Pension Issues & Divorce

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INTRODUCTION

When couples get divorced they must decide how to divide their property. Retirement benefits (pensions) often form a substantial part of the parties' total marital estate and many times are the largest single marital asset afforded the couple. Similar to other assets, pensions are typically divisible in cases of divorce to the extent that they are acquired during the period of marriage. In order to divide a pension, the value of the retirement benefits accumulated during the period of marriage must be determined. The division of these benefits follows a 3-step process.

1. Classification

Each pension is classified as to whether or not it is considered property, and from there, separate or marital property. There is a broad general consensus that retirement plans of all types do constitute property.

2. Valuation

Each pension that is considered marital property is appraised to determine its value.

3. Distribution

Each pension that is considered marital property is analyzed to determine the most equitable way it should be divided and distributed to the party

CHAPTER 1

OVERVIEW OF PENSION ISSUES IN DIVORCE

We are presenting this "Overview of Pensions" in a conversational format that takes place at a series of meetings between a young aspiring attorney whose parents are getting divorced and a well respected senior lawyer who specializes in Divorce Law.

Meeting #1

Junior Associate:

Thank you for taking this time to explain to me the basics of pensions. It will certainly help me explain to my parents how their divorce will impact their pensions.

Senior Law Partner:

Let's get started.

The first thing we should discuss is the definition of a pension plan. A pension plan is a tax deferred savings plan. In other words, the companies your parents work for are putting money into a pension plan instead of paying your parents additional

income each week. The money that they are putting into the plan accumulates tax free, and when they retire, they may withdraw the money in either a lump sum or periodically over the remainder of their lifetimes. Your parents will pay taxes on the money if, as and when it is received. The plan, by its nature, forces your parents to save money now and pay taxes on it later in life during their "golden years" when they are in a more advantageous tax bracket. Therefore, it is a tax deferred savings plan.

Senior Law Partner: Question?

What kind of pension plans do your parents have?

Junior Associate: Answer

My mother has a 401(k) Plan and my father has a regular pension that will be paid to him when he turns 65.

Junior Associate: Question?

What is the difference between the two plans?

Senior Law Partner: Answer

Your father's "regular pension" is what is called a defined benefit plan. A defined benefit plan promises that upon retirement your father will receive a defined or known monthly income for the duration of his lifetime. The monthly benefit that

your father will receive will be based upon a specific formula, which can be found in the plan documents, and usually includes his years of service with the company and his salary at the time of his retirement.

On the other hand, your mother's 401(k) Plan is what is called a defined contribution plan. A defined contribution plan is the type of plan in which the contributions to her plan account are known or defined. For example, 10% of her weekly salary is deposited into an account established within the plan specifically for her. The amount of money to be distributed to her upon retirement is unknown at the present time and will depend upon how effectively the contributions to her account are invested. When she retires she will receive the value of her account in a single lump sum payment.

As you can see defined benefit plans and defined contribution plans are very different.
The differences in the nature of these two plans cause differences in the manner in which they are valued and distributed in the case of a divorce.

Junior Associate: Question?

Maybe I jumped ahead a little. I have a very basic question. My parents both wonder why the benefits that they have worked for all of their lives are going to be split between them when they divorce?

Senior Law Partner: Answer

The answer to that question lies within the definition of what is considered to be property. Property has two basic attributes. The first being that it is certain and the second that it is transferable. Certainty, means that rights in property exist unconditionally in the present rather than rights that may possibly exist in the future. Transferability, means it can be given to another person on a permanent or temporary basis in return for consideration.

There have been a lot of arguments that contend that a pension is not property and therefore not divisible. However, all of the state courts within the United States take the position that a pension is property (certain and transferable), and, therefore, divisible upon divorce.

I'm sure your parents are wondering whether or not they will be forced to split all or just part of their pensions. The state courts are divided on this particular issue.

There are two basic property models. The particular model which is followed for a specific divorce depends upon the attitudes of the state court which has jurisdiction over that divorce.

Some states have adopted what is called the "all property model." Under this model, the court can divide any interest which constitutes property and is owned by one or both parties on the date the state considers the marriage to have ended (i.e. Divorce Date, Separation Date, Complaint Date, etc.) In other words, it doesn't matter when the property was acquired; whether it was before the marriage or during the marriage.

Under this model, all property owned by your parents on the date their marriage ended will constitute marital property, and can be divided when your parents divorce.

