



## Pension Lawyers Association Seminar

Vanessa Bell  
Associate  
Edward Nathan Sonnenbergs Inc  
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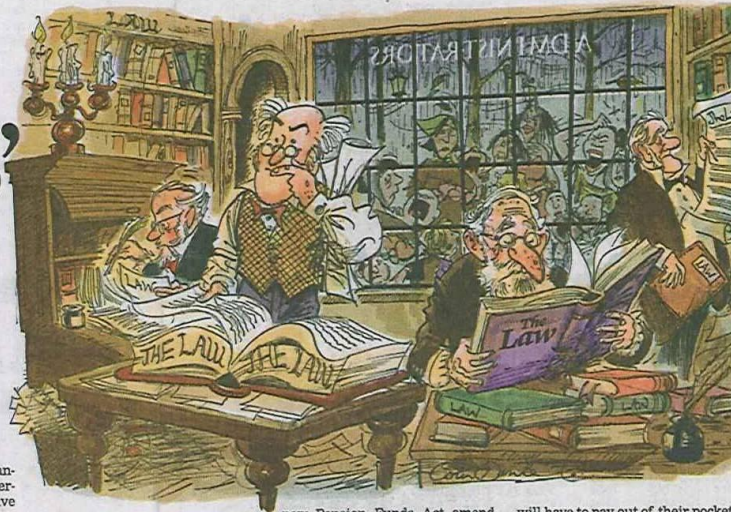
**DIVORCE BENEFITS – THE  
AMENDMENTS AND THE COCKCROFT  
ADJUDICATOR DETERMINATION**



■ ADMINISTRATORS QUESTION WHETHER AMENDMENT APPLIES TO SETTLEMENTS BEFORE SEPTEMBER 13

# Legal hurdle to splitting divorcees' pension money

Retirement fund administrators want greater clarity on how an amendment to the Pension Funds Act affects the separation of all divorcees' retirement assets. *Laura du Preez reports*



Divorcees, many of whom may have already waited some time for the right to access their portion of their former spouses' retirement fund savings, may face another hurdle that could prolong the time they will be denied growth on the money they are owed.

This is despite the fact that:

◆ Lawmakers intended to improve their lot immediately with an amendment that was meant to apply retrospectively; and

◆ A recent ruling by the Pension Funds Adjudicator that applied the amendment retrospectively in favour of a woman who claimed access to her share of her ex-husband's pension fund.

At least one retirement fund administrator, Old Mutual, has advised the retirement funds it

absolves the administrator of any potential claims.

The Pension Funds Act was amended with effect from September 13 to give divorcees immediate access to pension benefits awarded to them in terms of divorce orders – what is known as a “clean break” of pension fund interests.

Previously, former spouses – usually former wives – had been able to access their portion of the benefits only when their former husbands resigned or retired. From the date of divorce until either event, they were denied growth on their portion of the benefits.

But although the National Treasury has confirmed in a letter to the Life Offices' Association, which represents life insurers – many of which administer retirement funds

Treasury's chief director of financial sector policy, says to ensure certainty about the retrospective nature of the amendment, the treasury will consider a further amendment to the Pension Funds Act by way of the General Financial Services Laws Amendment Bill, which is expected to be tabled before the end of the year but will be considered by Parliament only next year.

On October 3, Mamodupi Mohlala, the Pension Funds Adjudicator, in a case before her, Cockcroft versus the Mine Employees' Pension Fund, ruled that the amendment should be applied to divorce orders made before and after September 13.

Mohlala's office said this week that former spouses who approach pension funds about the payment or transfer of divorce benefits and are

about the correctness of the adjudicator's ruling because they do not interpret the amended law as applying retrospectively to divorce orders made before September 13.

In a newsletter to funds and intermediaries, Old Mutual says the application of the amended Pension Funds Act to existing divorce orders could be challenged.

Jenny Gordon, a senior legal adviser at Old Mutual, says Old Mutual is concerned that if the funds it administers pay out former spouses in terms of divorce orders made before September 13 without having certainty on how the amendment should apply, the funds and Old Mutual may be held liable to

new Pension Funds Act amendments” and there is “a great deal of uncertainty regarding how the funds should apply the tax” if retirement funds pay out former spouses before proposed changes to the tax laws are implemented.

