

A decorative graphic in the top left corner consisting of several overlapping, stylized arrow shapes pointing to the right. The arrows are in shades of grey and red.

Legal update

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Withholding of benefits

A. Summary

An employer can request a fund to deduct an amount from a member's pension benefit as compensation for damages caused to the employer as a result of the member's theft, dishonesty, fraud or misconduct. The employer can also ask the fund to withhold the payment of the pension benefit pending the outcome of court proceedings relating to the damages referred to above. The fund will do this if specified requirements are met.

A fund can also withhold payment of a member's pension benefit pending a final maintenance order still to be issued, but not in respect of a divorce order to be issued where the member has exited service (in the case of occupational pension and provident funds).

This legal update deals with the 3 scenarios separately and the legal position applicable in each instance.

B. Deductions in favour of an employer where the member's dishonest conduct caused a loss to the employer

a. **Background**

Due to the socio-economic importance of a pension and to prevent over-reliance on State resources once pension benefits are depleted, the Pension Funds Act ("the Act") affords special protection to pension benefits. Sections 37A and 37D of the Act, as an exception, outlines the allowable deductions that can be made from a pension benefit.

A pension or provident fund may deduct from the pension benefit payable to a member or their beneficiaries an amount not exceeding the amount owed by the member to the employer on the

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date of their retirement or termination of membership before retirement as compensation for certain damages caused to the employer. In addition, the employer may also claim the legal costs (costs for institution of proceedings against the member) incurred in recovering the monies.

b. Section 37D(1)(b) of the Pension Funds Act

The deduction of monies from a pension benefit in favour of an employer, where the dishonest conduct of the member causes loss to the said employer, is regulated by section 37D(1)(b) of the Act. The Courts and the Pension Funds Adjudicator have held that the Act requires the following requirements to be met before a fund may effect a deduction:

1. There must be a pension benefit payable by a pension / provident fund.
2. There must be an amount due by the member to his / her employer on the date of his / her retirement or on the date which he / she ceases to be a member of the fund.
3. The damage caused to the employer must be by reason of theft, dishonesty, fraud or misconduct by the member. The term misconduct in this phrase has consistently been interpreted to mean conduct which contains an element of dishonesty and thus excludes negligent conduct.
4. The member must either admit liability in writing to the employer, or a judgment must be obtained in a court of law. In this regard, the Pension Funds Adjudicator has held that a civil judgment is required and a judgment by the Labour Court will not suffice. Furthermore, where the employee has been convicted of a criminal offense, this on its own is not sufficient. That is, in addition to the criminal conviction, a compensation order issued in terms of the Criminal Procedure Act, as part of the sentence, is required.
5. The judgment or the written admission of liability must relate to the compensation due in respect of the damage caused to the employer by the member's dishonest conduct.
6. The written admission must be made voluntarily and hence there must be no duress or undue influence.
7. The specific amount of compensation or damages suffered must be outlined in the written admission or court judgment.

c. Withholding pending litigation

While the law permits the deduction from pension benefits due to dishonest conduct of the employee, the difficulties faced by most employers is that at the time of termination of the employment contract, the employer will not have obtained a civil judgment. Thus, the issue in law was whether the section can be interpreted to mean the fund can withhold the benefit pending the outcome of litigation against the member.

The Supreme Court of Appeal in *Highveld Steel and Vanadium Corporation Ltd v Oosthuizen* [2008] ZA SCA acknowledged that practical problems threaten the very purpose and remedy afforded by this section, in that in most instances, if not all, employers only suspect dishonesty on the termination of the employee's employment contract, with the result that pension benefits are paid before the suspected dishonesty can be properly investigated, let alone quantified and proven. Furthermore, in most instances the employer would not have obtained a judgment against the employee by the time the employment contract is terminated due to the lengthy delays in the justice system. As a result of the above, the employer will find it difficult to enforce an award made in its favour by the time judgment is obtained.

