

Abused or not? Trust (un)certainities caused by the SCA at divorce

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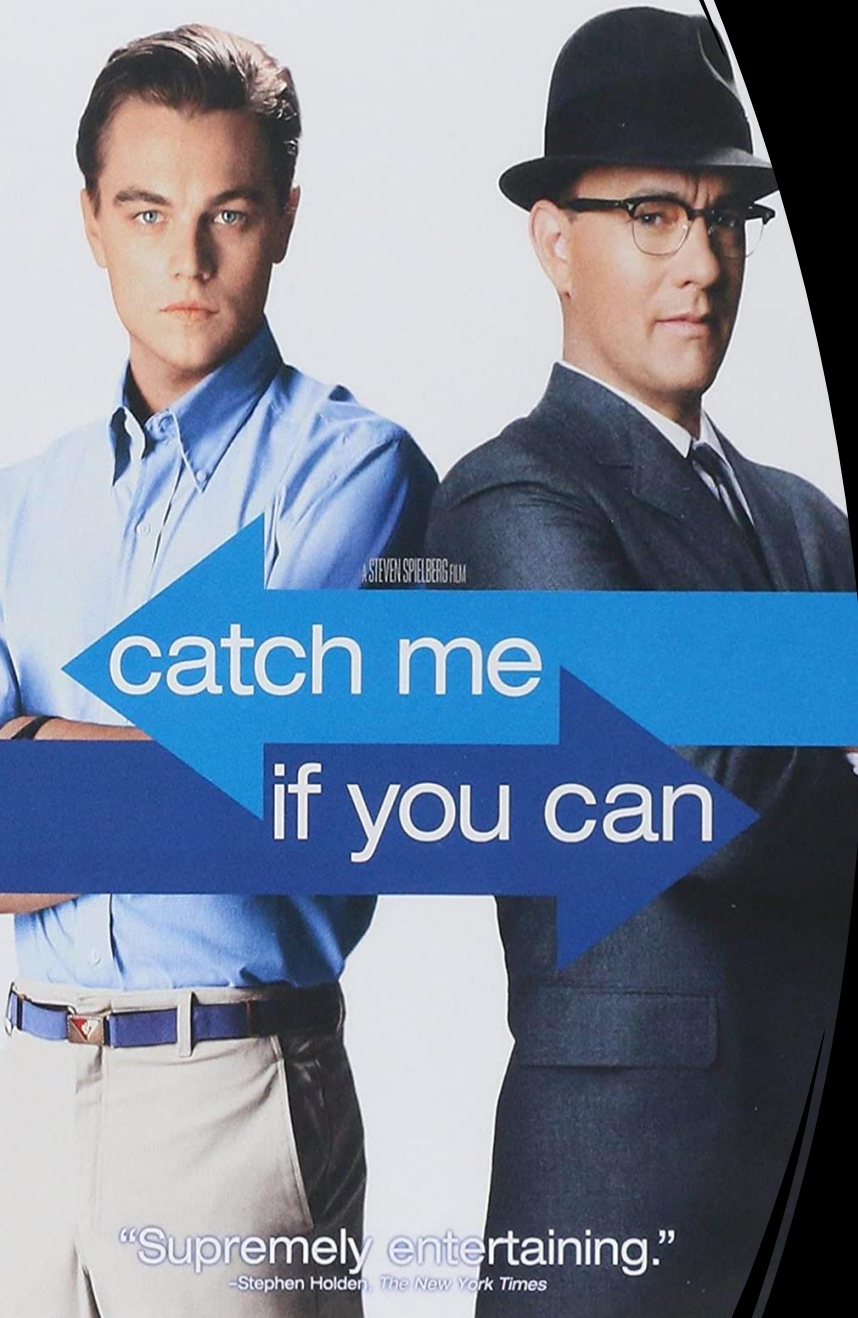


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Certainty ①:

“Divorce planning” is a frequent phenomenon ...



