



Divorce, Pensions and Retirement Benefits

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DEALING WITH QDRO'S THAT WERE NEVER WRITTEN

Introduction:

It is a normal occurrence in our office to be contacted by an attorney saying he or she has a new client whose divorce was finalized years ago but now that the ex-spouse is retired, the portion of the pension awarded to the client at the time of the divorce is not being received. In most cases the client has contacted the plan provider who tells them they have no record of a domestic relations order on file. Many of these divorces go back to the 1980's or the early 1990's. The final decree incorporated language awarding them a substantial marital share but their attorney, through ignorance or oversight, failed to prepare the order and follow-up with the Judge and the plan provider. In many cases their original attorney has retired or died. At this point the reasons why the order was never filed are not as important as determining what you can do to salvage the situation for your client. These are the issues we will be discussing this month. In most cases remedial action is possible but often the client will suffer losses because the DRO was not filed in a timely manner and you should be able to tell them what possible difficulties they are facing.

Practice Tip of the Month:

Deal with the retirement assets as early as possible to avoid unnecessary litigation!

In many cases the present value of a pension will be one of, if not the most, valuable marital asset to be distributed. This is more often true if one of the parties is a government employee or if the marriage is lengthy and the participant has less than 10 years before they can retire with unreduced benefits. Knowing the present value of that asset will be a key factor in structuring a settlement agreement. Alerting your opposing counsel to the importance of dealing with it and working together to try to agree to a value is critical unless the parties have pre-determined that a domestic relations order will be used for distribution purposes. But even if that is the case you still have to deal with survivorship, particularly in the case of a government pension. The monthly income to the non-participant spouse will stop (or never start) if survivor benefits are not included in the distribution if it is a government plan and the participant predeceases the non-participant spouse. If the intent is to offset the value of the pension against other marital assets then you must know that value before any negotiations can commence. Leaving the valuation to late in the process, and suddenly having to deal with an asset that dwarfs other substantial, assets, will always complicate your settlement and often lead to litigation that could have been avoided.

DEALING WITH QDRO'S THAT WERE NEVER WRITTEN

The unfortunate truth is that Qualified Domestic Relations Orders became a retirement asset distribution tool on January 1, 1985 but few attorneys knew much about them until they started being mentioned as areas of concern for potential malpractice in various legal publications. Federal government and military plans permitted Domestic Relations Orders even earlier than 1985. Many of those pension orders negotiated in the 1980's did not begin to payout until the 90's, or later. It was not until 1989 that plans were permitted to make immediate distribution of defined contribution, lump sum accounts, such as 401(k)'s, ESOP's and Retirement Savings Plans.

On a personal note, I remember drafting orders in 1985 and having to work with a private company's outside ERISA attorney in trying to work out acceptable language that would address the requirements of the Retirement Equity Act of 1984, the enabling federal legislation, and the plan's own provisions. Back then it was really a case of the blind leading the blind. For a number of years orders were reviewed at a fairly high corporate level and were very costly for the companies to administer. That changed significantly in the nineties with the job of QDRO review being relegated to lower level employees working off of a checklist of acceptable paragraphs. Many plans offered attorneys "model orders", which, if followed to the letter, were guaranteed to be acceptable to the plan. Unfortunately, many of these "model orders" were, and still are, badly skewed to the benefit of the participant. Attorneys, with little or no knowledge of actuarial terms, made liberal use of them, not realizing that their clients were not going to receive what was negotiated in the settlement.

But those issues are something we will explore at another time. What we are dealing with today are situations where a settlement provided an alternate payee with a share of a pension or a defined contribution lump sum account and no domestic relation order was filed. This is not as rare as you might think. Many attorneys were under the impression that if the retirement asset award was included in the settlement, they were done. They figured when the participant spouse retired the non-participant spouse would begin getting what had been awarded. As we all know now, that is not the case.

