IN THE HIGH COURT OF SOUTH AFRICA

(WITWATERSRAND LOCAL DIVISION)

CASE NO: 2008/02548

In the matter between:

THE REGISTRAR OF MEDICAL SCHEMES Applicant

and

SOLVITA MEDICAL SCHEME Respondent

J U D G M E N T

MBHA, J:

[1] The applicant seeks an order, amongst others:

1.1 approving the bringing of this application as contemplated in section 53(2) of the Medical Schemes Act 131 of 1998 ("*the Act*");

1.2 that the respondent be placed under a winding-up order in terms of section 53 of the Act read together with the provisions of Chapter XIV of the Companies Act 61 of 1973.

[2] This application served in the urgent court and, having listened to full argument, on 16 January 2009 I made an order:

2.1 Granting judgment in favour of the applicant in accordance with the prayers 1, 2 and 4 of the Notice of Motion; and

2.2 That reasons for my judgment would follow in due course. Such reasons follow hereinafter.

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[3] At the commencement of the hearing, three points *in limine* were raised by the respondent, namely:

3.1 that as the applicant had failed to obtain the "*approval of the High Court*" prior to making this application in terms of section 53(2) of the Act, for the winding-up of the respondent, the application ought to fail by reason of such failure;

3.2 that the applicant failed to timeously deliver its replying affidavit in answer to the allegations contained in the respondent's answering affidavit;

3.3 that the application is not urgent; and

3.4 that the applicant omitted to give due notice to certain interested parties like the Solidarity Unions and to members of the respondent and their beneficiaries.

[4] I was requested by counsel to forthwith rule on the first point *in limine*, i.e whether applicant was in breach of section 53(2) of the Act.

[5] After hearing argument, I dismissed the specific point *in limine* raised. Although I gave full reasons for my decision, I nonetheless deem it necessary to briefly summarise them again in this judgment:

5.1 Section 53(2) of the Act reads as follows:

> "*53. Winding-up*
>
> *…*
>
> *(2) The Registrar may with the concurrence of the Council and with the approval of the High Court, make an application under section 346 of the Companies Act, 1973, for the winding-up of a medical scheme if he or she is satisfied that it is in the interests of the beneficiaries of that medical scheme to do so.*"

5.2 In support of the argument that the applicant ought to have sought prior approval by this Court for lodging the present application, counsel for the respondent sought to rely on the provisions of sections 51(2) and 51(5)(e) of the Act, which read as follows:

"*51.*

(2) A medical scheme may, in regard to itself, apply to the High Court for an order contemplated in paragraph (b), (d) or (e) of subsection (5), if the medical scheme is of the opinion that it is desirable, because the medical scheme is not in a sound financial condition or for any other reason that such an order be made in regard to the medical scheme: Provided that a medical scheme shall not make such an application except by leave of the High Court and the court of appeal shall not grant such leave unless the medical scheme has given security to an amount specified in the Rules of the High Court for the payment of such costs.

…

(5) Upon any application in terms of the preceding subsections, the High Court may …

(e) order that the whole or any part of the business of the medical scheme, be wound up in terms of section 53.

[6] A simple reading of section 53(2) shows that the Registrar (of medical schemes) may with the approval of the High Court make an application for the winding-up of a medical scheme if he or she is satisfied that it is in the interest of the beneficiaries of the scheme to do so. Otherwise there is no compulsion whatsoever on the Registrar to first seek the approval of the High Court. As I will show later in the judgment, the aspect of the interest of beneficiaries was not, in any event, the only basis upon which the Registrar sought the liquidation of the respondent.

[7] Similarly, the attempt to rely on sections 51 (2) and (5) cannot succeed. A simple reading of the latter provisions shows that the submission is misplaced. Section 51(2) clearly provides for instances where a medical scheme seeks to make an application for its own winding-up. The section contains a clear proviso to the effect that in such instances a medical scheme shall not make such application except by leave of the High Court. This situation does not apply to this case.

