



Retirement Funds and Divorce

Introduction

The Pension Funds Act (“the PFA”) offers significant protection to members by preventing third parties to lay claim to members’ saving in pension and provident funds (collectively referred to as “retirement funds” in this document). There are however a few exceptions allowed for in the PFA, the Income Tax Act, the Maintenance Act and the Divorce Act.

The Divorce Act allows a retirement fund to assign (and either pay immediately or reserve for later payment) a portion of a member’s benefit in the retirement fund to the member’s former spouse (“non-member spouse”) in the event of divorce. There are certain conditions that have to be met in order for a divorce order to be binding on a retirement fund.

As consultants and administrators of retirement funds, we regularly have to deal with divorce orders that affect the retirement fund benefits of the divorcees.

In our experience, the vast majority of divorce orders served on the retirement funds we advise and administer “do not pass muster” when assessed against these conditions, due to poor drafting of the divorce order.

These unenforceable divorce orders are then referred back to the member and non-member spouse to bring substantive applications to the relevant court to rectify the bad drafting of the divorce order, which invariably leads to additional costs to the parties.

The conditions that a divorce order has to comply with to be binding on a retirement fund can be summarised as follows:

1. There must be a **valid decree of divorce** (divorce order) granted by a court (High Court, Regional Court or Divorce Court).
2. The member against whose retirement benefit is being claimed **must still be a member of the retirement fund** on the date that the divorce order is granted.
3. The **retirement fund** against which the order is granted **must be identified or identifiable** in the divorce order.
4. The divorce order must specify that the member’s “**pension interest**” is assigned to the non-member spouse and must **specify the proportion or amount** thereof that is assigned to the non-member spouse.
5. If so required, the divorce order **must order the retirement fund to make immediate payment** of the agreed proportion or amount of pension interest to the non-member spouse **or must order the retirement fund to adjust its records** to reflect the claim of the non-member spouse to be settled when the member eventually exits the retirement fund.

If any of these conditions are not met, the divorce order will not be binding on the retirement fund.

Let’s have a more in-depth look at the laws behind these conditions:

The Divorce Act

The Divorce Act, 1979 as amended by the Divorce Amendment Act, 1989 allowed for parties to a divorce action to take into account their pension benefits when determining the patrimonial benefits to which the parties may be entitled.

“Pension Interest”

It is important to note that reference must be made to “pension interest” in the divorce order, irrespective of whether the retirement fund is a pension fund or a provident fund.

“Pension interest” is in effect the member’s withdrawal benefit on the date of divorce. The full definition in the Divorce Act is as follows:

“Pension interest in relation to a party to a divorce who is the member of a pension fund, means the benefits to which that party as such a member would have been entitled in terms of the rules of that fund if his membership of the fund would have been terminated on the date of the divorce on account of his resignation from his office.”

Pension Interest is Part of Member’s Assets

The Divorce Act provides for a member’s pension interest to be regarded as part of the member’s assets that can be considered when deciding on the division of assets.

- Section 7(7)(a): deems a member’s pension interest to be an asset in his/her estate.
- Section 7(7)(b): provides that the amount which is deemed to be part of a party’s assets, shall be reduced by any amount of his/her pension interest, by virtue of section 7(7)(a), in a previous divorce:
 - Was paid or awarded to another party; or
 - For purposes of an agreement contemplated in section 7(1), was accounted in favour of another party.

- Section 7(7)(c): provides that the deeming provision of section 7(7)(a) shall not apply to:
 - a divorce action in respect of a marriage out of community of property entered into on or after 1 November 1984 in terms of an antenuptial contract by which community of property, community of profit and loss and the actual system are excluded.

Decree of Divorce

Section 7(8)(a) of the Divorce Act specifically refers to the ability of “the court granting a decree of divorce” to grant an order to the effect that the fund must make payment of a portion of the member’s pension interest to the non-member spouse and make an endorsement in the member’s records.

A decree of divorce may be granted in respect of the following:

- A marriage concluded in terms of the Marriage Act, 1961;
- A valid customary marriage in terms of the Recognition of Customary Marriages, 1998; and
- A civil union (i.e. marriage of civil partnership) concluded in terms of the Civil Union Act, 2006.

Note: Permanent life partnerships are not included in the above.

Proportion or Amount to be Specified

Contrary to popular belief, the non-member spouse is not automatically entitled to 50% of the member’s pension interest.

The parties may agree on any proportion of the pension interest (i.e. between 0% and 100%) or even an agreed fixed amount to be allocated to the non-member spouse.

It is however critical that the proportion or amount be specified in the divorce order.

Pension Funds Act (“PFA”)

Historically, divorce orders served on retirement funds only allowed retirement funds to flag the member’s records to reflect the claim of the non-member spouse against the member’s benefit, and the non-member’s spouse’s claim was only payable in the event of the member’s eventual exit from the retirement fund.

Clean-break Principle

The PFA was amended in 2007 to introduce the “clean-break principle”. This amendment allowed retirement funds to deduct the following from the member’s benefit:

- The amount of the pension interest allocated to the non-member spouse in terms of a divorce order containing an order in terms of section 7(8) of the Divorce Act; and
- The tax to be deducted or withheld in terms of the Fourth Schedule of the Income Tax Act as a result of the payment of the pension interest to the non-member spouse.

Notes:

The Financial Services Laws General Amendment Act, 2008 (which came into effect on 1 November 2008), allowed for the clean-break principle to apply to divorce orders granted prior to 13 September 2007.