Gorven AJA in *B v B* [2014] ZASCA 137 para [39]:

“The attitude of many [divorcing] parties, particularly in relation to money claims where they control the money, can be characterised as “catch me if you can”. These parties set themselves up as immovable objects in the hope that they will wear down the other party. They use every means to do so ... *in the hope that they will not be caught and have to disgorge what is in law due to the other party.*”

Prof Jacqueline Heaton:

“[Family trusts] are often created for purposes of estate planning, tax avoidance, or to protect assets from creditors, *including the founder’s spouse*. ... **[But a] family trust** may turn out to be a handy vehicle for **‘divorce planning’** *because transferring property to the trust reduces the scope of a person’s estate and consequently limits (or even eliminates) any claim the person’s spouse may have against him or her on divorce.*”

(Heaton in Atkin and Banda (eds) *The International Survey of Family Law* (2015)
311 at 313, emphasis supplied)

- *Parker* case (SCA): Family trusts are especially prone to abuse, because:
 - the trustees are often also beneficiaries, and
 - the beneficiaries are related to one another.

Certainty ②:

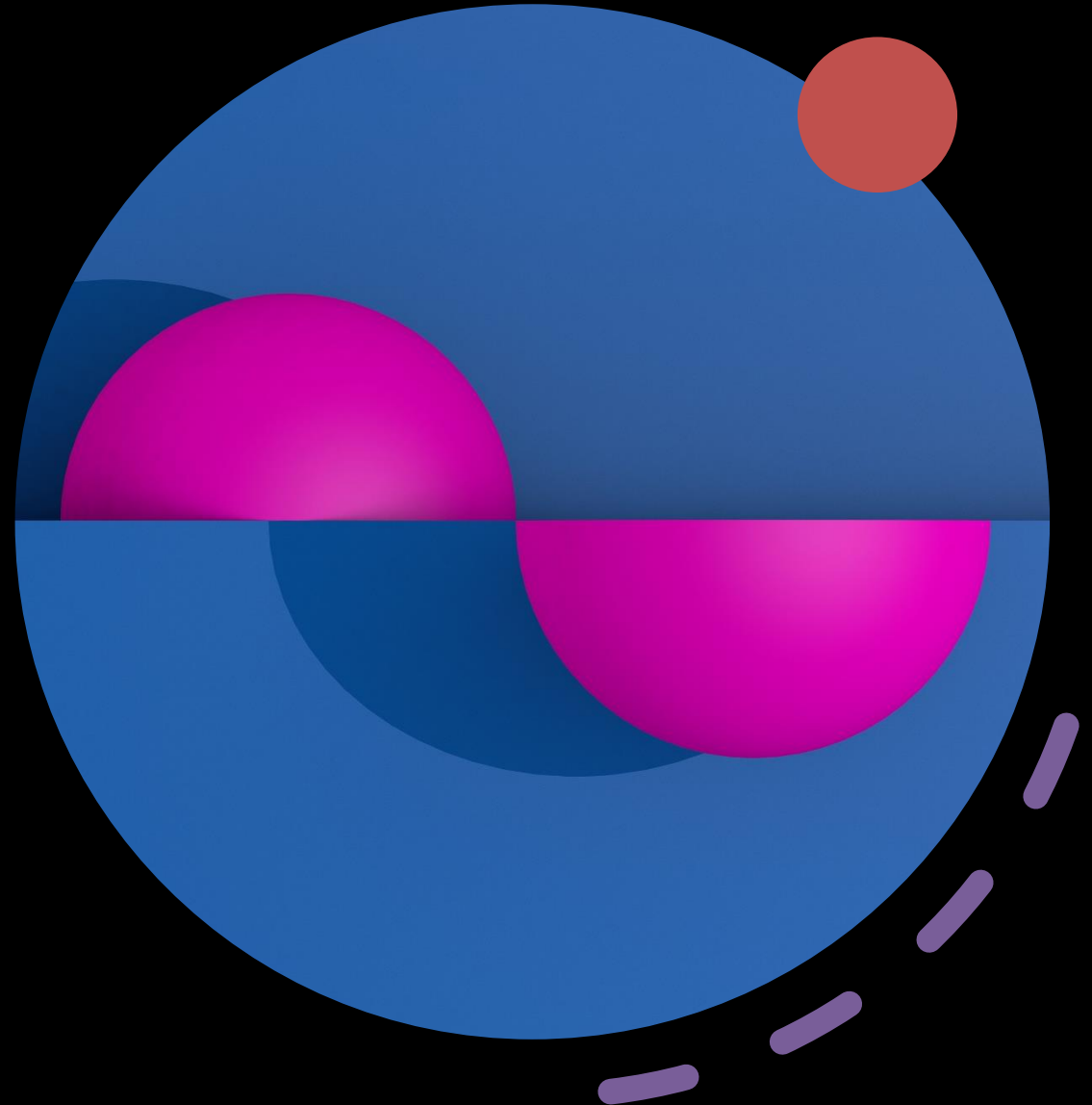
The “core idea” of SA trust law and golden rules of trusteeship

KEY PRINCIPLE:

The **“CORE IDEA”** of SA trust:

There must at all times be a **SEPARATION** of **ownership** (or **CONTROL**) of trust assets by **trustees**, from **ENJOYMENT** of trust benefits by **beneficiaries**:

(*Landbank v Parker*
2005 (2) SA 77 (SCA)).