The words "has in writing admitted liability" and "judgment has been obtained" in section 37D(1)(b)(ii)(aa) and (bb), both of which are in the past tense, reflects the intention that the proof of liability must be available on termination of the employment contract. According to the court, such a literal interpretation would render the protection afforded by this section meaningless and thus could not have been intended by the legislature. With approval of the approaches adopted by the Pension Funds Adjudicator in several determinations, the court held that in order to give effect to the specific purpose of this section, the wording must be interpreted purposively to include the power to withhold payment of a member's pension benefit pending the determination of such member's liability in a court of law. Thus, the funds have discretion to withhold payments of the pension benefits.

In accordance with the above rulings, the General Rules of the FundsAtWork Umbrella Pension and Provident Funds (the Funds) allow the Funds to withhold the payment of the benefit pending the outcome of the court proceedings.

d. Practical and procedural steps to be taken by the employer

Upon termination of the employment contract, where the employee's dishonest conduct has caused loss to the employer and the employer has or will within a short period institute civil or criminal proceedings against the member, the employer can request the fund/s to withhold the benefit.

The employer has to immediately address this request to the fund in writing and provide information relating to:

1. The nature of the damage (i.e. type of dishonest conduct) caused by the member.
2. The rand value of the damage suffered by the employer.
3. When the employer started with its investigation into the member's misconduct.
4. When legal, criminal or civil or both, proceedings were instituted and if not – why not.

5. The SAPS case no, SAPS station, investigating officer and the date on which the charges were laid (if applicable).
6. The amount claimed in the civil court action.
7. A copy of the summons / notice of motion/letters of demand, if applicable.
8. How far proceedings have progressed.
9. When the member's employment was terminated.
10. Other relevant factors.

The employer cannot refuse to complete the withdrawal notification as a way of ensuring that the benefit is not paid. Employers should also not move members to a preservation fund if the member owes money to the employer due to theft, fraud, dishonesty or misconduct. The consequence of this is that the member will be allowed to withdraw from the preservation fund and take their entire benefit and as such the employer loses the right to lay claim to that benefit. Instead, the employer should complete the withdrawal forms and indicate that it has a claim against the member under section 37D of the Pension Funds Act or submit a request for withholding as outlined above.

e. Steps to be taken by the fund

Once the information mentioned above has been received, the fund can then make a decision as to whether it should withhold the benefit or not. In deciding whether to withhold the benefit, the fund must consider various factors such as (but not limited to):

1. The substantive requirements outlined above.
2. The value of the benefit.
3. The losses suffered by the employer, including legal costs for recovery.
4. If the employer has taken reasonable steps to institute proceedings.
5. If there has been any unreasonable delay on the part of the employer in prosecuting the claim.

Where the fund decides to withhold the benefit, in accordance with the fund rules, the benefit will be invested in the portfolio chosen by the trustees for this purpose. Once proceedings have been finalised, the fund will make a final decision as to whether it can deduct from the benefit.

C. Divorce orders – can the fund withhold payment of a member's benefit pending a divorce order still to be issued?

Section 7(7) of the Divorce Act, read together with Section 37D(1)(d)(i) of the Pension Funds Act, provides for a deduction from the member's pension interest, in favour of the non-member spouse, if the

fund is in receipt of a final divorce order that is binding on the fund. In the case where the member's participation in the fund has come to an end before the divorce order has been granted, there is no obligation on the fund to withhold the benefit. In this case, the fund should pay the member's benefit to him.

This means that if the member withdraws prior to the divorce order being granted, the pension interest no longer lies with the fund, but has accrued to the member. The fund would therefore not be in a position to withhold the member's benefit to effect a deduction in terms of a divorce order still to be issued.

In *Naidoo v Feralloys Provident Fund* (PFA/KZN/9694/2006/AM 31 July 2008 (PFA)), the member had left the employer's service and summons for divorce had been served. The non-member spouse requested the fund to withhold the benefit pending the outcome of the divorce proceedings. The member was unhappy with this decision and lodged a complaint. The Pension Funds Adjudicator, based on the above reasoning, held that there was no basis for the fund to withhold the benefit.