## CHANGES TO TAX LAW

Hearings on the Revenue Laws Amendment Bill continued in Parliament this week. The bill proposes that payments from funds to former spouses in terms of divorce orders be treated as withdrawals by the fund member for tax purposes.

This means that once this is enacted, if a non-member former spouse is paid a portion of a member's retirement savings, the mem-

ber will have to pay out of their pockets because the tax cannot be paid from their retirement savings. But Gordon says comments on this issue are being considered and it is unlikely that the law when enacted will result in such a situation.

The amended Pension Funds Act provides for pension fund interests granted to non-member former spouses in terms of divorce orders to be transferred to another retirement fund. However, Gordon says the tax consequences of such a transfer are still unclear, and non-member former spouses should proceed with caution and seek professional advice on this issue before exercising this option.

Until the tax law is amended,



# All former spouses to get their share of pension benefits

LAURA DU PREEZ

The Pension Funds Adjudicator this week ruled that all former spouses who are entitled to a share of their partners' retirement benefits in terms of a divorce order must have immediate access to these benefits.

Pension funds lawyer Jonathan Mort, of law firm Edward Nathan Sonnenbergs, says the ruling affects thousands of people, giving them the opportunity to earn returns on their share of the benefits.

Recent amendments to the Pension Funds Act introduced the clean break principle to the separation of divorced couples' pension benefits.

Until the amendment was

promulgated on September 13, the ex-spouse, usually the former wife, would have to wait until her former husband withdrew from the fund – due to resignation, retrenchment or dismissal – or retired from the fund before she could get her share of the retirement benefits.

During that time, the former spouse was denied any growth on her share and, if she had to wait many years for it, the benefit could be seriously eroded by inflation.

The government moved to rectify the problem this year by amending the Pension Funds Act to state that a pension benefit granted in terms of a divorce order is deemed to accrue to the member on the date of

the divorce. But the amendment brought relief only for non-member former spouses who were given access to their former spouses' retirement benefits in divorce orders granted after September 13.

Former spouses divorced before this date did not appear to benefit.

## ADJUDICATOR'S RULING

But this week, Mamodupi Mohlala, the Pension Funds Adjudicator, ruled in favour of a divorcee who was in this predicament.

Her decision is likely to affect thousands of divorcees who are awaiting payment of the benefits from various retirement funds.

Mohlala made the ruling in a

case in which JC Cockcroft complained that she was entitled to the immediate payment or transfer of a portion of the pension benefit of her former husband, LB Cockcroft, in the Mine Employees' Pension Fund.

Cockcroft had stopped contributing to the fund but remained a non-contributory member.

The Cockcrofts were divorced in 2003. The divorce order stated that Mrs Cockcroft was entitled to 50 per cent of Mr Cockcroft's pension interest in the fund, to be paid to her on divorce or when the benefit accrued, whichever occurred first.

The fund, however, refused to pay the benefit. The fund argued that in terms of the then applicable

legislation, the benefit could be paid to Mrs Cockcroft only once Mr Cockcroft was paid his benefits.

The adjudicator, after consulting case law on retrospective legislation and, in particular, the impact on the member's vested rights, concluded that the new Act attaches new consequences to earlier events without altering the divorce order.

The Act must accordingly be seen as "operating prospectively" from September 13 to all divorce orders, whether they were made prior to or subsequent to this date.

Mohlala said the intention of the legislature was clearly to rectify the previously unfair position of non-member spouses in respect of the

payment of divorce benefits. She said if the legislation was applied retrospectively, it did not affect the vested rights of members.

Mohlala therefore ordered the Mine Employees' Pension Fund to pay out Mrs Cockcroft or transfer the benefit to which she was entitled to another fund.

## DILEMMA FOR FUNDS

Mort says funds will have to decide what to do if the former spouse of a member applies to it for the payment of his or her share of the benefits granted by a divorce order.

He thinks the funds should inform the affected member and, unless the member objects, pay out

the non-member former spouse.

If the member objects, possibly on the grounds that he or she will lose out on future growth on the non-member former spouse's portion, he or she should be instructed to complain to the Pension Funds Adjudicator, Mort says.

