

17 June 2009

LEGAL UPDATE FAW 10/2009: TAXATION OF DIVORCE ORDER PAYMENTS – CURRENT POSITION

Time periods applicable with regards to divorce orders

Section 37D(4)(b) of the Pension Funds Act stipulates the following time periods applicable to divorce orders:

1. Within 45 days of the submission of the court order to the fund, the fund must request the non-member spouse to elect if the amount to be deducted must be paid directly to them or if it must be transferred to a pension fund on their behalf. In this document, this is referred to as the **45 day period**.
2. Within 120 days of being requested to make an election, the non-member spouse must inform the fund of their election. If they elect that the amount must be paid to them directly, they must provide the fund with the details of how payment must be made. If they elect that the amount must be transferred to a pension fund on their behalf, they must provide the fund with the details of that pension fund. In this document, this is referred to as the **120 day period**.
3. If the non-member spouse makes an election, the fund must within 60 days of being informed of how the amount must be dealt with, pay or transfer the amount. In this document, this is referred to as the **60 day period**.
4. If the non-member spouse does not make an election, the fund must within 30 days of the expiry of the 120 day period, pay the amount directly to the non-member spouse. In this document, this is referred to as the **30 day period**.

DIVORCE ORDER GRANTED BEFORE 13 SEPTEMBER 2007

The Financial Services Laws General Amendment Act No. 22 of 2008 amended section 37D of the Pension Funds Act to make it clear that any portion of a member's pension interest allocated to a non-member spouse in terms of a divorce order granted before 13 September 2007 is deemed to accrue to that non-member spouse on 13 September 2007. This provision came into effect on 1 November 2008.

The Revenue Laws Amendment Act No. 60 of 2008 came into effect on 8 January 2009. It includes a new sub-paragraph 4(4) in the Second Schedule to the Income Tax Act dealing with the tax liability to the non-member spouse which applies from 1 March 2009 and provides that accrual takes place on the date that the non-member spouse **makes an election** as to whether the amount concerned should be paid to them directly or transferred on their behalf to another retirement fund in terms of section 37D(4)(b)(ii) of the Pension Funds, or on the date the amount is **payable** in terms of section 37D(4)(b)(iv) of that Act.

Section 37D(4)(b)(ii) of the Pension Funds provides that the non-member spouse must make an election within 120 days of being requested to do so.

Section 37D(4)(b)(iv) provides that in the event of no election by the non-member spouse, the fund must pay the amount directly to the non-member spouse within 30 days of the expiry of the 120 day period within which the non-member spouse should have made an election.

The accrual dates as provided for in the Revenue Laws Amendment Act No. 60 of 2008 for divorce orders granted prior to 13 September 2007, is thus either the date on which the non-member spouse **makes an election** (provided that it is within the 120 day period) or **30 days after the expiry of the 120 day period**.

If the accrual takes place before 1 March 2009, the amount concerned will be taxed at the highest average rate of tax of the current or previous tax year. If it takes place after 1 March 2009, it will be taxed as a withdrawal benefit in accordance with the tax tables applicable then. The intention was for a simplified tax table in respect of withdrawal benefits to be in place with effect from 1 March 2009. In a letter dated 18 March 2009 addressed to ASISA (Association for Savings & Investment SA), the South African Revenue Service (SARS) indicated that the SARS system to operationalise the new rate table will not be in place on 1 March 2009 and that the current system that applies for withdrawal benefits will continue to operate until the system changes can be effected. The only change is that the R1 800 tax deduction has been increased to R22 500. It is expected that the revised system will only be effective towards the middle of this year.

There is currently a discrepancy between the intention of the legislature and the actual legislation as far as the liability for the payment of the tax is concerned.

The intention is that, irrespective of when the divorce order is presented to the fund, the **member** will always be the person to pay the tax on the portion of their pension interest assigned to the non-member spouse in respect of divorce orders prior to 13 September 2007. The member will have a right of recovery of the tax from the non-member spouse.

However, the new sub-paragraph 4(4) in the Second Schedule to the Income Tax Act that was introduced in the Revenue Laws Amendment Act No. 60 of 2008 transfers the tax liability to the non-member spouse in respect of divorce order amounts deducted (within the 120 day period) or paid (30 days after expiry of the 120 day period).

The **current** position in respect of divorce order granted **prior to 13 September 2007** is as follows:

When is accrual?	If non-member spouse makes an election within the 120 day period	Date of election
	If non-member spouse does not make an election within the 120 day period	30 days after expiry of the 120 day period
Who pays the tax?	Non-member spouse	
At what rate?	If accrual before 1 March 2009	Highest average tax rate
	If accrual after 1 March 2009	Withdrawal tax table (not finalised yet)

DIVORCE ORDER GRANTED FROM 13 SEPTEMBER 2007 TO 31 OCTOBER 2008

The Taxation Laws Amendment Act No. 3 of 2008 amended paragraph 2 of the Second Schedule to the Income Tax Act to provide that accrual takes place on the date of the deduction of the amount concerned.

The Pension Funds Act as it read then provided for deduction on the date of receipt of the court order.

The **current** position in respect of divorce order granted **from 13 September 2007 to 31 October 2008** is as follows:

When is accrual?	Date of deduction = date of receipt of court order	
Who pays the tax?	If accrual before 1 March 2009	Member
	If accrual after 1 March 2009	Non-member spouse
At what rate?	If accrual before 1 March 2009	Highest average tax rate
	If accrual after 1 March 2009	Withdrawal tax table (not finalised yet)

DIVORCE ORDER GRANTED FROM 1 NOVEMBER 2008 TO 28 FEBRUARY 2009

The Taxation Laws Amendment Act No. 3 of 2008 amended paragraph 2 of the Second Schedule to the Income Tax Act to provide that accrual takes place on the date of the deduction of the amount concerned.