The other model is called the "dual classification model." This model is similar to the "all property model" in that in order to be divided in a divorce, the property must be owned by one or both parties on the date the marriage ended. However, the difference is that the property must have been acquired during the period of marriage. Therefore, under this model, only that portion of your parents pension benefits which were earned during the time they were married would be considered marital property subject to division in the divorce. Any portion of the pensions earned before your parents got married would be considered their separate property.

Your parents live in a dual classification state. Therefore, any portion of their pensions earned prior to their marriage would be considered their separate property, and any portion of their pensions earned while they were married would be considered marital property.

Junior Associate: Question?

Both my parents participated in their pension plans before they were married.

Therefore, the portion of each of their pensions that was earned prior to their marriage would be considered their own separate property (Not Divisible) and the

other part, that was earned during the marriage, would be considered marital property (Divisible). Is that correct?

Senior Law Partner: Answer

Yes, that is right. But it is still more complicated.

Under your mother's defined contribution plan, any growth on her separate property, that portion of her pension that was earned prior to the marriage, could be considered her separate property or it could be considered marital property. Each dual classification state model looks at this issue differently. Some states hold that any growth on the separate property which occurred during the marriage would be considered marital property. Others states say that any growth on the separate property which occurred during the marriage would be considered separate property. This is also true for your father's defined benefit plan. The only difference being that your father's plan does not grow in value unless he continues working, while your mothers' continues to grow even if she stops working.

Junior Associate: Question?

How do we determine which part of these pensions is marital property and which part is separate property?

Senior Law Partner: Answer

For your father's defined benefit plan, this is usually accomplished by applying what is called a coverture fraction to the monthly benefit your father has acquired for his years of employment up to the date their marriage ended. The coverture fraction is a tool that is used by pension appraisers to determine the portion of a pension which should be considered marital property as compared to that portion which should be considered separate property. The numerator of this fraction represents the period of time that your father participated in his plan during the marriage (from the Date of Marriage to the Date the Marriage Ended) while the denominator represents the total period of time that he participated in the plan (from the Date of Plan Participation to the Date the Marriage Ended).

As an example. Let's say that your father worked for 5 years prior to getting married and for 10 years while they were married, for a total of 15 years up until the date their marriage ended. The coverture fraction would be **66**% (rounded). He would have 10 working years while married divided by the total 15 working years, resulting in a coverture fraction of **66**%. This is called coverturing by time.

Junior Associate: Question?

Could this type of time coverture be used for my mother's defined contribution plan?

Senior Law Partner: Answer

It could be, but it is the least preferred method. Another way to determine the marital portion of your mother's pension would be to coverture by contributions. The total contributions made to her account during their marriage is divided by the

total contributions made to her account as of the Date their Marriage Ended. This fraction would then be multiplied by the account value as of the Date their Marriage Ended.

Junior Associate: Question?

So if my mother made small contributions to her plan in the early years and larger contributions during the marital years, this type of coverture could vary drastically from a coverture by time.

Senior Law Partner: Answer

Yes, it could.

Junior Associate: Question?

It seems to me that since they live in a "dual classification" state that says the growth on separate property remains separate property upon divorce, we must somehow track the growth or interest that has accumulated on the portion of her pension that was earned prior to their marriage?

Senior Law Partner: Answer

You are correct in your thinking. Unfortunately, this can get very complicated. That is one of the reasons why we hire an expert pension appraiser.

Junior Associate: Question?

How do you actually distribute the marital portion of a pension?

Senior Law Partner: Answer

There are two competing methods of division, each with its own rules. One is called the "Immediate Offset Method" and the other is known as the "Deferred Distribution Method".

The major difference between these two methods is the time at which division is accomplished.

Under the immediate offset method, a pension appraiser determines the present value of the retirement benefits. The non-employee spouse is awarded his or her share of the benefits as an immediate lump-sum award of cash or other property (i.e. additional equity in the marital home, a time-share purchased during the marriage, etc.) .

Under the deferred distribution method, by contrast, there is no immediate division of the retirement benefits. Instead, the non-employee spouse is awarded a percentage share or specific dollar sum from the employee's pension when the employee is entitled to receive his or her benefit directly from the Plan. Since the employee spouse in most cases will not begin receiving benefits until some point in the future, the actual division of the pension under this method is deferred until the

employee spouse retires. This form of distribution is accomplished by using a court order or a Qualified Domestic Relations Order (QDRO).

The court order or QDRO is a written set of instructions that explains to the pension plan administrator that a portion of the pension has been determined to be marital property subject to distribution in the divorce. The QDRO will provide specific instructions as to the manner in which this pension is to be divided.

