

Balancing fairness

Kathryn Mason reviews the approach to pension assets accrued prior to marriage, including the significance of needs



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This article considers the courts' treatment of pre-marital pension contributions in financial remedy cases. With the implementation of automatic enrolment, and the increased age at which parties are marrying, it is now likely that the courts will see an increase in arguments in respect of pre-marital pension pots.

The pension is often one of the largest assets in the matrimonial pot, second only to the matrimonial home. There has been a focus on increasing payments into pension funds from a younger age through the introduction of automatic enrolment, which is being rolled out across all employers (subject to limited exceptions) in the UK. Automatic enrolment is available to all eligible jobholders and it is hoped that it will lead to more people making contributions to their pensions from a younger age. Meanwhile, according to statistics released by the Office of National Statistics, the age at which people get married is increasing (see: www.legalease.co.uk/ons-marriages). As pension contributions are made from a younger age it seems very likely that pre-marital contributions to pension schemes will be on the rise.

General principles

The pension is often an asset 'sacrificed' by the financially weaker party, especially in circumstances where one party gives up their career to take on the role of homemaker. The difficulty is not just the amount of money paid into the pension, but the benefit a pension can confer both on retirement and on death (for example, through the provision of a widow's pension). Pensions are a hybrid asset, they are neither pure capital nor pure income. Changes with effect from 2015 mean that it is now possible, under

defined contribution schemes, for the pensioner to take the money out of the pension scheme as a capital lump sum (draw-down). Pensioners aged 55 or over may take the first 25% tax free. Thereafter, the balance will be taxable at the marginal rate. The courts will therefore now, depending on the age of the parties, also have to consider how much a pensioner may be able to take as a capital sum, and the flexibility under the pension scheme.

The courts have the following powers in relation to pensions:

- to make a pension sharing order pursuant to s24B, Matrimonial Causes Act 1973 (MCA 1973) in cases where the divorce petition was filed after 1 December 2000;
- to make a pension attachment order pursuant to ss25B-25D, MCA 1973 in cases where the divorce petition was filed on or after 1 July 1996 (note that pension attachment orders are available in judicial separation cases, but pension sharing orders are not); and
- to apply offsetting pursuant to s25B and 25C, MCA 1973.

When might pension contributions be non-matrimonial assets?

Following *White v White* [2000], the court will look to achieve fairness between the parties after assessing the s25, MCA 1973 factors by testing any proposed financial order against the yardstick of equality, with a departure from equality being justified only where there is good reason to do so.

Non-matrimonial assets are considered to be a good reason to

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depart from the equal division of the assets, but only if the parties' needs have been met. The court in *Hart v Hart* [2017] considered that (para 2):

Non-matrimonial property can... be broadly defined in the negative, namely as being assets (or that part of the value of an asset) which are not the financial product of or generated by the parties' endeavours during the marriage.

Pension contributions made prior to the marriage fall into the category of assets that have not been 'the financial product of or generated by the endeavours during the marriage'. Unless the parties marry at a very young age, there may already have been significant contributions paid into the pension scheme.

Case law

Straight-line discount for pre-marital pensions

When considering the treatment of pre-marital pensions, the decision in *H v H* [1993] is often cited. Thorpe J (as he then was) held:

... in deciding what weight to attach to pension rights it is more important in this case to look to the value of what has been earned during cohabitation than to look to the prospective value of what may be earned over the course of the 25 or 30 years between separation and retirement age.

Thorpe J said that it was more important to look at the value of the pensions earned during cohabitation than to look at the value of the pension which could be earned in the future. *H v H* introduced the straight-line discount, which has been applied to pre-marital pension contributions. The straight-line discount effectively looks at the amount of discount to be applied to the pensions, by dividing the period of cohabitation by the period of contributions.