Mort says funds should also inform non-member former spouses of their new-found right to claim their share, and former spouses should ensure that funds have their contact details.

Ken Stuart, a financial adviser with Netto Financial Services, says the adjudicator's ruling provides an ideal opportunity for all divorced couples to plan their finances.



■ RANGE OF TAX-FREE TOP-UPS TO RETIREMENT FUNDS ■ DIVORCED FUND MEMBERS MAY FACE HEFTY BILL

# Payouts for some, pay up for others

Retirement fund members who are divorced may have to cough up a sizeable amount of cash to pay the taxman if their former spouses claim their share of the benefits from the members' funds. Bruce Cameron reports

There is good tax news on the way for some retirement fund members and pensioners, but many fund members who are divorced may be in for a big tax shock following various changes to legislation.

The good news is: no tax will be payable by pensioners or former members of retirement funds, including retirement annuity (RA) funds, who benefit from:

- ◆ A lump sum payout of a retirement fund surplus;
- ◆ The repayment of secret profits by a retirement fund administrator; and/or
- ◆ The anticipated R3 billion that must be paid by the life assurance industry to compensate policyholders and RA fund members for confiscatory surrender penalties.

The bad news is: in terms of current draft legislation, any retirement fund member who is party to a divorce settlement that awards pension benefits to a former spouse could face significant tax payments if a former spouse uses provisions in the new Pension Funds Amendment Act to claim the benefits before the member retires or withdraws from a fund.

Details of how the various payments will be taxed – which are contained in the latest tax legislation – were provided by Mientjie Botha, the director of the tax policy unit of the National Treasury, at the annual con-

## HEALTH WARNING

You should preserve all your retirement fund savings until you retire. Recent research by financial services company Alexander Forbes shows that the average retirement fund member retires from his or her last fund with a pension that is 28 percent of his or her final pay cheque. And most people do not preserve the savings they accumulated in any retirement funds to which they previously belonged.

Botha says any lump sum payment of this surplus amount after January 1, 2006 will be tax-free.

Active contributing members of retirement funds will not benefit from this tax concession. Any amounts from a surplus distribution due to active members will be added to their retirement savings and taxed in the normal way when they retire.

## CLEAN BREAK AT DIVORCE

Botha says tax legislation will be amended as a result of the recent promulgation of the Pension Funds Amendment Act, which introduces the "clean break" principle to awards made in terms of divorce settlements.

## THEY ROSE TO THE CHALLENGE



The Institute of Retirement Funds Communications Challenge awards for 2007, which were sponsored by Old Mutual and Personal Finance, were presented at the Institute's annual convention this week. The awards are aimed at encouraging funds to communicate properly with their members, keeping them informed of fund policies and issues that affect members' retirement savings.

Pictured above are representatives of the funds that won in the competition's different categories. From left: Zsöfi Fouche, of the Cape Joint Retirement Fund; Andrew Welsh, of the Steinmuller Group Retirement Fund; Brandon Gillham, of the M Retirement Fund; and Dr K Bezuidenhout, of the Sentinel Mining Industry Retirement Fund and Mine Employees Pension Fund.

The retirement funds that won in the various categories are: **Umbrella funds:** 1. Cape Joint Retirement Fund, 2. Cape Joint Pension Fund. **Highly commended:** KwaZulu-Natal Building Industry Retirement Fund. **Small funds:** 1. Steinmuller Group Retirement Fund, 2. Vacation Exchanges International Pension Fund. **Medium funds:** 1. M Retirement Fund, 2. Seppi Provident Fund, 3. Idwala Provident Fund. **Highly commended for special project award:** University of Cape Town Provident Fund. **Large funds:** 1. Sentinel Mining Industry Retirement Fund and Mine Employees Pension Fund, 2. Satava National Pension Fund. **Highly commended for special project award:** De Beers Pension Fund.

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## A bit of history

- Pension interests on divorce prior to the amendment of the Divorce Act, 1979 by the Divorce Amendment Act, 1989
  - The interest which a spouse had in respect of benefits which had not yet accrued “was generally not regarded as an asset in his/her estate, or where the marriage was in COP, as an asset in the joint estate” (see *Old Mutual v Swemmer* (5) SA 373 (SCA)).
  - ‘pension expectations’ of a member spouse therefore not taken into account.



