death of the Assured before 1 November 2012 the balance in the Accumulation Account becomes available to purchase an annuity'.

[38] The general provisions of the policy do not provide for surrender but provide instead for the policyholder to change the date of retirement (thereby terminating the policy by bringing it to earlier maturity) in the following terms:

‘The Assured also has the option, subject to the Rules of the Fund, legislation in force at the time and the conditions imposed by OLD MUTUAL at the time, to change the date of retirement.’

[39] In August 2003 Freeman advised Old Mutual, after he had been informed of the amount that would be paid, that he wanted to change the date of retirement to the then date (which would ordinarily then have entitled him to the retirement benefit). Old Mutual acceded to his request but was willing to pay only R886 072.72. Once more that amount was arrived at by applying the market adjuster (which was set at 5% at that time) to the credit balance on the accumulation account, and it led to the same complaint being made. Once more the adjudicator made an order declaring that Old Mutual ‘was not entitled to apply the market adjuster to the balance in the Accumulation Account to determine [the] benefit on the ground of [the advanced] retirement date’.

[40] What occurred in substance is that Old Mutual was willing to advance the retirement date only on condition that Freeman would not then be entitled to the ordinary retirement benefit but only to the value that Old Mutual attributed to the policy. The policy makes it perfectly clear that Freeman was entitled to change the date of retirement only if he accepted that condition. There is no basis for construing the policy to mean that he

was entitled to change the date of retirement unilaterally and continue to be entitled to the retirement benefit that would have accrued had that been the date of retirement initially.

[41] Permeating all the arguments that were advanced on behalf of the appellants at various times is the fallacy that the declaration of a bonus vests in the policyholder an unconditional right to receive the bonus. The right that vests in the policyholder is one that is conditional upon a defined event occurring. The accumulation account is not to be likened to an ordinary creditors' account. It is an account that records contingent liabilities. And the contingencies that will give rise to liability – at least in this case – do not include early termination of the policy.

[42] For these reasons the court below was correct in setting aside the adjudicator's determinations and the appeals must fail. Because the case has wider implications Old Mutual has graciously not sought the costs of the appeal.

[43] The appeal in each case is dismissed.

R W NUGENT
JUDGE OF APPEAL

APPEARANCES:

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