The position was recently confirmed by the Pension Funds Adjudicator in *Williams v Alexander Forbes Retirement Fund (Pension Section) and Another* 17 October 2012 (PFA), wherein it was held as follows:

- “5.6 In this matter, the member spouse (Mr. Williams) withdrew from the fund in March 2010 and as a result became entitled to receive his fund credit in terms of the fund rules. The divorce order was only granted on 29 November 2010 after Mr. Williams had already been paid his fund credit. Thus, there was no pension interest payable to the complainant as at the date of divorce. The final divorce order that was issued on 29 November 2010 is not valid and enforceable against the first respondent as it holds no pension interest in respect of Mr. Williams.
- 5.7 The definition of “pension interest” above refers to a notional benefit that would have been payable to the member spouse had his membership terminated at the date of divorce. This means that the member spouse must still hold a pension interest in the fund as at the date of divorce. As confirmed in the matter of *Eskom Pension and Provident Fund v Krugel*, once the pension benefit has accrued to the member spouse before the date of divorce, the provisions of sections 7(7) and 7(8) of the Divorce Act are no longer applicable. Put simply, there is no pension interest for purposes of sections 7(7) and 7(8) of the Divorce Act and section 37D(4)(a) of the Act.
- 5.8 The fact that there was an interdict preventing the payment of any benefit to Mr. Williams does not detract from the fact that there was no valid and binding divorce order as at the date of his exit from the fund. The first respondent was bound in terms of its rules to pay Mr. Williams his full fund credit upon his withdrawal.”

As a result of the above, whilst the non-member spouse may have a personal claim against the member, as the member left service prior to the anticipated date of divorce, the aforesaid provisions regulating the assignment of pension interest do not apply. Hence, any order assigning pension interest will not be enforceable against the fund. The fund can therefore not withhold payment of the benefit pending the final divorce order to be issued. Refer to Legal Update 6/2015 - Divorce order issues relating to a member's pension interest for more information.

D. Maintenance orders – can the fund withhold payment of a member's benefit pending a final maintenance order to be issued?

Section 26(4) of the Maintenance Act, read together with Section 37D(1)(d)(iA) of the Pension Funds Act, provides for a deduction from the member's pension interest, in favour of the non-member spouse and/or the member's child, if the fund is in receipt of a final maintenance order that is binding on the fund.

Section 26(4) makes it clear that a court has the power to attach a pension benefit for the *arrear* maintenance of a child. What was not clear, was whether or not the same can be done in respect of *future* maintenance. The Durban court in *Mngadi v Beacon Sweets and Chocolates Provident Fund* established that South African courts have a legal obligation to also enforce orders that deal with the future maintenance of a child. In order for such an application to succeed, the applicant must show that the defaulting member has a history of failure to take maintenance responsibilities seriously. In this far-reaching decision, the High Court ordered the fund to retain the withdrawal benefit due to the father of two minor children and to use the benefit to pay maintenance monthly to their mother until they no longer require support and maintenance. Thereafter, the balance of the benefit (if any) must be paid to the father or his estate. This principle has been confirmed in a series of subsequent High Court rulings.

Another question that arises is whether or not a fund is allowed to withhold a pension benefit or a part of it pending the finalisation of a maintenance claim. Opinion is divided on whether the fund may legally withhold the benefit in these circumstances. On the strength of rulings by the courts in accepting that there can be a claim for future maintenance (including the strong emphasis on courts taking all possible steps to protect the rights of children as the interests of a child is always paramount in matters dealing with children) and the approach taken by the courts and the Pension Funds Adjudicator on the issue of withholding of benefits to secure the employer's claims pending civil or criminal proceedings, one can make a compelling argument supporting the withholding of the benefit pending the maintenance inquiry. The General Rules of the FundsAtWork Umbrella Pension and Provident Funds allow the Funds to withhold the payment of the benefit pending the outcome of the maintenance court proceedings. In terms of the Rules, where the maintenance court or the person claiming maintenance informs the Funds in writing of a claim and if the funds are satisfied that the proceedings will be finalised within a reasonable period, then it can withhold the benefit (or part thereof) to satisfy the claim.

In conclusion, maintenance creditors may request the fund to withhold the benefit to secure any future order that could be granted by the court.

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