For example, let's assume that on the date your parents marriage ended, your father was entitled to receive $1,000 a month at retirement. The coverture fraction, of this benefit is determined by time, to be 33%. This means that 33% of the $1,000 was earned during the marriage, therefore, the marital portion of your father's $1,000 a month pension benefit is $330. This is the amount your mother and father will split. Let's further assume that it has been decided that your parents will divide their marital property on a 50/50 basis, due to the longevity of their marriage. Your mother would be entitled to $165 of the marital portion of your father's benefit, and your father would receive $165 of the marital portion plus $670 which was his non-marital portion. Therefore, the QDRO would be drafted by either our law firm or a pension expert to provide instructions for the plan administrator to pay directly to your mother $165 per month beginning when your father actually retires or is eligible to retire.

Junior Associate: Question?

Is marital property always divided equally?

Senior Law Partner: Answer

That depends upon the laws of each state. The state in which your parents are divorcing does not require an equal division.

Junior Associate: Question?

Would the deferred distribution method work the same way for my mother's pension as it did for my father's?

Senior Law Partner: Answer

Yes. A Qualified Domestic Relations Order would be drafted to provide the plan administrator with a set of instructions to follow in dividing the pension. However, since there is a lump sum amount in a defined contribution plan at any point in time, the QDRO would typically instruct the plan administrator to set up a separate account for your father's portion of your mother's pension. The plan administrator would then transfer your father's share into his account.

Junior Associate: Question?

So under the deferred distribution method, all payments would be made in the future when my parents actually retire?

Senior Law Partner: Answer

In general terms - yes. Under some defined contribution plans, distribution can be made as soon as the QDRO is drafted. However, there can be significant tax implications with this type of cash distribution. This should be examined further when the time comes.

Junior Associate: Question?

How would an Immediate Offset Method work?

Senior Law Partner: Answer

In order to explain this, let's first look at your mother's defined contribution plan. Let's assume that the marital portion of her plan is worth $10,000 and that your parents also have a car that's worth $10,000. What in essence happens is that one asset offsets the other. In other words, your mother would keep the marital portion of her pension worth $10,000 and your father would get the car that is worth $10,000. This, of course, assumes that your parents would be splitting their assets equally.

Junior Associate: Question?

How would an immediate offset be accomplished for my father's defined benefit pension plan? It's hard for me to understand how a monthly benefit that he is going to receive in the future could be converted to some sort of immediate offset?

Senior Law Partner: Answer

Well, valuing a defined benefit plan is a lot more complicated than dealing with a defined contribution plan. Under the defined benefit plan we first must determine what your father is going to receive in the form of a monthly benefit when he retires. That monthly benefit is then converted to a lump sum present value using an interest rate and tables to measure his expected lifespan. The present value of the benefit represents what it is worth today for your father to know that he will be able to collect a monthly benefit for his lifetime starting on his retirement date.

Junior Associate: Question?

You know what. I don't understand exactly what you are telling to me.

Senior Law Partner: Answer

Well, let me explain it another way. Let's assume you are at a meeting with your local banker and you tell him you would like to be able to withdraw $100 a year from from your account. He says, OK, I can pay you 10% interest on the money you deposit in my bank. Therefore, if you put approximately $90 in my bank today and leave it there for one year, you will earn roughly $10 in interest over the course of the year. Therefore, one year from now you will have $100. The $90 is the present value of receiving $100 a year from now at 10% interest.

We are saying the same thing with regards to your father's pension. How much money must we put away today, at interest, so that it will grow in value to pay him

$1,000 a month for as long as he lives. The amount that would have to be set aside today is the present value of his pension.

Junior Associate: Question?

So, in order to determine the present value of my father's pension, you would have to determine how long my father is going to live?

Senior Law Partner: Answer

Yes, a pension appraiser would use either mortality tables or life expectancy tables to determine how long a male your father's age would live. Therefore, based on his estimated lifespan, the length of time your father would actually receive his pension could be determined.

Junior Associate: Question?

Would the process then be as follows? A pension appraiser determines the present value of the defined benefit plan. This present value is then compared to the value of my parents' cars and house. If the value of the pension can be offset against the car or the house, the Immediate Offset Method can be used. However, if the value of the pension is greater than the value of their car and house the Deferred Distribution Method is utilized.

Senior Law Partner: Answer

Yes, that's exactly right.

Junior Associate: Question?

Does one method have advantages over the other method?

Senior Law Partner: Answer

There are pros and cons for both methods. However, courts generally feel that if an offset can be accomplished, it is preferred.

Senior Law Partner:

Why don't you discuss with your parents our conversation. Then we can have another meeting.