[8] Counsel for the respondent sought to rely on the decision in *Jacobs en Andere v Polmed Medical Fund en Andere* 2001 (2) SA 502 (TPA), where Daniels J found that leave of the High Court must be obtained before an application in terms of section 51 of the Medical Schemes Act 131 of 1998 can be issued and served. As I have already pointed out, section 51 does not apply to this case.

[9] There was thus no need for the applicant in this case to have first sought the court's approval before launching this application

[10] The next point *in limine* raised which is the applicant's alleged failure to timeously deliver its replying affidavit, cannot succeed. The complaint is that the respondent's answering affidavit was served on the applicant on 13 December 2008 and that the applicant filed its replying affidavit together with the annexures, on the respondent on 12 January 2009.

[11] It has to be borne in mind that the matter was enrolled for hearing on 15 December 2008 and the applicant was ready to proceed with the matter on that day. However, the matter was postponed by agreement between the parties after the respondent had made certain undertakings, inter alia to furnish a guarantee to the applicant by no later than 31 December 2008.

[12] It is trite that no guarantee was ever furnished. This, together with other reasons, necessitated that the matter proceed further in January 2009. It therefore became incumbent upon the applicant to file its replying affidavit. In any event a 17 day delay is not in my view unreasonable. In the circumstances this point raised is similarly dismissed.

[13] I decided that the last point *in limine* raised relating to urgency can best be dealt with together with the merits of this case. Two issues will thus be treated together. I now proceed to deal with the merits of the application.

[14] Section 53(1) of the Act provides that:

> "*Chapter XIV of the Companies Act, 1973 (Act No. 61 of 1973), shall, subject to the provisions of this section and with the necessary changes, apply in relation to the winding-up of a medical scheme and in such application the Registrar shall be deemed to be a person authorised by section 346 of the Companies Act, 1973, to make application to the High Court for the winding-up of the medical scheme.*"

[15] It is common cause that the deponent to the founding affidavit is duly authorised to bring this application and that he accordingly sought and obtained approval from the Council of Medical Schemes to bring this application. It follows that he is properly deemed to be a person contemplated in section 346 of the Companies Act and is thus competent to bring this application for the respondent's winding-up.

[16] The respondent is a medical scheme registered and defined as such in terms of the provisions of the Act and which, for convenience, will hereinafter be referred to as the Scheme.

[17] The Scheme is what is defined in section 1 of the Act as a restricted membership scheme which is one the rules of which restrict the eligibility for membership by reference to, amongst others, employment or former membership or both membership or former membership of a particular profession, professional association or union. The membership of the Scheme is restricted to members of the Solidarity Trade Union ("*Solidarity*").

[18] The Scheme was registered and commenced business in January 2008. It is common cause that it enrolled its first members in January 2008 and that as at the end of October 2008 it had 722 principal members and 1 866 beneficiaries. As at December 2008 it had 771 principal members.

[19] It ought to be mentioned at the outset that in terms of membership the scheme is in contravention of Regulation 2(3) of the Act ("the Regulations") which provides as follows:

> "2…
>
> *(3) The minimum number of members required for the registration of a medical scheme established after these regulations have come into operation is 6 000, and this number must be admitted within a period of three months of registration of the medical scheme.*"

[20] As the Scheme failed to achieve the required membership within three months of its registration, it accordingly does not comply with the provisions of Regulation 2(3).

[21] In terms of section 35(1) of the Act, the Scheme is, at all times, required to maintain its business in a financially sound condition by –

21.1 having assets as contemplated in section 35(3) of the Act which specifically requires the Scheme to have assets the aggregate value of which, on any day, are not less than the aggregate of the aggregate value on that day of its liabilities and the nett assets prescribed;

21.2 providing for its liabilities;

21.3 generally conducting business so as to be in a position to meet its liabilities at all times.

[22] In terms of Regulation 29 of the Regulations the Scheme is required to maintain accumulated funds expressed as a percentage of gross annual contributions for the accounting period under review which may not be less than 25%.