The application of the straight-line discount as in *H v H* may not find favour with all judges in respect of pre-marital contributions to pension schemes for a number of reasons:

- the straight-line discount may result in an unfair outcome if applied to some pensions – pension accrual at the end of

the marriage may have a greater value than the pre-marital contributions, and inflationary factors and growth on returns of investments funds may be problematic;

- the discount in *H v H* was applied in a case that dealt with, and contrasted, the pension accrued post-separation with

pension portfolio continued to increase in value and in 2001, he converted the pension funds into a commercial property portfolio, with a 'pension wrapper'. During the course of the seven-year marriage, the husband liquidated the pension funds and sold the relevant commercial properties in order to purchase other assets. The value of the assets taken out of the pension fund increased to £3.6m.

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that accrued during periods of cohabitation and did not, therefore, specifically refer to the treatment of pre-marital contributions;

- the case predates pension sharing orders and *White*; and
- the same judge later took a different approach, stating in *Harris v Harris* [2001]:

... I think that in deciding what weight to attach to pension rights it is more important in this case to look to the value of what has been earned during cohabitation than to look to the prospective value of what may be earned over the course of the 25 or 30 years between separation and retirement age.

Whether pension funds have been converted into matrimonial assets

When looking at pre-marital contributions to a pension, the court will carefully consider the use of the pension fund during the marriage. In *FS v JS* [2006], the court had to consider how to treat pre-marital pension assets that had been taken out of the pension fund and liquidated/sold, with the proceeds funding the purchase of commercial properties (as a self-invested pension fund (SIP)). At the time of the marriage in 1997, the husband was 52 and the wife some 20 years younger. This was the husband's second marriage. At the outset of the marriage, the husband had amassed a significant pension portfolio. The

The husband argued that the properties were non-matrimonial assets, as they had been funded by his pre-marital pension, but the judge, Burton J, was not with the husband, saying (at para 34):

Had the pension funds remained as they were, with the seemingly substantial increase in value since 1998 from £435,000 to £972,528, they would, in my judgment, have remained *pre-matrimonial*, and therefore non-matrimonial, property. However, they were liquidated, just as the other commercial properties were sold, and the respondent [husband] entered into the exercise of replacing the sold properties, but above all investing the substantial cash in properties which have, indeed, proved very successful investments.

This case should serve as a stark warning to parties considering converting funds from one type of asset to another; Burton J concluded that taking the pension funds out of the pension scheme effectively converted the funds into matrimonial property.

Whether the parties' needs have been met

The court will cross-check any award against the parties' needs. In *GS v L* [2011], King J excluded the husband's pre-marital pension before he divided the assets equally, on the basis that the pension could

not meet the wife's needs in the short or the medium future, saying (at para 86):

So far as the pension is concerned, it can and should in my judgment properly be excluded from the division of the assets, a position effectively,

judgment requires that the husband should retain his pension fund absolutely.

It is worth noting that in this case, the wife's needs had been met by other capital assets, some of which had also been non-matrimonial.

Non-matrimonial assets are considered to be a good reason to depart from the equal division of the assets, but only if the parties' needs have been met.

although not absolutely, conceded by the wife. The pension cannot be drawn down for many years and was accrued in its entirety before the marriage; the fund cannot be used to provide for the wife's needs in either the short or medium term. Given the benefit of the capital with which she will leave the marriage and a working life of 25 years ahead of her, fairness in my

Had it not been possible to meet the wife's needs from other assets, the court may well have been inclined to consider the pre-marital contributions to the pension scheme.

The parties' needs were again considered in *M v M* [2015], which was a sharing case. The parties married in 1986. At the time of the marriage, the wife was 29 and the husband was

42. The marriage came to an end in 2008. The parties had two children, now adults. Having been separated for five years, the wife issued divorce and financial proceedings. A few months later, she sadly discovered that she had ovarian cancer. One of the key issues in the case was how the court should treat the pension. It was agreed that approximately 80% of the pension had been acquired during the marriage. The judge calculated that the difference between the pre-marital and the marital pension was £84,935.70. Considering the facts of the case and the type of pension, the judge found that he was not in a position to engage in an uplift for the pre-marital value in the manner of *Jones v Jones* [2011]. Further the court considered that it was not possible to calculate the pension accrual that would have accelerated during the currency of the marriage because there would be a marked increase in pension accrual towards the end period before the pension is drawn.