Meeting # 2

Junior Associate: Question

Since the last time we met, I have had an opportunity to sit down with my parents and discuss this whole pension issue in great detail. As a result they have more questions and concerns.

My parents have decided, that in order to make an intelligent decision about dividing their pensions, they should have them valued by a pension appraiser to

determine exactly what they are worth. We have decided to utilize the services of Pension Appraisers, Inc. They sent to us copies of their Pension Valuation Request Form. The form itself is pretty self-explanatory, except there are some key issues that my parents aren't sure about.

The first issue concerns which method of valuation should be used for the analysis.

Let's address my mother's defined contribution plan first. Pension Appraisers states that there are three basic ways of valuing a defined contribution plan. The first is the Segregation Method, whereby they would track the growth in the non-marital portion of the pension (the portion my mother earned prior to their marriage) and subtract it from the total value as of the date my parents marriage ended, to obtain the value of the marital portion. The second is the Coverture Method, which multiplies the account balance on the date their marriage ended by a coverture fraction to determine the marital portion. The third is the Subtraction Method, which subtracts the account value on the date of marriage from the account value on the date the marriage end to arrive at the marital value. Which one should they use?

Senior Law Partner: Answer

If they have all the required information, it should be valued by the Segregation Method. This method is the most accurate. However, in order to do this type of valuation, your mother will have to supply Pension Appraisers with quarterly statements (or at the minimum annual statements) of the value of her plan from the time that they were married until the time that their marriage ended. If your

mother can't supply this information, then I would suggest that they use the Coverture Method.

Junior Associate:

My mother saves everything. She kept all her quarterly statements from the time she started participating in the plan. I'll recommend they use the Segregation Method to value her plan.

My father's defined benefit plan appears to be a lot more complicated to value than my mother's defined contribution plan.

Pension Appraisers offers two methods for valuing defined benefit plans. One is called the PBGC Method, which stands for Pension Benefit Guaranty Corporation. Another method is called the GATT Method, which stands for the General Agreement on Tariffs and Trades. We are confused at this point as to which method we should choose.

Senior Law Partner: Answer

Both methods employed by Pension Appraisers are acceptable methods. However, they do yield different values because the facts utilized to do the valuation are different. Let me see if I can explain in a little bit more detail.

The PBGC method utilizes interest rates that are published monthly by the Pension Benefit Guaranty Corporation. The interest rate used in the GATT Method is the

30-year Treasury Bill Rate. When you use different interest rates you will get different values. There is an inverse relationship between interest rates and present value. As interest rates go up, present value goes down. So, if there is a major difference in the interest rate assumption, there will be a substantially difference in values. Because one method may yield a higher or lower value than the other, doesn't mean that one of the methods is appropriate or inappropriate. It just means that different methods produce different values.

Remember when we had your parent's house appraised, the real estate appraiser came up with three different values based upon three different approaches to value (Cost Approach, Income Approach and Sales Comparison Approach). Each approach yielded a different value. It doesn't mean that one approach is inappropriate. It just means that the appraiser has established a range in value for their house. The same is true for valuing pensions. If you use different methods you, are going to come up with different answers. This will then provide a range in value. As an example, let's say we have your father's pension appraised by both methods. One method yielded a value of $100,000 , and the second $110,000. The range in value would be between $100,000 and $110,000. This range represents a variance of 10%, which is minimal. Therefore, I would say it doesn't matter which method or methods you use.

Junior Associate: Question?

Other than interest rates, what other factors can impact value?

Senior Law Partner: Answer

Any change in any assumption could have an impact on the value. For example, changing any one of the following will have an effect on the value: the normal retirement age, the date employment started, the marriage date or the cutoff date for ending the marriage.

Junior Associate: Question?

How do all these different dates impact the value?

Senior Law Partner: Answer

These dates are used to determine the coverture fraction, your father's age, and how long he is expected to live past his normal retirement age. All of these facts go into determining the value of his pension. Here is a list of "What Ifs " relative to what happens to present value when assumptions change. Why don't you take this information along with you and discuss it with your parents. I'm sure it will help them understand how certain factual differences can impact the present value of your fathers pension. Then, you should have their pensions valued.

Junior Associate:

That's a good idea.

Let's assume, my mother's pension is worth $50,000 and my father's pension has a present value of $100,000. Furthermore, assume that, in addition to the pensions,

my parents have other assets that are worth $50,000. If they agree to split their assets equally, is it fair to say that, my mother would keep her pension worth $50,000 plus she would get the other asset worth $50,000 and my father would keep his pension which is worth $100,000?

