

4 December 2006

PRACTICE NOTE

INTEREST ON LATE PAYMENTS

1. Rule 3.2.6 reads:

3.2 *“The determination aforesaid may be to:*

3.2.6 *order a subscribing member, in addition to any other recommendation or determination made, to pay interest to a complainant on the pertinent sum at a rate and from a date that is considered to be fair and equitable in the circumstances.”*

2. There are three grounds on which the office can order an insurer to pay interest:

- (a) mora interest at the legal rate of 15.5% per annum;
- (b) the LOA protocol in respect of the payment of death and disability benefits;
- (c) fair and equitable interest.

3. Mora Interest

3.1 Mora interest, at the legal rate of 15.5% per annum, is payable when a determined or objectively determinable sum of money is to be paid by the insurer to a complainant on or before a determined or objectively determinable date, and it is not paid by that date.

3.2 Such interest represents damages for breach of contract – the breach (*mora debitoris*) being the failure by the debtor (e.g. the insurer) to effect payment in terms of the contract to the creditor (e.g. the policyholder or nominated beneficiary). Since it would be unfair to hold the debtor liable for damages when he did not know exactly when he was supposed to pay, the exact date must be fixed (e.g. the maturity date on a policy) or must be objectively ascertainable (e.g. 5 years after inception date of a policy commencing on receipt of the first premium) and the debt must be due and enforceable. Where, for example, a policy is payable simply on the death of the insured life, the time of payment is not sufficiently defined for mora to commence on the date of death.

- 3.3 The date can be stipulated in the contract itself (*mora ex re*) or, when the contract is silent as to when payment is to be made, the creditor must place the debtor in mora by giving him advance notice e.g. a letter of demand that payment is to be effected by a certain date (*mora ex persona*). The period allowed in the notice must be reasonable but it is conceivable that a request for the immediate payment of a money debt may be reasonable. (See Van der Merwe et al Contract 2nd edition 331-318).
- 3.4 Where the office rules against an insurer that payment is to be made to a policyholder or beneficiary, it should at the same time stipulate a date for such payment, from which date mora interest will then accrue.
- 3.5 *Circumstances exonerating the debtor.*
- 3.5.1 In particular the debtor cannot be in *mora debitoris* when the creditor is in *mora creditoris*. A debtor is obliged, speaking generally, to render performance in terms of the provisions of the contract. When such performance requires the co-operation of the creditor in order to render it, as in the case with payment, the performance constitutes a bilateral consensual act. Thus a debtor cannot pay if he cannot locate his creditor on the day of payment or if the creditor fails to comply with certain prescribed contractual or legislative formality. For as long as the creditor fails to render his required co-operation the debtor is not in breach and mora interest will accordingly not accrue against him.
- 3.5.2 When the contract itself is silent on the point, it is the duty of the debtor to call upon the creditor to render such co-operation as is required to enable the debtor to perform fully and timeously. When this cannot be done on the day itself it must be done in advance of the day. When the preparatory work is thus required to enable the creditor to render his co-operation such preparatory work must be completed by the debtor on or in advance of the day stipulated for the payment. Where the pre-condition consists of a request to furnish certain information, such as bank details, such a request must therefore be made either before or at the latest on the day on which payment is to be made so as to ensure timeous payment.

3.5.3 It stands to reason that a debtor may not delay his own duty to pay by delaying the request for such co-operation without which payment cannot be effected. So for instance, where the insurer cannot effect payment without having been furnished with the banking details of the creditor, it is the duty of the debtor to require such details in advance of the date for payment so as to enable the debtor to comply with its contractual obligations. (See Van der Merwe et al 343-345.)

4. The LOA Protocol

4.1 The source of this form of interest was the LOA's circular Number 86/2003, of 29 May 2003, a copy of which is attached.

4.2 See too our 2004 Annual Report 18-19.

4.3 The rationale for this form of interest is that the insurer is basically enriched at the expense of the complainant, having had the benefit of funds to which the insured or the complainant, as the case may be, were in truth entitled. It follows that the insurer should not be held liable on this basis or, at least not to the extent of the rate specified by the LOA protocol, if the insurer was not enriched to that extent.

4.4 Hence the LOA protocol is subject to the rider i.e. that the insurer is allowed to show that the Standard Bank rate on deposits is in excess of the value of the benefit it derived from being possessed of the assets. Where the insurer can satisfy the office that the money due, while in its hands, earned a lesser rate of interest than the stipulated rate of interest, our office would apply the lesser rate. A recent example is where the insurer explained that it "parked" the money in a special account which generated a lesser rate of interest than the money market or the Standard Bank rate.

5. Equitable Interest

5.1 The office has on occasion, when the circumstances made it fair to do so, extended the principle of the LOA protocol to instances other than the payment of death or disability benefits.

5.2 Preconditions for this extension would be:

- (a) the payment of a specific sum of money ("the fund") due by the insurer to the insured or complainant, whether by a specific date or some time in the future;

- (b) the earmarking of the fund for payment to the party entitled thereto;
- (c) a benefit by the insurer of income from the fund.

5.3 In addition it is conceivable that there may be other instances, not covered under any of the previous categories, where it would be fair and equitable to award interest against the insurer and in favour of the party entitled to the payment. In each instance it would be necessary for the office to enquire what a fair and equitable rate would be and from what date such interest is to be paid.

5.4 *Refund of premiums*

Whenever a complainant is entitled to a refund of premiums paid and the question arises whether, and if so at what rate, interest is to be added, it may be a relevant factor that the complainant has had the benefit, albeit only potentially, of risk cover or of a rise in the equity market during the period for which interest is being considered.

Examples would be where the complainant has cancelled the contract because of the insurer's misrepresentation or where the contract is set aside for lack of consensus in circumstances where the complainant could in the alternative have enforced the contract by invoking the reliance theory – i.e. where the contract, broadly speaking, is "voidable" at the complainant's election.

In such circumstances it is only fair that in order to achieve mutual restitution, allowance should be made for the potential benefit the complainant enjoyed in the interim. One way of doing so would be to reduce the rate at which the interest which is to be added is pitched.

**PMN/GR
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