Golden rules of trusteeship

- (i) Trustee must exercise an **independent discretion**;
- (ii) Trustee must **give effect to the trust deed**;
- (iii) Trustee must **act with care, diligence and skill** in performing duties/exercising powers;
- (iv) Must adhere to the **joint-action rule**.

Certainty ③:

Various **forms of trust abuse** are recognised in our
law

(See Cameron *et al Honoré's South African Law of Trusts* 6th ed (2018) 311,
312)

TRUST ABUSE: Typically two forms:

(1) Trust (ab)used for **dishonest or unconscionable purpose of evading a liability or avoiding an obligation** (e.g. contractual liability). (Eg: *Hydraberg Hydraulics* 2010 (5) SA 555 (WCC))

AND / OR:

(2) Trust is treated as the ***alter ego*** of the founder / trustee / trustee-beneficiary:

→ Treating trust property **AS IF** his/her **own personal property**;

→ **BREACH OF “CORE IDEA”** of trust and **golden rules**.

→ **NB!!** *Honoré* “**Leading case**” is *Badenhorst*

(Un)certainty ①:

Abused trusts and divorce: Do different tests apply depending on the specific matrimonial property regime?

Trust assets and Divorce



- Starting point:

Badenhorst v Badenhorst 2006 (2) SA 255 (SCA)

- Parties married with **complete separation of property** in 1981;
- Wife (appellant) sought a **redistribution of assets order** (§ 7(3) – (6) Divorce Act 70/1979) and wanted **trust assets** to be taken into account as part of husband's estate.

NB!! SCA: “Control Test”

“To succeed in a claim that trust assets be included in the estate of one of the parties to a marriage there needs to be **evidence that such party controlled the trust and but for the trust would have acquired and owned the assets in his own name**. Control must be **de facto** and not necessarily **de iure**.”

To determine whether a party has such **de facto** control:

- (i) Terms of the **trust deed**, and
- (ii) Evidence of **how the affairs of the trust were conducted** during the marriage.



- *Because this test complied with:*
 - VALUE of trust assets were added to husband's personal estate to calculate redistribution amount owed to his wife
- **BUT:** Badenhorst created **confusion**:
 - Is “control test” in *Badenhorst* confined to marriages contemplated in § 7(3) of the Divorce Act?
 - Conflicting case law on this question (even in the SCA)!

THEN: ACCRUAL CLAIMS:

Can trust assets be considered to calculate accrual?

- Early conflicting High Court judgments until 2017;
- Then: **REM v VM** 2017 (3) SA 371 (SCA):
- **Different TEST** prescribed in **accrual** context:

Aggrieved spouse must prove that the other spouse:

“transferred personal assets to [the trust] and dealt with them as if they were assets of [the trust] with the fraudulent or dishonest purpose of avoiding his obligation to properly account to the [aggrieved spouse] for the accrual of his estate and thereby evade payment of what was due to [her], in accordance with her accrual claim.”

- **REM “TEST”**: Two processes involved:
 - 1) Is the trust *an alter ego trust*? “as if”
Answer: Use “control test” as set out in *Badenhorst*
 - 2) *If so*, was trust *unconscionably abused to evade an obligation imposed by matrimonial property law*?
- In the case of the *accrual system*, this obligation is **to PROPERLY ACCOUNT** to the other spouse *for the accrual of one’s estate*:
 - ➔ **Trust form** has therefore been “abused” to evade payment of what is **RIGHTFULLY DUE** to the other spouse.

Thus: Process *seemed* to be quite clear, and **REM** was initially **hailed as a victory!** (See e.g. Smith 2017 SALJ 715 – 729).

BUT, with the benefit of hindsight ... was ***REM***
merely a **pyrrhic victory**?

Nevertheless: Positive law position after **REM**:

- In divorces involving redistribution orders:
 - Only use “control test” in *Badenhorst*;
- In divorces involving accrual system:
 - Use two-stage “REM test”.