The Government Employees Pension Fund Law was also amended to allow for the application of the “clean-break” principle with effect from 14 December 2011.

Order of deductions

Section 37D(3) of the PFA, provides for the following order of deductions where there is more than one possible deduction to be made against a member’s benefit at the same time:

- Home loan / guarantee (granted prior to the granting of the court order).
- Maintenance order.
- Divorce order.

Note:

It doesn’t stipulate this, but it would be prudent to also set aside a provision for tax on the outstanding housing loan in order to safeguard the fund security. The member spouse would then be liable for any shortfall due to the non-member spouse in terms of the divorce order.

Time periods

The changes to the PFA required certain administrative practicalities to be addressed to ensure that the interest of both the member and the non-member’s spouse were protected. To this effect, Section 37D(4)(b) of the PFA introduced timelines for the orderly administration of divorce orders served on retirement funds.

These can be summarized as follows:

Timeframe	Action Required
45 days from receipt of valid divorce order	Fund must request non-member spouse to make an election on cash payment or transfer to another fund
120 days from being asked to make selection	Non-member spouse must inform fund of choice and provide appropriate detail to facilitate payment (bank account information) or transfer (name and contact details of other fund)
60 days from receipt of non-member spouse’s choice	Fund must pay or transfer the benefit
30 days after expiry of 120 day period	If non-member’s spouse has failed to inform fund of choice, the fund must make payment into non-member spouse’s bank account, unless it does not have such details.
From expiry of 120 day period	If no choice has been made by the non-member spouse and the fund does not have bank details to make payment, fund return must accrue from the expiry of the 120 day period to date of payment

Payment of Interest

Section 37D(4)(c) of the PFA clearly states that the non-member spouse is not a member or beneficiary in relation to the fund and will only be entitled to fund return from the expiry of the 120 days period within which a non-member spouse must make an election until payment or transfer of the pension interest, but not to any other interest or growth.

Example:

- Non-member spouse makes an election after 30 days of being asked to do so.
- The fund gives effect to the election 70 days after receiving his/her election.
- Even though the fund took more than 60 days to give effect to the election, no fund return will accrue because payment was made within the 120 day period.
- Fund return only begins to run after the expiry of the 120 day period and not after the expiry of the 60 day period.
- In terms of the latter provision, the fund must give effect to the election within 60 days of being informed of it, but should the fund not do so, the Act is clear that fund return does not begin to run at the end of the 60 day period, but only at the end of the 120 day period.

The definition of pension interest in the Divorce Act also makes no reference to the payment of interest on the portion of the pension interest allocated to the non-member spouse.

A provision in a divorce order providing for the payment of interest/growth by the member on the portion of the pension interest allocated to the non-member spouse is therefore not enforceable against the fund, but would have been enforceable between the parties.

Transfers Prior to Receiving or Giving Effect to a Valid Divorce Order

If a retirement fund transfers the benefit of a member to another retirement fund before a valid divorce order is served upon it in respect of such a member, the retirement fund to which the transfer was made will be required to give effect to the provisions of the valid divorce order. This would apply to both section 14 transfers and a transfer based on a recognition of transfer (ROT).

Foreign divorcee must seek SA court order

A member who has emigrated and subsequently divorces in that country must apply to a South African court to have the divorce order recognised and enforced in South Africa. This is particularly true if the non-member spouse wants to claim a share of the former spouse's retirement savings.

Income Tax Act

The member and non-member spouse should be aware of the provisions of the Income Tax Act as part of their divorce negotiations.

Current legislation requires the non-member (ex) spouse to pay any tax due on his/her portion taken as a cash lump sum if the divorce order was granted after 13 September 2007 and the deduction was made from the member's pension interest after 1 March 2009. Any transfer to another approved retirement fund will not attract tax at the time of transfer.

Things get a bit more complicated if the valid divorce order was granted before 13 September 2007 and payment is made after that date.

The same tax regime applies to public sector funds and both spouses are to retain the tax free benefits of the member's pre 1 March 1998 years of service.

Summary

The introduction of the clean-break principle in 2009 has significantly changed the way retirement fund benefits can be divided upon divorce and has introduced clear practical processes to facilitate this.

Despite the simplification, many divorcees continue to find themselves having to spend time and money approaching courts to request amendments to remedy poorly worded divorce orders that are not binding on their or their former spouses' retirement funds.

It is extremely important to ensure that you obtain advice from a suitably competent legal advisor when drafting a divorce agreement.

The three most common problems Ensimini experiences with divorce orders are:

- Divorce orders that states that the non-member spouse is entitled to a portion of the member's "provident interest" or "pension or provident fund". It MUST refer to "pension interest".
- Where claims are made against multiple retirement funds to which a divorcee belongs and the divorce order simply

refers to "the funds to which the member belong". It is important that the name of each of the retirement funds be explicitly mentioned as well as the proportion or amount of the "pension interest" in each retirement fund that is due to the non-member spouse.

- The divorce order fails to contain an order to the fund to make payment to the non-member spouse.

Note:

Suggested simplified wording for binding divorce order:

"The [Insert full name and Id number of non-member spouse] is entitled to [Insert agreed percentage or fixed amount] of the pension interest of [Insert name and ID number of member] in the [Insert full name and registration number of fund].

The [Insert full name and registration number of fund] is ordered to pay this amount to the non-member spouse / transfer this amount to the [Insert full name and registration number of the fund to which the transfer is to be made to]".

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