



## Divorce, Pensions and Retirement Benefits

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### **GATHERING THE INFORMATION NEEDED TO VALUE AND DISTRIBUTE A DEFINED BENEFIT (PENSION) RETIREMENT ASSET**

#### **Introduction:**

Before the attorney and the client can make any decision as to how to approach the negotiations involving the marital retirement assets, you must gather all the information you can as to how the plan works and the marital value of these assets. Some States allow you to put the whole pension into play for distribution purposes but most States, in one way or another, limit the distributable portion to that part of the pension attributable to the period the parties were accruing marital assets. How that determination is made is dependent on statutory and case law in the State of jurisdiction. In some States because of, frankly, less than equitable precedents, attempting to reach a fair distribution of this asset can present real difficulties to the attorney. In some States it is impossible. Just as long as the client is aware of what you are up against, and that you are doing the best you can, working within the limitations of the statutory or case law constraints, you will be providing the best services that can be expected. But if you fail to obtain all the information necessary to reach an intelligent distribution decision or you do not have a thorough working knowledge of what is permitted in your State you can anticipate problems.

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#### **Tip of the Month:**

##### **Anticipate some major changes in pensions in the coming years.**

If you have been following the business journals and newspaper articles you have to be aware that on-going and future defined benefit obligations are forcing company and public plan providers to rethink how to finance their employees' retirements. With a rapidly aging population, the cost of continuing to provide generous, guaranteed annual pension income, at little, or no cost to the employee, is fast becoming too burdensome. The trend in the nineties of terminating pension plan accruals and switching to defined contribution plans (401k's, etc.) will continue. Companies who do not change could face bankruptcy.

When drafting settlement language addressing a defined benefit pension consider including a statement that increases the alternate payee's share of the pension if the accrual is frozen in the future and a new, non-marital defined contribution plan replaces the pension. This would be appropriate if your State uses Matured Full Benefit language for a QDRO and the non-participant client is counting on his or her share being paid with dollars having the same purchasing power as that of the participant. As the participant will continue to accrue benefits in the new plan and the intent was to have the non-participant's share determined using the actual pension income, at the time of retirement, you can use an estimate of what was expected, without the change, to craft language that will address this possibility. This is only fair.

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## **GATHERING THE INFORMATION NEEDED TO VALUE AND DISTRIBUTE A DEFINED BENEFIT (PENSION) RETIREMENT ASSET**

**All pension schemes are a form of deferred compensation that the employer obligates itself to provide to all employees as a condition of employment.**

Understanding this, it becomes obvious that they are joint assets earned during the marital period but not available as income to the couple until the future. It really equates to the parties having set aside a portion of their income for their retirement.

The benefit to be received is determined by a formula such as final salary x years of service x 1.6% = annual pension payable to the retiree for life (i.e. \$60,000 X 1.6% X 32.5 years = \$31,200 annual pension for the life of the participant). There are no individual accounts in the name of the employee. Private pensions are funded by the company paying sufficient funds into a general account that is invested at a rate of return targeted to fund its future outstanding pension liabilities. Many public pensions have the employee contributions invested specifically to fund part of their pensions but still a large part of the public pension obligations are simply unfunded liabilities being paid currently, and in the future, by taxpayers from the general funds of the government entity.

States have taken two different approaches as to how these plans are to be valued and distributed incident to marital dissolution:

1. Deferred vested pension appraisal and distribution - assumes the employee stops working on the marital property cut-off date and the benefit earned up until that date is the only part of the retirement asset valued for marital property distribution purposes. This is the case law in a minority of states. Application of that methodology can grossly underestimate the present value of the pension. It permits no consideration of supplemented, early retirement benefits and will always make settlement of the case more difficult if the attorneys and the parties are aware of the inequities created by use of deferred vested methodology. A QDRO would cut off the non-participant's interest on the marital cut-off date and limit the distribution to the marital portion actual accrued benefit on that date. No consideration for future inflation and the penalty for waiting 15 or 20 years to receive the benefit are taken into consideration. The benefit dollar amount will be frozen on the cut-off date.
2. Matured full benefit pension appraisal and distribution - assumes the employee will continue to work until his or her earliest unreduced retirement date without any imputed increases in salary between the marital cut-off date and the retirement date. Any early, supplemented, pension enhancements that will be available at the time of retirement will be included in the projected pension income. The present value of that benefit is then reduced by a coverture calculation to eliminate all spousal interest in the present value of the pension beyond the marital property accrual cut-off date. A QDRO would be based on the actual retirement income received by the participant.

Once you know how your State treats these assets you can begin to plan your negotiating strategy your next move is to determine the present value of the pension by hiring a pension expert. But before you can do that you will have to have the information the expert will need to prepare a valuation. This is your opportunity to gather a lot of financial information about the plan participant if you do not represent him or her.

