



Divorce, Pensions and Retirement Benefits

Number: 29

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April 2005

RULES THE OF THE GAME #1

Introduction:

Each month, I present you with information that can be daunting in its complexity. I try hard to make it as simple and readable as I can without over-simplifying. Still there is a lot of data to retain. I am very aware of the fact that this info is competing for brain space with the cases you are now juggling, new case law and legislation in your district and the myriad minutiae of information to which we are all exposed. To try to help you keep some of the more important data in the forefront I try to occasionally do a little summary newsletter highlighting some of the topics we have covered in the past. I think that in the future I will make this a regular, though not scheduled on any particular time frame, feature of this column. To make it easier I will use numbered lists and try to make each point as succinct as possible. We'll call them "The Rules of the Game" and try to limit the information to the stuff you really should know cold if you handle a lot of divorce cases.

I have been accused of being an advocate for the non-participant spouse when discussing how to deal with marital retirement assets. I suppose to some degree it might appear that way but the reality is that it is the attorney for the non-participant spouse who has the greatest risk of malpractice in this area of the law. It is also true that in many cases each spouse is a non-participant and a participant so both attorneys are confronted with the same challenges. The participant's attorney has the client with all the facts about his or her benefits and the physical possession of these assets. It is incumbent upon the non-participant's attorney to gather information, value the assets and make sure the client gets his or her equitable share. My task is to try to point out the pitfalls that may be encountered throughout the process and help the attorney protect himself or herself and the client. The burden for getting this right falls more on the non-participant spouse's attorney, thus most of these newsletters are directed to that goal. I am not an advocate for the non-participant but rather a resource for attorneys who try to settle the retirement asset issues equitably. A divorce case is not to be won or lost. It is intended to be a process whereby the marital assets are correctly identified and valued and then, equitably distributed.

Tip of the Month:

Have the client chronologically list all employment for both parties (including part-time and volunteer) to be sure all sources of retirement assets are identified.

The divorce process can be a very emotional exercise for many clients. Using a good intake form is critical to getting them to focus on the facts that will be pertinent to the case. Include a section in your intake form for your client to chronologically list all of their employment and that of their spouse, as well as any information they might have about retirement assets earned with each employer. Approaching the gathering of this data chronologically usually results in a more comprehensive listing of the information you will need to address the retirement assets with which you will be dealing.

THE RULES OF THE GAME

1. Use defined contribution retirement benefit (lump sum 401(k) plans, ESOP's, Retirement Savings Plans, etc.) Qualified Domestic Relations Orders as an immediate source of funds for the non-participant spouse. Most defined contribution plan providers have amended their by-laws to allow immediate payout of these funds upon receipt of a QDRO. A trustee-to-trustee transfer is tax-free (tax deferred) but any subsequent withdrawals are subject to income taxes and the 10% early withdrawal penalty. A direct payment is taxable (at the tax rate of the recipient) but the 10% penalty for early distribution normally imposed by IRS is waived, if payment is incident to a QDRO.

2. Organize the process. Have comprehensive intake forms for use by the client to get as much employment and benefit plan information as possible. Make the client get the addresses and telephone numbers of the retirement benefit providers. Get your opposing counsel to have his or her plan participant client sign release forms so you can get the income and retirement benefit information directly from the employer. Include in your standard release form the right for you to discuss the retirement plan mechanics with a company representative. Get plan booklets and accrued benefit statements from every plan provider.

3. Be prepared for negotiations. If you represent the non-participant spouse always draft the section of the settlement agreement dealing with the retirement assets prior to negotiations, or employ a pension consultant to prepare one for you, to insure that all of the plans and the plan provisions are addressed in the negotiations. If you have any trepidation about your knowledge in this area – always use a pension consultant. This is when most of the errors that will cause a client to seek redress are made. Insist on survivor benefits for the non-participant spouse. If it is a public plan all benefits stop upon the death of the participant unless the non-participant spouse is named the beneficiary of the survivor benefit. If it is a private plan the alternate payee's benefit will be actuarially computed if there are no survivor benefits awarded. Depending on the age and sex of the alternate payee this could reduce the amount anticipated by as much as 50% (even more in some situations) and create a very unhappy client.

4. Beware of military retirements. In order to submit an acceptable military domestic relations order (Uniformed Services Former Spouses Protection Act order) the parties must have been married for at least 10 years while the participant was on active duty. In other words, the marriage must overlap the military service period for at least 10 years. The 10 years are based on the date of divorce and not the marital property accrual cut-off date in your state. If that criteria cannot be met you cannot use a domestic relations order for settlement.

5. Be creative and knowledgeable about the impact of bad case law. Consider using an amortized payout if your state case law unjustly penalizes the non-participant spouse. In some states QDRO's are limited to include only the accrued amount of the monthly pension income on the marital property cut-off date. Because of the nature of pensions, this means that the monthly amount awarded to the alternate payee will never change even if 20 years must pass before it can go into pay status. Obviously, the purchasing power of the dollar over a 20 year period will probably be severely eroded (with an inflation rate of just 2.5% annually approximately 63% of the purchasing power of a dollar will be lost). When the marital estate does not have sufficient assets to make an immediate offset settlement, based on the present value of the pension, by giving the non-participant spouse a larger interest in another marital asset (real estate, stocks and bonds, auto's, etc) consider having the non-participant's share of the present value paid by the participant using an amortized payout schedule over a five or ten year period. A reasonable rate of interest should be included. Naturally, the payments have to be made affordable to the participant after other obligations (child support, marital debt, etc.). This can be an attractive alternative to the

non-participant spouse in that it could provide another source of income at a time when income might be badly needed. Another benefit is that only the interest would be taxable.

6. Settlement agreements require specificity. When drafting settlement agreements always be very specific about the intent of the parties. If survivor benefits are awarded in a QDRO, identify which of the many survivor options usually available (i.e. 50%, 75% or 100% Joint and Survivor Annuity, a survivor annuity limited only to that portion attributable to the marital period, pop-up options in the event of the death of the alternate payee, etc.) is to be awarded. Always include pre-retirement death benefits in your settlement agreement. Some plans levy a small reduction in the final pension benefit if pre-retirement survivor benefits are provided, so theoretically they are assets to be obtained through negotiation. Spell out exactly how the portion awarded to the alternate payee is to be determined and address any supplemented contingent benefits the participant may be entitled to receive if certain employment criteria are met. If all the retirement options and issues are not addressed in the settlement agreement, they cannot suddenly appear in the QDRO.

[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.

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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