## The Divorce Amendment Act, 1989

- Introduced deeming provision
- S7(7)(a) of the Divorce Act “deems” a member spouse’s “pension interest” to be an asset in his/her estate for purposes of determining patrimonial benefits.
- Does not apply to marriages out COP entered into on or after 1 November 1984 where COP and accrual systems excluded (S7(7)(c)).



## The Divorce Amendment Act, 1989(Cont.)

- “Pension fund” and “pension interest” for the first time defined in Divorce Act.
  - Pension interest in pension and provident funds = member’s withdrawal benefits to the rules of the fund if membership would have terminated on date of divorce on account of member’s resignation (i.e. exit from the fund).
  - Pension interest in retirement annuity fund = member’s contribution up to date of divorce + 15.5% interest (prescribed rate of interest to Prescribed Rate of Interest Act).



## The Position Pre – PFA Amendment: dealing with pension interests in the Divorce Act, as amended

S7(8)(a): the court granting a degree of divorce... may make an order that –

- Any part of the pension interest of the member which is due or assigned to the other party to the divorce action, shall be paid by the fund to the other party “**when** any pension benefits **accrue** in respect of that member”.
- An endorsement be made in the records of the fund that that part of the pension interest concerned is so payable to the other party.



The Position Pre – PFA Amendment: dealing with pension interests in Divorce Act, as amended (Cont.)

- Any part of the pension interest may be awarded by the court to the non-member spouse (could be 100% as in Swemmer case referred to).
- Narrow definition of 'pension interest' establishes a method of ascertaining the value of the interest as at date of divorce: this fixes the amount payable to the non-member spouse.



The Position Pre – PFA Amendment: dealing with pension interests in Divorce Act, as amended (Cont.)

- Payment when the pension benefit accrues to the member
  - It is “the when” that is important
  - When the accrual takes place is determined by the rules of the pension fund governing the relationship between it and the member
  - Generally depends on an employment event such as retirement, resignation, retrenchment or dismissal.



## Some of the problems

- The 'new' provisions in the Divorce Act gave rise to problems and inequities as a result of the way in which the non-member spouse's portion was dealt with.
- Resulted in two investigations by the South African Law Commission and its reports of March 1995 and June 1999 – inequities highlighted
- Clean – break principle cannot be given effect to
- No provision for the fund to be ordered to pay the non-member spouse interest or capital growth on the portion of the pension interest allocated to the non-member spouse from the date of divorce to date of payment.
- Devaluation over time: considered unfair as no growth or interest on non-member spouse's portion.



## Some of the problems (Cont.)

- If non-member spouse dies before accrual – benefit not payable into his/her estate.
- Badly drafted settlement agreements or divorce orders; non-compliance with secs 7(7) and 7(8) of Divorce Act; funds not named or properly named – divorce order cannot be given effect to.
- True value of member's pension interest at DOD would in many instances have to be determined actuarially wrt the contingencies which determine the payment of those benefits - instead narrow definition of "pension interest" in Divorce Act (but more practical) to fix value at DOD.



## The Pension Funds Amendment Act, 2007

- What are the changes?
- Have the changes resolved the problems or created new ones?
  
- S28(b) of the Amendment Act has amended S37D of the PFA by the addition of paragraphs (d) and (e) to subsection (1)



## The Pension Funds Amendment Act, 2007 (Cont.)

- A registered fund may:
  - (d) deduct from a member's benefit or minimum individual reserve, as the case may be, any amount assigned from his or her pension interest to a non-member spouse or any other person in terms of a valid order made by a competent court.
  - (e) for the purposes of section 7(8)(a) of the Divorce Act, 1979 (Act No. 70 of 1979), the pension benefit referred to in that section is **deemed to accrue** to the member on **the date of the court order**:



## The Pension Funds Amendment Act, 2007 (Cont.)

Provided that—

- (i) such deduction shall be effected by the pension fund named in the order upon receipt of the order;
- (ii) such deduction shall have the effect of reducing the accrued benefit at the date of such deduction;
- (iii) the non-member spouse shall have the option to elect that the assigned amount be paid directly to him or her, or that it be transferred to an approved pension fund on his or her behalf, and such transfer or payment must take place within 60 days of such election having been exercised;
- (iv) the non-member spouse shall not acquire the rights of a member or beneficiary in relation to the pension fund;
- (iv) the non-member spouse shall not acquire the rights of a member or beneficiary in relation to the pension fund; and



The Pension Funds Amendment Act, 2007 (Cont.)