To avoid the time and expense of filing a discovery motion, always ask your opposing counsel to have his or her client sign a release form. One should be sent to every current and former employer as well as any other possible benefit provider (military reserve, volunteer fire department - some do provide pensions, Union headquarters if the participant is an officer, etc.). A "Release Form" is attached at the end of this newsletter.

Once the values are known you can proceed to formulate your distribution negotiating strategy. Even if your State requires a deferred vested distribution, it is a good idea to have the pension valued using both methods. That way, if you represent the non-participant spouse you can show your opponent the real value of the pension to hopefully make the negotiating process a little easier and possibly justify a greater than 50/50 split.

Once the present value of the benefit has been determined, defined benefit plan pension assets are either distributed using immediate offset methodology (real estate, cash, autos, other assets, etc.) or deferred by use of Qualified Domestic Relations Orders (or Domestic Relations Orders if the retirement plan is a public plan or a private plan not covered by ERISA).

For younger individuals the easiest way to distribute pension values is by immediate offset. In those cases the pensions are normally not as valuable. There will usually be sufficient marital assets available to trade to allow the plan participant to retain his or her pension benefits. The non-participant spouse can be compensated with additional interest in the marital real estate or some other marital assets. This is even more appropriate if the right to receive the pension is still decades in the future.

If the parties to the divorce are relatively young and do not possess sufficient marital assets to make the offset then the amount owed to the non-participant spouse can be established and an amortized payout over a period of years can be structured to compensate the non-participant spouse for his or her share of the pension. If both parties have pensions or defined contribution accounts, then, after determining the value of each party's retirement benefits, the difference is distributed by the individual whose benefits have the greatest value using either an immediate offset distribution or a QDRO if the funds can be immediately paid out to the alternate payee from a defined contribution account. Again this is more appropriate for younger clients.

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### **[Model Property Settlement Language](#)**

Download our settlement language form and let the experts at LawDATA, Inc. [draft model property settlement language](#) (<http://www.lawdatainc.com/SetLanForm.pdf>) that deals specifically with the pension plan to which the order is addressed and the facts of your case.

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Mr. Commerford has been active in the valuation of pensions and the preparation of Domestic Relations Orders for his attorney clients since the founding of LawDATA, Inc. in 1984. He has presented Continuing Legal Education programs, dealing with the valuation and distribution of retirement assets incident to divorce cases, for State Bar Associations throughout the country and written many articles on the subject for legal publications.

For any questions or ideas for upcoming articles you can reach Paul Commerford at [paul@lawdatainc.com](mailto:paul@lawdatainc.com).

Web: [www.lawdatainc.com](http://www.lawdatainc.com)

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## RETIREMENT ASSET RELEASE FORM

I, \_\_\_\_\_, do hereby instruct a representative of  
(Plan Participant - printed)

\_\_\_\_\_  
(Name – address – phone # of benefits provider)

to cooperate fully with \_\_\_\_\_  
(Name of attorney - address - phone #)

\_\_\_\_\_ or his/her designee and answer any and all questions relating to my pension plan or any other retirement or deferred income plans in which I participate. I also request that you furnish this individual a current plan booklet and a current accrued benefits statement, and a statement as of \_\_\_\_\_,

(Marital Property Cut-off Date)

of all of my accrued retirement benefits including any defined contribution and defined benefit plans in which I am a participant. The defined benefit plan statements should detail the accrued vested benefit payable to me on my normal retirement date along with a statement of projected pension benefits, including supplemental benefits, if any, payable to me on the earliest date that I may receive them on an actuarially unreduced basis (based on my current income) assuming continued employment to that date. If my benefit is contingent upon my classification or job level or contribution level please so state and advise what that may be. Also, please provide a statement showing my service computation date (first day of employment), dates of all breaks in service (if any), my current salary and my annual salary for the past five years, the legal names of the plans in which I participate and their addresses and the name, address and telephone number of the person to be contacted if additional information is needed. I authorize that person to answer all questions incident to this request. The defined contribution plan statements should show my current plan balances as well as my account balances on

\_\_\_\_\_ and on \_\_\_\_\_.  
(Marital Property Cut-off Date) (Date of Marriage)

\_\_\_\_\_  
Signature of Plan Participant

\_\_\_\_\_  
Today's Date

\_\_\_\_\_  
Date of Birth

\_\_\_\_\_  
Social Security #

\_\_\_\_\_  
Witness # 1 - Signature

\_\_\_\_\_  
Witness # 2 - Signature

\_\_\_\_\_  
Witness # 1 - printed

\_\_\_\_\_  
Witness # 2 - printed