Senior Law Partner: Answer

Yes, that's exactly the way an immediate offset would work.

Junior Associate: Question

Would that really be a fair way of doing it?

Senior Law Partner: Answer

Normally the courts would consider it fair unless there would be some extenuating circumstances. As an example, suppose your father is in poor health and the probability of his living very long is questionable. It would not be fair to give your mother the asset worth $50,000; when in essence your father probably won't end up collecting on his pension because of his poor health.

Junior Associate: Question

So, just because an immediate offset can be achieved, it's not always the fair way of distributing the pensions. In some cases, even though immediate offset is possible, the deferred distribution method should be utilized instead. Is that correct?

Senior Law Partner: Answer

Yes. Every divorce case is different. The facts of each case should be examined in depth to determine what is fair for those people.

Junior Associate: Question

Do you mean that in one case a 50%-50% split is fair; and in another case a fair split could be 70%-30%.

Senior Law Partner: Answer

That's correct. A 70%-30% split could be considered fair and equitable. However, keep in mind, some states have specific statutes instructing the courts as to how marital assets should be divided.

Junior Associate:

Thank you very much for your time.

Senior Law Partner:

I'm glad to be of help. After you have had your parent's pensions valued, we should get together and discuss an appropriate way to divide them.

Junior Associate:

Okay.

Meeting # 3

Junior Associate:

We took your advice and we have had the pensions valued exactly as we previously discussed. We did my father's defined benefit pension using two methods; the PBGC Method, the GATT Method. We had my mother's defined contribution plan valued by the Segregation Method.

The value of my father's pension by the two methods was very interesting. Among the two methods, the values varied by approximately 10%. Basically indicating that my father's pension is worth around $100,000, after applying a coverture fraction to the total value which was $150,000. My mother's pension, using the Segregation Method, had a marital value of $50,000.

My parents have discussed the distribution issue in great detail and have decided that they want to split their marital assets equally, but they do not want to do an immediate offset. Their preference would be to defer distribution until they both retire and start receiving payments. What would be the best way to accomplish this for my parents?

Senior Law Partner: Answer

Well, there are a few different ways that you can accomplish the desired result.

Scenario #1

Your mother keeps her pension in total and by way of a QDRO she gets 25% of your father's pension.

Father's Pension:	$100,000
Less:	
Mother's Pension:	$ 50,000
Balance of Father's Pension to be Split:	$ 50,000
50/50 split:	X 50%
Present Value of Benefits Awarded to your Mother:	$ 25,000

$\frac{\$\ 25{,}000}{\$100{,}000} = 25\%$

Scenario #2

You can do a QDRO for both pensions.

Your father would get $25,000 of your mother's pension rolled over into a separate account for him. Likewise, your mother would get 50% of you father's pension when he retires or is eligible to retire. As an example, assume your father is entitled to

$1,000 per month when he retires (this is the benefit earned during the marriage), he would get $500 a month and your mother would get a check for $500 a month.

Junior Associate:

Well, which way is the best?

Senior Law Partner: Answer

Neither one is the best. The best way to divide these benefit is the way that works best for your parents. Again, we are back to the unique situation of each individual couple. If you father is close to retirement, it might be better for both of them that he gets $500 a month and she gets an income of $500 a month.

There are other issues that are addressed in a QDRO other than how you split the value. As an example, what would happen if your father dies prior to retirement? There are a number of issues like this that must be addressed if they are going to do a QDRO.

Here is a list of the different issues that may come up when drafting a QDRO.

If your parents decide that drafting a QDRO is an acceptable way of dividing one or both of their pensions, a number of different issues should be settled before getting started.

CHAPTER 2
THE BASICS OF PENSION/RETIREMENT PLANS

Future Benefit Plans:

A pension plan is a tax deferred savings plan which falls under the category of a future benefit plan. A future benefit plan is a general term which describes any benefit plan instituted by a company to help ensure the future well being of its employees. A future benefit plan provides an employee with income at some point in the future. This is different from a salary which is received at the present time. A future benefit plan typically has two parts: a retirement portion, which provides benefits to employees after they retire; and a disability portion, which provides benefits in case of a work-related disability.

Any plan which provides benefits in the future in exchange for services rendered at the present time is typically considered a future benefit plan.

Classification of Future Benefit Plans:

Based upon the principles of property division, as well as those of retirement benefits, a future benefit plan is typically categorized according to the status of the employees' benefits. A plan that is currently providing benefits to an employee is considered to be matured. Those plans which have not begun distributing benefits are considered unmatured.