Before a plan can pay out any funds to other than the participant, it must receive and approve a domestic relations order, signed by the judge and certified by the Clerk of the Court, that directs the plan, specifically, as to what they are supposed to do with the portion of the benefit awarded to the alternate payee. The order must comply with the changes made to the IRS code and ERISA by the Retirement Equity Act of 1984 (and revisions since) and the plan's own provisions and bylaws. If it doesn't, and the plan honors the order, the plan is in jeopardy of losing its tax-deferred status and being fined.

If a client comes to you today and tells you that their ex-wife or ex-husband is about to retire and they checked with the plan to find out how much a month they will be receiving from the pension, only to find out there wasn't any record of a QDRO, all is not lost. You should immediately advise the plan that you will be filing a domestic relations order because the former spouse has been awarded a portion of the retirement benefits. This will put the plan on notice and, in most cases, preclude the participant from actually retiring before you can get your order filed. Most plan providers do not want to get caught up in a lawsuit involving an employee's domestic problems. But they are under no legal restraint to refuse the employee's request to retire and commence receiving his or her benefits. They will usually hold things up for a short period of time. Therefore you must quickly file the order and get it to the Plan Administrator. In that case, you have saved the day.

Another scenario, and unfortunately more common, is the former spouse who comes to you and says that their ex-husband or wife retired six months, or six years, ago and when the client contacted the employer they found out that the plan had never received a domestic relations order. If the ex-spouse was unmarried at the time of retirement and did

not designate a survivor but, rather took his or her full, unreduced monthly pension or if your new client was not named the beneficiary for survivor benefits in the settlement, you will be able to solve his or her dilemma. You can file an order, with the monthly payment increased over a period of time, amortized to include a reasonable interest rate, to reflect the funds that were not paid. If your client was designated survivor the participant's pension can be recalculated with the actuarial reduction necessary to provide survivor benefits. The monthly amount payable to the participant has to be reduced (usually about 10%) to provide pension benefits payable in the form of a joint and survivor annuity. Not all plans will do this but there is no reason why they can't. You may have to be persistent. The alternate payee's share of the monthly pension is also reduced proportionately to reflect the cost of survivorship. You may need some help with the arithmetic to figure the monthly pension income that is due to be paid to the alternate payee and the amortized pay-back of the now reduced, monthly pension amount but that is not difficult. The important thing is that it was possible to make your client whole.

If the former participant spouse had remarried before his or her retirement, and the new spouse has been designated survivor, even though your client was to be named the survivor, there is little you can do to rectify that situation. You can get the monthly pension payments to your client into pay status, along with any repayment of income that was not made by using increased, amortized payments for a period of time, but if your client takes the full percentage of the pension due to them it will only be paid while the ex-spouse is alive. If they elect to have their share paid to them on an actuarially reduced basis so they will get income for life the reduction in the monthly amount due to them will be very substantially decreased. Depending on age and sex of your client, the reduction could be 50% or more. They may want to seek redress from their original attorney if he or she is still around, but there is nothing you can do.

If the Qualified Domestic Relations Order that was not filed was to address a lump sum Defined Contribution Plan (401(k), ESOP, etc.) your client can get his or her share, plus all earnings and/or losses from the marital property cut-off date up to the present, from the plan, if it is still intact, with a Qualified Domestic Relations Order or, from the ex-spouse if it had not been converted into an annuity when he or she retired. If it was converted into an annuity, a pension expert or an accountant can figure what portion of the monthly annuity income is due your client and a Qualified Domestic Relations Order can be filed with the annuity provider. If the former spouse has the funds in some kind of a personal account you will have to go to court to get an order to get the funds paid to your client if he or she refuses your request for payment.

The worst case scenarios are in those instances where the participant is deceased and no order has yet to be filed. You can't file an order, under any circumstances, if the participant dies prior to the plan's receipt of an order. A good reason to always do your own orders promptly.

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) (<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.

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.

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