[22] The Scheme is required, in terms of Regulation 29(3A), to meet a phased-in solvency level of 10% during the first year of its registration and 13,5% during the second year of registration.

[23] It is common cause that the Scheme has not reached the 10% solvency level in the first year of its registration and is accordingly not complying with Regulation 29(3A). The Schemes solvency levels are below the prescribed levels.

[24] A guarantee in the amount of R4 million has been issued as security for the payment of the Schemes liabilities. This guarantee is due to lapse on 17 January 2009 and an extended guarantee should have been issued on 31 December 2008. However, the Scheme failed to issue or furnish such replacement guarantee despite undertaking to do so.

[25] In terms of section 35(9) of the Act, the liabilities of the Scheme include:

25.1 the amount which the Scheme estimates will be payable in respects of claims which have been submitted and assessed but not yet paid;

25.2 the amount which the Scheme estimates will become payable in respect of claims which had been incurred but not yet submitted; and

25.3 the amount standing to the credit of a member's personal savings account.

[26] The Scheme has two benefit options, Kosmos and Protea. The Kosmos Benefit Option is an entry level option designed to cater for members earning between R3 500 and R7 500 per month. It has 353 members, 34 of who are chronic patients having a high claims ratio. The Protea benefit option is designed to cater for members earning between R5 000 and R9 000 per month and has 369 members. Approximately 99 beneficiaries under this option are chronic patients who necessarily have a high claims ratio.

[27] In terms of section 33(4) of the Act, a medical scheme's benefit option may be withdrawn if it is not financially sound. Furthermore, in terms of section 33(2) of the Act, the Registrar is not empowered to approve any benefit option unless the Council is satisfied that such benefit option –

27.1 include the prescribed minimum benefits;

27.2 shall be self-supporting in terms of membership and financial performance;

27.3 is financially sound and

27.4 will not jeopardise the financial soundness of any existing benefit option within the medical scheme.

[28] As the Scheme was operating in breach of various sections of the Act and its regulations as I have shown above, amongst which was its failure to comply with the provisions of Section 35 (1) and its low membership, on 23 July 2008 a meeting was held between the representatives of the applicant and the Scheme's Principal Officer, Malcolm Colman, the Scheme's financial manager and actuary. It is common cause that at this meeting, the Scheme's representatives indicated that the Scheme was unable to comply with the provisions of section 35(1) of the Act and that it had negative reserves.

[29] At the aforesaid meeting, the Scheme was requested to submit a business plan as contemplated by Regulation 29(4) of the Regulations, and was requested to set out the nature and causes of the Scheme's failure to be in a sound financial position, specifically its failure to maintain the prescribed level of accumulated funds, and the cause of action to be adopted to bring the Scheme to a sound financial position. Such business plan had to be submitted on or before 1 August 2008.

[30] On 28 October 2008 the Scheme submitted its business plan in which it explained how it sought to meet the solvency requirements in terms of Regulation 29. The Scheme also attributed its failure to comply with the provisions of section 35(1) to the following:

30.1 the fact that it was a new medical scheme that was launched in January 2008 from a zero cash base and which started with members whose premiums were paid in arrears and not in advance;

30.2 that it had experienced high rate of claims that exceeded international norms for a medical scheme of its size;

30.3 non-health related costs which were unavoidable and which could not be amortised as the Scheme did not have a large membership base;

30.4 prospective members refrained from joining the Scheme due to the Scheme being administered by Prosperity Health managers which is associated with medical schemes which failed;

30.5 the Scheme's administrator, Prosperity Health managers breached its undertaking to finance the scheme's restructuring plan, and that this was ultimately what had placed the Scheme in a very vulnerable position; and

30.6 an inadequate health information technology system which is unable to meet the Scheme's requirements.

[31] In the same business plan which is marked Annexure "FA4" to the founding affidavit, a restructuring plan is set out by which it is planned to:

31.1 grow the Scheme's membership by at least 239 members per month during 2009,

31.2 that there was a need for a cash injection into the Scheme of at least R6,04 million over the next twelve months starting with R2,7 million for current arrear claims in October 2008 and overheads totalling R3,3 million over the next twelve months.