If the employee's right to receive benefits under the plan is permanent, even if such employee were to leave employment immediately, the plan is said to be vested. If the employee's right to benefits would be forfeited if he or she left employment immediately, such plan is said to be unvested. Typically, under most retirement plans, an employee's benefits will become vested after completing a required number of years of service. Such requirement usually falls somewhere between 3 and 20 years. All matured benefits are vested, due to the fact that the employee is receiving benefits even though he or she terminated their employment.

Conventional retirement plans can also be categorized according to the way in which the employee's benefits are defined. If the plan defines an employee's benefit as a periodic dollar amount, for example a $1000 per month, the plan is considered a defined benefit plan.

If either or both the employee and the employer make contributions to a retirement plan account, and the employee's benefits are expressed in terms of the present balance in his or her account, the plan is a defined contribution plan.

A defined contribution plan typically expresses the employee's interest in terms of his/her account balance. However, the employee does not have to receive his/her interest from the plan in the form of a lump sum payment. Most defined contribution plans use the balance in the plan account on the date of retirement to purchase an annuity. This annuity will pay periodic benefits, usually on a monthly basis, to the employee for the remainder of his or her lifetime.

The primary difference between defined benefit and defined contribution plans lies in the manner in which the plan benefits are determined, and not the form in which the benefits are to be received.

Retirement plans can also be categorized relative to the manner in which the benefit is funded. If the benefit is funded entirely by the employer, the plan is considered noncontributory. However, most plans provide the employee with the option of contributing his or her own funds (often through salary deductions), to acquire additional benefits within the plan. Some plans require the employee to contribute towards his or her benefits. In cases where the benefits are derived from contributions made from both the employee and employer, the plan is said to be contributory.

CHAPTER 3

WHY PENSIONS ARE DIVIDED UPON DIVORCE

In order for the court to divide a future benefit plan upon divorce, it must first determine the extent to which it is considered property. Any benefit which does not meet the criteria to be considered property cannot be divided in cases of divorce.

What is Property?

In order for something to constitute property, it must be considered certain and meet the characteristics of transferability.

The first attribute of property is that it is certain. A right to property exists unconditionally. Retirement benefits can be considered contractual rights. If an employee achieves a predetermined status or meets specific requirements, he or she has an undeniable right to receive benefits. This undeniable right can be termed a contractual right, and is not considered to be a mere expectancy. This undeniable right to benefits creates certainty.

The second characteristic of property is transferability. Property can be given away on a temporary or permanent basis in return for consideration. Since property can be given to another person, it is considered transferable. Many state statutes contain anti-assignment provisions which do not permit an employee to transfer their benefits to another person. However, this inability to transfer benefits is not

an inherent quality of retirement benefits, and therefore, should not preclude such benefits from being considered transferable.

Pensions as Property

The case against treating retirement benefits as property centers around the characteristics of property: certainty and transferability. As stated earlier an individual's rights to property are unconditional at the present time. Rights to property are not something that may exist or evolve at some point in the future. For example, a future inheritance does not provide any ownership rights at the present time, but purports an expectancy for ownership in the future. Since ownership rights do not exist at the present time, such would not be considered property. In addition, property is considered to be transferable, meaning it can be given to another in return for consideration. A professional degree or designation is not considered property due to the fact that it cannot be given to another in exchange for money or other property. Those who wish to dispute the notion that retirement benefits are considered property argue that similar to a potential inheritance or professional degree, retirement benefits are received in the future and cannot, under federal law, be transferred to another person.

The case in favor of treating retirement benefits as property centers on the nature of retirement benefits, and the way these benefits are perceived by both the employers and employees in the workplace. Retirement benefits are considered contractual rights. This consideration is due to the fact that if the employee meets certain requirements he or she has an absolute right to benefits under the plan. The employee's right to these benefits can be considered part of the employment

contract, thereby making it a contractual right not a mere expectancy. If the employee meets the requirements set forth by the plan, such employee will have an undeniable legal right to receive benefits in the future. Therefore, if the employee has already met all requirements necessary, the undeniable right to benefits is fully established at the present time. These qualities distinguish retirement benefits from a future possible inheritance, which only provides an expectancy of benefits rather than an absolute guaranty.