Section 37D(4)(a)(ii) of the Pension Funds Act was amended with effect from 1 November 2008 to provide for deduction on the date on which the non-member spouse makes an election, or, if no election is made within the 45 day period, the expiry of that 45 day period.

If the accrual takes place before 1 March 2009, the amount concerned will be taxed at the highest average rate of tax of the current or previous tax year, in the hand of the member. The member will have a right of recovery of the tax from the non-member spouse. If it takes place after 1 March 2009, it will be taxed as a withdrawal benefit in accordance with the tax tables applicable then, in the hand of the non-member spouse. As stated above, these tables are not in effect yet.

The **current** position in respect of divorce order granted **from 1 November 2008 to 28 February 2009** is as follows is as follows:

When is accrual?	If non-member spouse makes an election within the 120 day period	Date of election
	If non-member spouse does not make an election within the 120 day period	After expiry of the 45 day period
Who pays the tax?	If accrual before 1 March 2009	Member
	If accrual after 1 March 2009	Non-member spouse
At what rate?	If accrual before 1 March 2009	Highest average tax rate
	If accrual after 1 March 2009	Withdrawal tax table (not finalised yet)

DIVORCE ORDER GRANTED FROM 1 MARCH 2009

The Revenue Laws Amendment Act No. 60 of 2008 shifts the tax liability on divorce order payments to the non-member spouse if the divorce order amount is payable after 1 March 2009. No specific accrual date is mentioned, which means that the normal principles applicable to accrual as established through case law applies. It also provides that where the non-member spouse transfers the amount concerned to a pension fund, pension preservation fund, provident fund, provident preservation fund or retirement annuity fund, this will be a tax free transfer.

The same principles as those applicable in respect of divorce orders granted between 13 September 2007 and 28 February 2009 are accordingly also applicable here.

The **current** position in respect of divorce order granted **from 1 March 2009** is as follows:

When is accrual?	If non-member spouse makes an election within the 120 day period	Date of election
	If non-member spouse does not make an election within the 120 day period	After expiry of the 45 day period
Who pays the tax?	Non-member spouse	
At what rate?	Withdrawal tax table (not finalised yet)	

Hettie Joubert
 Legal adviser at FundsAtWork
 Momentum

Disclaimer:

The information contained in this document is not intended to be legal, tax, or other professional advice. With respect to the content of this document, Momentum Group Ltd does not make any warranty, expressed or implied or statutory, about the accuracy, completeness, or usefulness of any information disclosed herein. Any reliance by you upon any such information obtained in this document is at your sole risk. Finally, in no event will Momentum Group Ltd be liable to anyone for any direct, indirect, special or other consequential damages for any use of information obtained in this document, including lost profits, business interruption, or otherwise.

		Before 13/09/07	13/09/07 – 31/10/08	01/11/08 – 28/02/09	From 01/03/09
Date of deemed accrual		Date of election [within 120 days] / date on which amount is payable [30 days after expiry of 120 days]	Date of deduction [= date of court order]	Date of deduction (s37D(4)(a)(ii) = date election is made [within 120 days] / if no election, date in (4)(b)(i) [45 day period]	Date of deduction (s37D(4)(a)(ii) = date election is made [within 120 days] / if no election, date in (4)(b)(i) [45 day period]
Who pays tax?	Accrual before 01/03/09	Non-member spouse	Member	Member	Non-Member spouse
	Accrual after 01/03/09	Non-Member spouse	Non-Member spouse	Non-Member spouse	
How much?	Accrual before 01/03/09	Highest average rate	Highest average rate	Highest average rate	Withdrawal tax table (not finalised yet)
	Accrual after 01/03/09	Withdrawal tax table (not finalised yet)	Withdrawal tax table (not finalised yet)	Withdrawal tax table (not finalised yet)	
Transfer to another approved fund		Where member already paid tax, transfer gross amount (without deduction of any tax) to new fund	Same as for period before 13/09/07	Same as for period before 13/09/07	Transfer to pension, pension preservation, provident, provident preservation and retirement annuity funds tax free, irrespective of where it came from
Non-member spouse withdrawal from new fund after 01/03/09		<ul style="list-style-type: none"> Where member paid tax, transferred amount = tax free Tax per applicable table on balance of lump sum, subject to 2nd schedule deductions Not aggregated with future lump sum benefits 	<ul style="list-style-type: none"> Where member paid tax, same as for period before 13/09/07 Where non-member spouse paid tax, full lump sum taxable per withdrawal / retirement table, depending on whether it is withdrawal or retirement/death benefit, subject to 2nd schedule deductions Lump sum aggregated with all lump sum benefits after 01/03/09 	<ul style="list-style-type: none"> Where member paid tax, same as for period before 13/09/07 Where non-member spouse paid tax, full lump sum taxable per withdrawal / retirement table, depending on whether it is withdrawal or retirement/death benefit, subject to 2nd schedule deductions Lump sum aggregated with all lump sum benefits after 01/03/09 	<ul style="list-style-type: none"> Full lump sum taxable per withdrawal / retirement table, depending on whether it is withdrawal or retirement/death benefit, subject to 2nd schedule deductions Lump sum aggregated with all lump sum benefits after 01/03/09
Effect on member's lump sum benefit		Aggregated with member's lump sum benefits on future withdrawals, retirement & death	<ul style="list-style-type: none"> Where member paid tax, aggregated with member's lump sum benefits on future withdrawals, retirement & death Where non-member paid tax, no effect 	<ul style="list-style-type: none"> Where member paid tax, aggregated with member's lump sum benefits on future withdrawals, retirement & death Where non-member paid tax, no effect 	No effect