31.3 self administration where all staff is housed under one roof and managed centrally to curb poor quality and high costs.

[32] The Scheme's financial management accounts which are attached to the founding affidavit as Annexure "FA7", reflect the Scheme's financial position as at the end of October 2008 as follows:

32.1 the Scheme's current liabilities which the Scheme is currently unable to pay amount to R4,3 million. These liabilities exceed the Scheme's assets by R2,9 million;

32.2 the Scheme's solvency level is - 35,8% which is grossly lower than the phase-in solvency level of 10% that is required of the Scheme during its first year of operation;

32.3 in October 2008 the Scheme received gross contributions of R1 million, resulting in a projected future income of R2 million over the next 2 months ending 31 December 2008.

32.4 in October 2008 the Scheme received gross contributions of R1 million, resulting in projected expected nett income for November and December 2008, based on the current membership on 722, 1 866 beneficiaries of R2,078 million. The projected net claims for the same period is R2,5 million to which must be added the non-health expenditure figure of R362 546,00.

[33] Clearly the projected income will still be well below projected claims and other expenditure.

[34] It is not disputed that members of the Scheme are still consulting with medical service providers on the basis that the Scheme would settle whatever fees are incurred as a result of consultations within the scope of the Scheme's rules. Similarly medical service providers are still attending to members of the Scheme on the assumption that their relevant fees will be paid when they become due.

[35] When regard is had to the above it is clear to me that there is no hope that the Scheme would be able to pay any claim submitted to it.

[36] Considering the Scheme's low membership and the division of that low membership between the two benefit options I have already referred to, the two options are not self supporting in terms of membership and financial performance and are not financially sound in terms of Section 33 (2) of the Act. They are thus liable to be withdrawn in terms of Section 33 (4).

[37] In an electronic mail dated 29 October 2008 attached as Annexure "FA8" to the founding affidavit, from Adriaan Dippenaar of the Scheme's administrators, Prosperity Health managers, to the Scheme's principal officer, the Scheme's principal officer was advised as follows:

> "*Find attached the management account Solvita Medical Scheme for the month of September 2008. As indicated in my previous email regarding the position of the Scheme reflected in the management accounts for the month of August 2008, I am concerned about the fact that the Scheme is currently still trading while its liabilities are exceeding its assets…"*

[38] On 24 November 2008 Adriaan Dippenaar again wrote to the Scheme's Principal Officer in an electronic mail attached as Annexure "FA9" to the founding affidavit where Dippenaar again raised his concern:

"*… about the fact that the Scheme is currently still trading while its liabilities are exceeding its assets*."

[39] The Scheme is in my view hopelessly insolvent and unable to meet its liabilities as contemplated in section 35(1) of the Act, a fact that has in fact been conceded by the Scheme in its answering affidavit.

[40] The Scheme's membership base is such that there are no prospects of members' premiums being sufficient to turn the Scheme around into being a financially sound medical scheme. There are no prospects of it attracting sufficient new members and retaining current members to make it financially viable and to be able to reach and maintain the prescribed solvency levels. Furthermore there is no evidence that the Scheme will be able to reach the membership figures projected in its revised business plan by which it will be able to recruit and enrol 450 new members per month. Even if it does, it does not necessarily follow that the Scheme's solvency levels would reach the prescribed levels.

[41] Furthermore, for purposes of the relief which the applicant seeks, the question which is not whether or not the Scheme will at some later stage be capable of reaching and maintaining the prescribed solvency levels – the question is whether or not on the date of hearing of this application the Scheme is in contravention of section 35 of the Act. If it is, the relief which the applicant seeks must be granted without any further enquiry.

[42] In my view a case for a contravention of section 35 of the Act has been made and there is no reason why a winding-up order should not be granted.