(v) the non-member spouse shall be entitled to the accrual of interest on the assigned amount at fund return from the expiry of the period referred to in subparagraph (iii) until payment or transfer thereof, but not to any other interest or growth.



*en*

## The Pension Funds Amendment Act, 2007 (Cont.)

- Effect of amendment is to change “the when” i.e. when pension benefits accrue to the member
  - Position prior to amendment is still the same in that payment of the non-member’s share takes place when the benefits accrue i.e. payment on accrual
  - Previously benefits accrued on exit event = determined by rules of the fund
  - Now as a result of the deeming provision, benefits accrue at date of divorce: change is that accrual is set by legislation, no longer the rules of a fund



## Issues arising out of the Amendments

- Will deal with 3 main issues:
  - (1) Retrospective or not?
  - (2) S14 or ROT
  - (3) Proposed tax amendments



## (1) Retrospective or not: the burning issue

- Does the new section 37D apply to divorce orders granted prior to its effective date of 13 September 2007?
  - (1) Retroactive and Retrospective legislation defined
  - (2) The Cockcroft Adjudicator determination
- Retroactive statute: operates as of a time prior to its enactment...operates backwards. A retroactive statute changes the law from what it was
- Retrospective statute: operates for the future only. It is prospective, but it imposes new results in respect of a past event; attaches new consequences for the future to an event that took place before the statute was enacted...changes the law from what it otherwise would be with respect to a prior event.

*[National Director of Public Prosecutions v Carolus and Others 2000 (1) SA 1127 (SCA)]*



## (1) Retrospectivity (Cont.)

- There is a presumption against both retroactive and retrospective legislation – thus intention of legislature must be clear.
- A statute is retrospective in its effect if it takes away or impairs a vested right acquired under existing laws or creates a new obligation or imposes a new duty or attaches a new disability in regard to events already past.
- What does the Cockcroft determination say?



## Cockcroft v Mine Employees Pension Fund (3 October 2007)

- The crux of the determination was whether S28(b) of the Amendment Act applies to divorce orders granted prior to 13 September 2007.
- Q posed by Adjudicator: Does the fact that divorce orders were granted prior to the enactment of the legislation render it retrospective in operation? In her view it does not.
- Her reasons:
  - S28(b) of the new Act only applies wef 13 September 2007. Only from that date, is the non-member spouse entitled to have the divorce benefit disinvested and paid.
  - Member is not required to pay interest retrospectively from DOD – interest only after 60 days from election = clear and unambiguous.



## Cockcroft v Mine Employees Pension Fund (cont.)

- Adjudicator concluded that S28(b) is therefore not retrospective but prospective in operation.
- She stated that “it gives a different legal result to a set of transaction/s (the divorce order and related pension consequences) completed prior to 13 September 2007. However, it does not affect the underlying concluded transactions in any way”
- Agree with Adjudicator on this finding



## Cockcroft v Mine Employees Pension Fund (cont.)

- BUT, Adjudicator went on to consider whether S28(b) does constitute retrospective legislation.
  - Looked at question of interference with vested rights: member's right to investment growth on non-member spouse's portion
  - Member has no quantifiable right, at best a '*spes*'
  - Therefore no question of interference with vested rights.
  - Also looked at the fact that the position of the non-member spouse is improved considerably by the amendment.



## Cockcroft v Mine Employees Pension Fund (cont.)

- Adjudicator referred to *Kruger v President Insurance Co. Ltd* 1994 (2) SA 495 (D):

“The conclusion that a statute was intended to operate with retrospective effect may be more readily arrived at in a case where vested rights would not be affected by a retrospective operation and also where the intention of the legislature was clearly to bestow a benefit or to effect evenhandedness in the operation of the law.”