In approaching the pension, the court relied on its discretion and

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determined that in a case looking at entitlement and not need, the court was able to apply a discount for the pre-marital acquisition. HHJ Wildblood QC held that:

The extent of the discount is not capable of being proved on actuarial figures on a strict mathematical basis and so there must be an element of discretion.

Overall, the court divided the assets such that there was a 55/45 division in favour of the husband considering that the division satisfied the needs of both parties.

Standard of proof

The decision in *B v B* [2012] made it clear that the onus of proof is on the person seeking to run a pre-matrimonial asset argument. In that case the parties had married on 16 May 1997, having cohabited since March 1993. The husband attempted to run an argument that the entire value of his SIP had been acquired pre-1993, so was pre-marital. He failed to produce adequate evidence of the value of the pension scheme in 1993 so the SIP was treated as matrimonial, with Mr David Salter, sitting as a deputy High Court judge, finding that he had ‘no means of assessing the value of such rights as at 1993’, so he ignored the husband’s arguments in respect of the pre-marital contributions and emphasised Mostyn J’s view in *N v F* [2011] that:

... if a party is going to exert the existence of pre-marital assets then it is incumbent on him to prove the same by clear documentary evidence.

Hart v Hart

The approach of the court in *Hart* applied only to sharing cases, per Moylan LJ who said:

... this case concerns the approach which the court should take to non-matrimonial property when determining a financial remedy claim by application of the sharing principle. I emphasise that what I say in this judgment, is confined to this principle

The case concerned the proper division of assets for the parties who had met in 1979 and married in 1983,

separating in 2006. It was accepted by the wife that at the time of the marriage, the husband was a ‘man of substance’. The husband argued that the court should depart from an equal division of the assets, and on that basis the judge at first instance had awarded the wife 37% of the assets.

In the Court of Appeal, the wife’s appeal was dismissed. Moylan LJ said that the:

... sharing principle applies with force to matrimonial property but does not apply, or applies with significantly less force, to non-matrimonial property.

Turning to the approach the court takes when dealing with non-matrimonial property, he said (at para 68):

Put in simple terms, the court ultimately has to decide, as part of the discretionary exercise, how to weigh or reflect the existence of non-matrimonial property when determining the award. A key question which has emerged, and which is engaged in the current case, is whether this should be undertaken in a formulaic manner or whether the court can adopt a broader approach.

Ultimately, the Court of Appeal found that the judge at first instance had ‘independently conducted an overview of the case to ensure that his proposed award was fair’.

Conclusions

Although the decision in *Hart* was widely reported in the media as leaving the law in a state of flux, the judgment reinforces the discretionary element in family law proceedings. For that reason, it would seem unlikely that the courts will take a dramatically different approach to pre-marital pensions. The key, as shown across all the case law, will be in cross-checking the parties’ needs and ensuring that those needs have been met. In cases that are needs driven, the ring-fencing of non-matrimonial assets, including

pre-marital contributions to pensions, will be difficult to justify. A case based on sharing will typically be approached differently, and the court may use its discretion to justify a departure from equality and the exclusion of pre-marital contributions to pensions. Other factors that may affect the court’s judgment in respect of pre-marital contributions include whether the parties took the money

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out of the pension, thus potentially changing its status. The court will expect evidence before it in respect of the pre-marital pension contributions, and the onus will be on the party exerting the existence of non-matrimonial contributions to provide the evidence (although it may be noted that in *Hart*, Moylan LJ said (at para 91) that he disagreed with the approach of Mostyn J in *N v F* and that ‘the normal evidential rules apply. These include the court’s ability to draw inferences if such are warranted’). In cases where pensions are a significant asset, and where contributions have been made prior to the marriage, it would be sensible for the parties to instruct a pensions expert. ■

B v B
[2012] EWHC 314 (Fam)
FS v JS
[2006] EWHC 2793 (Fam)
GS v L
[2011] EWHC 1759 (Fam)
H v H
[1993] 2 FLR 335
Harris v Harris
[2001] 1 FCR 68
Hart v Hart
[2017] EWCA Civ 1306
Jones v Jones
[2011] EWCA Civ 41
M v M
[2015] EWFC B63
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[2011] EWHC 586 (Fam)
White v White
[2000] UKHL 54