Retirement benefits more similarly resemble the many forms of deferred compensation offered to employees during the course of their working lives. For example, an employee may be offered a bonus for good performance on the job for the past five years. These five years coincide with the period of marriage, but the bonus itself is not awarded until after the marriage has ended. The bonus would be considered marital property due to the fact that it is a direct result of the active efforts of the employee during the period of marriage. The very nature of the structure of retirement benefits provides the employee with a benefit at a point in the future due to efforts on the job in the past. Therefore, retirement benefits which are earned for years of employment which coincide with the period of marriage would be considered marital property. The theory is, had the employee not participated in the retirement program during those years of employment which coincide with the marriage, he or she would have brought a larger salary home to the family. Since a retirement benefit is a direct result of efforts put forth by the employee during the period of marriage, it is considered payment for those efforts. The fact that payment occurs at a point in the future does not change the reason for compensation. Since retirement benefits more closely resemble deferred

compensation than professional degrees or a future inheritance, there is a very strong and valid argument that such benefits constitute property.

Further, retirement benefits are clearly treated as property by both employees and employers in the workplace. Most retirement plans allow employees to take a reduction in salary in exchange for increased retirement benefits in the future. The majority of the time such an option is exercised by the employees, if available. In addition, employers often use enhanced retirement packages instead of additional salary as a lure to attract new employees or as a means to keep productive employees on staff. These examples of how retirement benefits can be substituted for current salary illustrates the argument in favor of treating them as property. If these benefits were contingent in nature, employers and employees alike would never substitute them for increases in salary.

Not considering retirement benefits as property subject to distribution in divorce would cause serious problems in the divorce arena. As mentioned above, employees often choose to exchange current salary for future retirement benefits. Obviously, salary earned during the period of marriage is considered marital property. If the employee had the ability to take marital property, that being current salary, and exchange it for retirement benefits, assuming they were considered non-marital property, it would provide the employee with a method of dissipating the marital estate. This would result in a major disadvantage for the non-employee spouse. As long as employers provide retirement benefits in lieu of salary, the courts will have to view both sides of this exchange as property.

Many of those who argue that retirement benefits should not be considered marital property use the "alimony argument." They believe that the inequities mentioned above are compensated for by the court when retirement benefits are considered for purposes of calculating and awarding alimony. To a certain extent, this argument is valid. However, alimony, by its very nature, is a contingent concept. Alimony ceases upon death or remarriage, and is usually subject to modification in order to accommodate a change in circumstance for either party. Therefore, there are a number of reasons a spouse's claim to alimony can be reduced after the divorce has been finalized. However, property division is almost always absolute and final upon completion of the divorce. Each spouse receives the property awarded to them regardless of a change in circumstance of either party. Therefore, if the court uses alimony as a vehicle for providing a property distribution, an absolute right to property is being attached to a contingent concept. A spouse would have to never remarry or rely on the continued life of the employee in order to be sure that he or she receives the full amount of the property awarded. Further, a change in circumstance of the employee could affect the property awarded to the spouse. A change in circumstance after the divorce would not normally affect division of other types of property, such as the marital home, vehicles, etc., and therefore, should not affect distribution of retirement benefits. In addition, some believe that using alimony as a method for division of retirement benefits could stir an element of reverse discrimination. Men are substantially less likely to receive alimony than women. Therefore, this could lead to problems ensuring that men receive a proper and fair division of property.

The argument in favor of treating retirement plans as property is very strong. When examining the pieces of these arguments, the characteristics of certainty and

transferability seem less important. Since employees often trade salary for retirement benefits, it would be hard to make the argument that retirement benefits are not sufficiently certain enough to be considered property. If retirement benefits were not certain, employees would never trade salary in exchange for them. The issue of transferability presents more of a problem. However, lack of transferability is not an inherent quality of retirement plans. Federal law prohibits people from transferring their retirement benefits in an attempt to eliminate the chance that they will jeopardize their future financial well being. This inability to transfer retirement benefits has nothing to do with the nature of the benefits, but hopes to eliminate people from ending up on public assistance due to poor decisions regarding their retirement. Therefore, since this federal law does not relate to the nature of the benefits, it should not create an obstacle for treating retirement benefits as property.

CHAPTER 4
PROPERTY DIVISION LAW

After the court decides that retirement benefits meet the criteria to be considered property, the language of the state statutes must be examined to determine if such property is subject to division. State property division statutes can vary, but there are two general models.

All Property Model

According to the all property model, the court may divide any interest which

- meets the criteria to be considered property and
- is owned by one or both of the parties on the date of classification.

Dual Property Model

The dual property model provides that the court may divide only that property which is considered marital or community property. An asset can be considered marital or community property if it

- meets the criteria to be considered property,
- is owned by one or both parties on the date of classification,
- was acquired during the period of marriage,
- and does not specifically qualify as the separate property of either party.

Comparison of the Two Models

The first two requirements of these models are the same while the last two are unique to the dual classification model. Following is a discussion of the requirements.