QUESTION: Is this differentiation sensible / justifiable?

(Un)certainty ②:

What is the impact of the *SCA's* 2022 judgment in
PAF v SCF?

- Before 2022: All case law dealt with a *trustee-spouse* who allegedly **controlled** trust as his/her *alter ego*.
- But, in the wake of *Badenhorst* and *REM* an important question arose:
 - What about a trust where the spouse exercises **NO control**?

PAF v SCF 2022 (6) SA 162 (SCA)



A CUNNING PLAN

- **Facts:**
 - Married with **accrual system** in 2001;
 - **But, 3 weeks before divorce trial**, husband (applicant) created a trust in the British Virgin Islands;
 - A day later, he donated R 2,2 million to trust (£ 115 000);
 - Brother was sole trustee;
 - Daughter was sole beneficiary (apparently for her maintenance);
 - Wife (respondent): Creation of trust and donation = **abuse of trust form** to **reduce her accrual claim**

SCA (unanimous, *per* Makgoka JA):

- Power to pierce an abused trust's veneer **derives from common law** and has nothing to do with *Divorce Act* or *Matrimonial Property Act*;
- **NB!!!** Interestingly, *PAF* does not cite *REM* test;

Instead: Holds that **control test** in *Badenhorst* also to be used where accrual system applies !!!!

→ **Why ?** Because (i) both spouses have a “**protectable contingent right**” to accrual sharing **during** the marriage, **and** (ii) both redistribution orders and accrual system “**have as their objective, equitable and fair patrimonial consequences of a marriage**”

→ **BUT,** on the facts, the **control test** does **NOT** find application!

→ **What now?**

- There is a **SOLUTION**, provided by a **PROVISO** mentioned in *Badenhorst* :
 - *After* setting out “control test”, court remarked as follows:



“... It may be that in terms of the trust deed **some or all the assets are beyond the control of the founder**, for instance where a vesting has taken place by a beneficiary, such as a charitable institution accepting the benefit. In such a case, provided the party **had not made the bequest with the intention of frustrating the wife’s or husband’s claim** . . . the asset or assets concerned **cannot** be taken into account.”

As such:

- **Absence of control by a spouse** does **NOT** necessarily exclude **abuse** of trust form;
- **Significant progress made:** A “court must **vigilantly examine the facts in each case** to determine allegations of trust form abuse”:
 - Courts now given **wide discretion!!**
- ∴ **New paradigm created** – trust abuse no longer **confined** to “**typical**” *alter ego* scenario (as in all previous cases);
- **But TEST is then:** Were assets transferred to the trust ***with the intention of frustrating the other spouse’s accrual claim?***
- **FACTS** of case confirmed this.

Uncertainty ③:

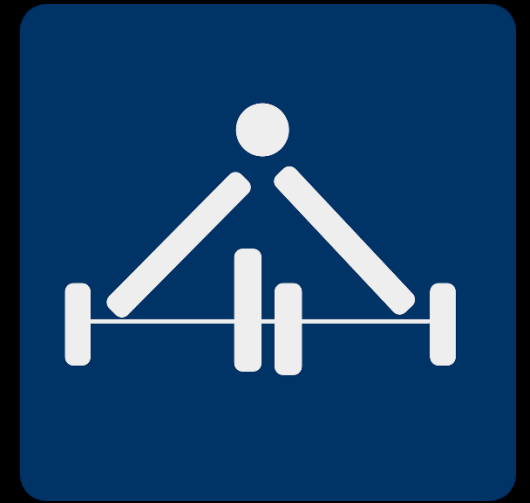
Given *PAF*, should the “control test” in *Badenhorst* also be applied to accrual marriages instead of the “*REM Test*”?

This question posed at FISA 2022 ...

After *PAF*, a new “grey area” emerges ...