[43] In terms of section 53(3) of the Act, in applying the provisions of Chapter XIV of the Companies Act 61 of 1973 –

> 43.1 a reference which relates to the inability of a medical scheme to pay its debts shall be construed as relating to its inability to comply with the requirements contemplated in section 35(1) of the Act.
>
> 43.2 in addition to any question whether it is just and equitable that a medical scheme should be wound up, there shall be considered also the question whether it is in the interest of the beneficiaries of that medical scheme that it should be wound up.

I now turn to consider the aspect of urgency.

[44] The Scheme contends that this application should not be heard as one of urgency. In determining this issue I consider it expedient that I look at the events which took place before and after the matter was initially enrolled.

[45] On 15 December 2008 the matter came before Boruchowitz J in the urgent court. On that day it was, by agreement, postponed to the urgent court roll for the week beginning 12 January 2009 for hearing on 13 January 2009.

[46] In postponing the matter to 13 January 2009, the parties agreed amongst others, that:

46.1 the trade union Solidarity would make a cash injection of not less than R3 million into the Scheme not later than 13 January 2009,

46.2 Solidarity would directly provide the applicant with an undertaking that it would pay any of the Scheme's liabilities in excess of R4 million presently secured by a guarantee which will lapse on 17 January 2009. This undertaking was intended to operate during the period 15 December 2008 to 12 January 2009, and

46.3 the guarantee which was going to lapse on 17 January 2009 will be replaced by a new guarantee by not later than 31 December 2008.

[47] It is trite that none of the above have been complied with.

[48] Three letters were exchanged between the parties pursuant to the agreement reached on 15 December 2008. These letters are attached as Annexures "RA2", "RA2A" and "RA2B" to the replying affidavit.

[49] On 22 December 2008 the Scheme delivered a revised business plan setting out the course of action it intended to adopt in order to reach the prescribed solvency levels. It was the parties' intention that this application would be settled if the applicant was satisfied with the Scheme's proposed

course of action and if the terms of the agreement as aforesaid were complied with.

[50] Applicant considered the Scheme's revised business plan and found, quite justifiably in my view, that it is unacceptable for the following reasons:

50.1 It is based on the assumption that the Scheme will recruit and enrol at least 450 members per month. It must be borne in mind that in terms of its original business plan, the Scheme should have had 10 000 members by the end of June 2008. The Scheme however later revised this estimate and then estimated that it would have 2 000 members by December 2008 and 3 200 members by December 2009. It is trite that the Scheme only had 771 principal members at the end of 2008. There is accordingly no evidence or actual basis to accept that the Scheme will be able to recruit and enrol the projected number of members.

50.2 The Scheme now contemplates in terms of this revised business plan that it would be able to recruit and enrol a larger number of members than the number which it failed to enrol in the past year. There is no evidence to show as to where these projected members would come from. In my view this is all baseless speculation. It appears from the Scheme's revised business plan that only 102 new members joined the Scheme in January 2009 and that only 25 new members would join the Scheme in

February 2009. These figures are far lower than the projected 450 new members per month. There is great scepticism that the projected 5 400 membership number will be reached by the end of 2009.

50.3 Even if the projected 5 400 could be reached by the end of 2009 it does no necessarily mean that the Scheme would then automatically comply with the provisions of section 35. Differently put there is nothing that suggests that it would take the Scheme out of its current insolvency situation.

[51] In terms of the Scheme's revised business plan, it intends to terminate the administration contract and become self-administered. Self-evidently this route will increase the Scheme's non-health care costs. The Scheme cannot afford such costs at this stage due to its low membership base and its present dire financial position.

[52] The revised business plan also fails to make any provision for re-insurance. Given the Scheme's low membership, it follows that its risk pool is not big enough to absorb any catastrophic claims.

[53] In paragraph 2.10.1 of the Scheme's answering affidavit, it is conceded that the Scheme is currently trading, while liabilities exceed its asset and that has been the case from the very inception of its existence in January 2008

and… "*when it was allowed to start the conduct of its business without any capital, but only supported by a R4 million guarantee*".