## Cockcroft v Mine Employees Pension Fund (cont.)

- Concluded that even if wrong on prospective application of the legislation, satisfied that legislature intended it to apply retrospectively and presumption vs retrospectivity trumped because intention of legislature was clearly to rectify the previous unfair position of non-member spouses
- Unnecessary conclusion, trying to cover all bases
- Simplify uncertainty – understand amendment to S37D as operating prospectively, same result achieved wrt correcting unfair position in circs where intention of legislature not clearly stated.

If Adjudicator finding on retrospectivity challenged, first finding still stands and correct in law.

- Conclusion: Cockcroft should be applied to divorce orders prior to 13 September 2007.



## (2) S14 OR ROT

- Non-member spouse may elect to transfer assigned amount to an approved pension fund.
- Problem: conflict between amended S14 and S37D.
  - Transfer to S14 must be effected within 180 days vs 60 days from election to S37D.
- S14 (1) of PFA refers to the transfer of business from a registered fund
- Word “business” not defined – but business of a fund is the provision of benefits to its rules.
  - Test is whether the benefit has accrued – if yes = no more business of that fund in relation to the member or beneficiary except for payment or transfer to another fund.



## (2) S14 OR ROT (cont.)

- If benefit not accrued, but still accruing – then properly a transfer of the business of a fund.
- Exceptions to S14 transfers in PF Circular 120.
  - Although para 10.1 of PF120 refers to benefit accruing to member which entitles member to receive same in cash or elect to transfer to another fund, seems applicable to situation of non-member spouse.
- If treated as withdrawal benefit, then ROT not S14 applies.
- Delays in S14 transfers (inevitably longer) would prejudice non-member spouse = reason why transfer should not be to S14 if unnecessary.



### (3) Tax Amendments

- 2B of 2<sup>nd</sup> Schedule to Income Tax Act
  - the amount of the pension interest ordered by a court to be paid to a non-member spouse is deemed to accrue to the member on the date on which the pension interest of which that amount forms part, accrues to the member.
- Accrual was on exit from the fund
- Member is responsible for tax at his/her average tax rate, tax on his and hers paid on exit.
- Right to recover the amount of the tax paid on non-member spouse's portion from former spouse ito 2B



### (3) Tax Amendments (cont.)

- Revenue Laws Amendment Bill

- Previous draft provided for member to pay tax at the time non-member spouse's portion paid
- Right to recover from former spouse retained
- But problem, tax would have to come out of member's pocket because tax could not be paid from the residual amount of member's pension interest because does not accrue until exit.

- Latest draft of Revenue Laws Amendment Bill

- Released last week, 6 November 2007
- S4(1) amends S37D of PFA to allow the deduction of the tax payable on non-member spouse's portion from the member's benefit or minimum individual reserve



### (3) Tax Amendments (cont.)

- The pension benefit referred to in S7(8)(a) of the Divorce Act and the tax payable thereon is now deemed to accrue to the member on the date of the court order
  - Subsec (1) is deemed to come into operation on 13 September 2007
- Better but what do funds do until Tax Bill becomes law?
  - Amended S37D is now law. Funds obliged to apply law as it stands - non-member spouses' benefits must be paid within 60 days of election. If not interest is payable



### (3) Tax Amendments (cont.)

- Is solution to pay non-member spouse and park tax amount in fund until tax amendments effected?
  - Problem: if proposed tax amendments change
- Unlikely to change significantly but not ideal to act in anticipation of legislative change.
- Apply tax laws as they stand until amendments effected? Difficult, can only pay tax when member's portion accrues on exit
- Seems it may be best to await final tax amendments and pay interest



### (3) Tax Amendments (cont.)

- Tax position if non-member spouse elects to transfer interest to approved pension fund.
  - If tax paid by member and recovered from ex-spouse, no incentive to transfer to pension fund because non-member spouse taxed again on exit from that fund.
  - What about social objective of encouraging saving for retirement?
  - Ex-spouses placed at disadvantage in securing retirement savings if no tax incentive to transfer to pension fund.
  - Treasury has advised that the recommendation that non-member spouse be allowed to transfer withdrawal amount to another fund tax-free is being considered



thank you



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