- Given *PAF* case’s reliance on *Badenhorst* in **accrual context** **what is the status of the *REM* Test?**
 - Remember: *REM*: **Two-stage** test for **accrual** marriages:
 - Must prove *alter ego* **AND** trust unconscionably abused *to evade an obligation imposed by matrimonial property law*
 - **But**, as held in *PAF*, should compliance with “**control test**” **alone not be sufficient** in accrual cases too?
 - Was *REM* case truly a victory, or should this test **be jettisoned?**

The problem:



- **REM test** places an unacceptably arduous burden on spouses married with accrual system:
 - Effectively requires a spouse to prove **BOTH FORMS** of trust abuse ... “**catch me if you can!**”
- In fact, 7 years later, **I am not aware of any case** in which a spouse has successfully relied on **REM test!**

- My argument after PAF :
 - ➔ In **accrual** context:
Compliance with **“control test”** (eg by **ignoring difference** between trust assets and personal assets) **must IPSO FACTO show** that a spouse’s personal accrual has been **undervalued**; **AND**
- It must therefore **AUTOMATICALLY follow** that the trust form was abused **to evade the obligation to render a proper accounting of that spouse’s accrual ...**

Uncertainty ④:

Has the **progress** in *PAF v SCF* potentially been undermined by the SCA's **latest judgment** on point?

Just when we thought progress was being made ...

- SCA delivers **MJK v IIK** 2023 (2) SA 158 (SCA) (unanimous)
- Also a marriage involving **accrual** system
- Decided only **5 weeks after PAF**
- Although court refers to *PAF*, it **misinterprets / overlooks** the key findings in that case:
 - Court **fails to engage with PAF's finding that "control test"** can be also applied in accrual marriages; and in fact criticizes court *a quo* for doing so!
- **Superficial and unconvincing** engagement with *PAF* → creates a problematic **inconsistency** between **SCA's own judgments!!!**
(See Smith *THRHR* 2023 pp 491 – 503 for criticism of case)

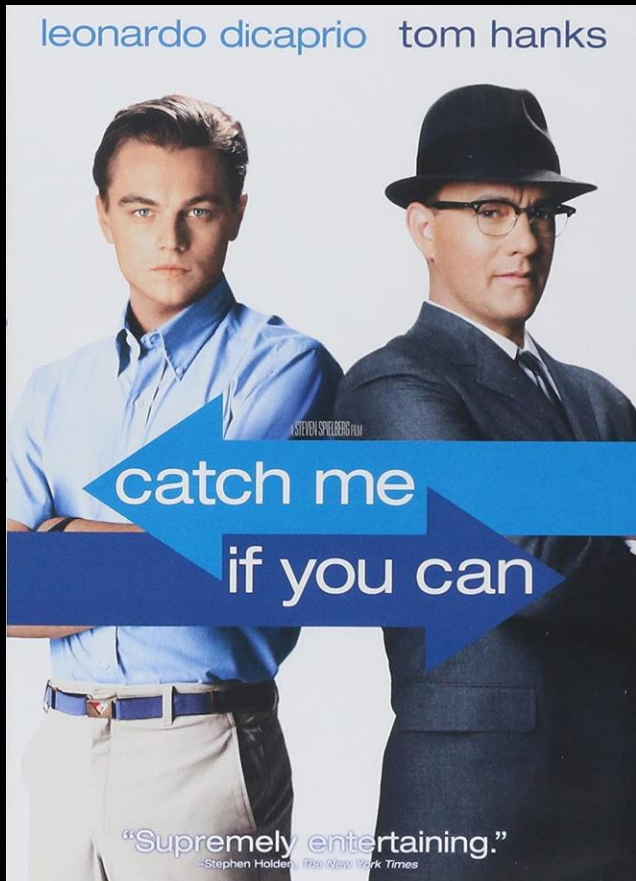
Has the progress made in *PAF* been undermined?

ONLY TIME WILL TELL !!!

Conclusions and the way forward



- 1) We have seen **progress** in terms of combating **unscrupulous “divorce planning”** – cases such as **Badenhorst** and **PAF** have been **trailblazing** in this regard;
- 2) The position regarding the **correct test** to be applied in **accrual marriages** remains **uncertain**:
 - ➔ Compare **REM**, **PAF** and **MJK** cases;
- 3) My view: **Litigation needed** to **confirm application of “control test”** in **accrual marriages** for reasons mentioned.



Bottom line: The “control test” issue is merely one of the uncertainties that persists in this area, but clarification will help to change the approach of “catch me if you can” to “**If you abuse the trust form, you’ve already caught yourself ...**”

THANK YOU !!!

Acknowledgements:

- “Catch Me If You Can': The Casting of the Film” © 2003 Paramount Pictures. (Accessed from https://www.imdb.com/title/tt0923573/mediaviewer/rm547875585/?ref=tt_ov_i 26/7/2023).
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