[54] I have already mentioned that the present guarantee will lapse on 17 January 2009. It should have been replaced by another one before 31 December 2008, which never occurred. It follows that if the order for liquidation was not granted before 17 January 2009, there will be no security for the payment of any claim.

[55] In paragraph 2.19.1 of its answering affidavit, the Scheme proffered that it had no objection if the Court would postpone the urgent application (on 15 December 2008) *sine die* and allowed the applicant to re-enrol it if an extended guarantee was not lodged to the applicant by 31 December 2008.

[56] As an extended guarantee was never lodged by 31 December 2008, the matter was accordingly re-enrolled for hearing on 13 January 2008 as per agreement between the parties. I accordingly have a difficulty to accept the Scheme's contention that this matter does not deserve to be heard as one of urgency.

[57] Furthermore, the Scheme has conceded that it is insolvent and that its solvency levels are below the prescribed levels. On this basis alone, I am satisfied that any delay in hearing this application would only serve to worsen the Scheme's financial position to the detriment of its members and would result in the expiry of the guarantee leaving the Scheme without any security to

settle any of its liabilities. I cannot allow the Scheme to remain in business whilst it is clearly insolvent and is operating in contravention of the Act and the Regulations.

[58] Whilst I am in agreement with the Scheme's contention that the Scheme's current members will be left without medical insurance upon the Scheme's liquidation, such members will be free to join other medical schemes and may in any event simply be transferred to another medical scheme together with the balance of their medical savings account, if any. The members' past and current claims will be settled by the guarantee that is due to lapse on 17 January 2009.

[59] It was also submitted on the respondent's behalf that the matter was not urgent as the Council approved the bringing of this application either on 21 or 22 November 2008 and that this application should have been filed then or shortly thereafter. In my view this does not assist the respondent in any way. The application was brought timeously because the resolution passed by the Council approving the bringing of this application which is attached to the founding affidavit clearly shows that it was passed on 9 December 2008.

[60] I am accordingly satisfied that the application properly served before the urgent court.

[61] Furthermore, the point raised that the applicant failed to give any notice to any of the members and/or beneficiaries of the respondent or to Solidarity

cannot hold. Solidarity was a party to all the negotiations even to the extent of the undertaking that it would make a cash injection and/or furnish an extended guarantee on behalf of the Scheme.

[62] There is no legal requirement that this application should have been served on members and/or beneficiaries of the Scheme.

[63] I am satisfied that the Scheme is currently trading while its liabilities exceed its assets. As a result of this continued trading, its members are being exposed to litigation by medical service providers as their claims will in all likelihood not be paid. In addition unsuspecting medical service providers are being financially exposed in that they are continuing to provide medical services to the Scheme's beneficiaries when there is no hope that the Scheme will be able to settle their claims after providing services to its members.

[64] I am thus satisfied that it is in the interests of the beneficiaries that a liquidator be appointed on an urgent basis to take steps to settle the Scheme's liabilities to the extent that its remaining assets would permit so as to protect the interests of members.

[65] Based on the entire facts of this case, I am thus satisfied that the order for the liquidation of the respondent will be for the benefit of the members. There is thus no impediment against the granting of the approval contemplated in section 53 (2) of the Act.

[66] I am satisfied that the applicant has made out a case for the relief set out in the Notice of Motion. Furthermore the Scheme is also liable to pay the costs occasioned by the postponement of this matter on 15 December 2008 including the costs occasioned by the employment of two counsel.

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B H MBHA
JUDGE OF THE HIGH COURT

MATTER HEARD ON	: 15 JANUARY 2009
ORDER GRANTED ON	: 16 JANUARY 2009
REASONS FURNISHED ON	: 24 APRIL 2009
COUNSEL FOR THE APPLICANT	: ADV JJ BRETTS SC AND ADV KN TSATSAWANE
INSTRUCTED BY	: MAPONYA INCORPORATED
COUNSEL FOR THE RESPONDENT	: ADV PA SWANEPOEL
INSTRUCTED BY	: SERFONTEIN VILJOEN & SWART