* meets the criteria to be considered property;

This is very important. Anything that cannot be considered property is not divisible upon divorce.

* is owned by one or both parties on the date of classification;

This is typically not an obstacle when applying these requirements against retirement plans since it easy to determine, based on employer records, who owns the benefits.

* was acquired during the period of marriage;

Something which qualifies as property will not always meet the criteria to be considered "marital property." The criteria to be considered "marital property" differs from state to state. However, the general consensus is that the property must have been acquired during the period of marriage in order to be considered "marital property." Typically, property acquired prior to the marriage or after the

marriage has ended is considered separate property, not qualifying as "marital property."

In order to determine whether a pension is marital or separate property, the period of time over which it was acquired must be determined.

In general, Courts have decided that retirement benefits are a form of deferred compensation for past employment. Therefore, it is logical to conclude that such is earned over the course of the employee's years of service.

In reconciling retirement benefits versus other property, the courts have held that similar to other property, a retirement benefit is acquired when its economic value is being created. The economic value of a retirement benefit is created during the period of time such benefits are being earned, not when they are being received. Therefore, if the employee is earning the right to receive retirement benefits for employment which took place during the period of marriage, such retirement benefits would be considered marital property. If the retirement benefits are earned relative to employment which took place either before or after the marriage, such benefits would be considered separate property. It should be noted that the point in time retirement benefits are received has no effect on determining whether or not they are considered marital property.

The method for determining what portion of an employee's pension is to be considered marital property and which is separate property depends upon the type of plan. Under a defined contribution plan, the marital portion would be comprised of contributions made by the employee during the period of marriage and

contributions made by the employer which are attributable to service performed during the marriage. The separate property component would be comprised of contributions made by the employee prior to or after the marriage or from private funds, and contributions made by the employer for service performed either before or after the period of marriage. In addition, any investment gains (or losses) should be applied proportionately against both the marital and separate property interests.

Determining the marital property interest of a defined benefit plan can be a more complex issue. Since neither the employee nor the employer make regular equal contributions, it is not possible to use the same approach as is followed for a defined contribution plan. In determining the marital portion of a defined benefit plan, a Coverture Fraction has become a relied upon tool of the Court. This fraction compares the period of time the employee was married and earning retirement benefits to the total period of time the employee was employed and earning benefits. The formula is as follows:

$$\frac{\text{time employed during the marriage}}{\text{total time employed}} = \text{coverture fraction}$$

For example, if the employee worked for the same company for 20 years, 14 of which coincide with the period of marriage, 14/20 or 70% of his retirement benefits are marital property.

As the example illustrates, the coverture fraction is used to determine only the marital share of the pension. The separate property interest would be 6/20 or 30%,

where 6 is the number of years the employee was earning benefits outside of the period of marriage.

* does not specifically qualify as separate property of either party.

In determining that portion of retirement benefits which were accumulated during the period of marriage, in many instances, the portion which were accumulated outside of the marriage becomes obvious. Very few states provide amnesty to specific retirement benefits in the property division arena. Therefore, in conducting an analysis of benefits to examine them against the above discussed criteria, qualification under this category will become obvious.

CHAPTER 5
DISTRIBUTING RETIREMENT BENEFITS

Deciding upon the best method for distributing retirement benefits can be one of the most difficult problems faced in a divorce. Most states do not prescribe one method as being superior or preferable to another, but instead provide the court with options. The two most common methods of distributing retirement benefits in divorce are the Immediate Offset Method and the Deferred Distribution Method.

The Two Methods of Distribution

The major difference between the Immediate Offset Method and the Deferred Distribution Method is the time at which the division of benefits occurs. Under the Immediate Offset Method, the court determines the present value of the retirement benefits and then awards the spouse a lump sum interest in cash or other property. In other words, the spouse receives an interest in other property owned by the parties which is equal to his/her interest in the pensionholder's benefit, and the pensionholder retains full ownership rights to the retirement benefits.

The Deferred Distribution Method does not provide for an immediate division of the benefits. Instead, the court determines the percentage interest or specific dollar amount to be awarded to the spouse, and orders that the spouse receive this award when the pensionholder is eligible to receive retirement benefits. In most cases, the pensionholder will not be eligible to receive retirement benefits until a date some

time in the future. Therefore, distribution of the benefits is deferred until a point some time in the future. This method of distribution is accomplished by a Court Order (example - Qualified Domestic Relations Order).

Strengths and Weaknesses of Immediate Offset Method

The two methods of distribution have their own sets of strengths and weaknesses. The primary strength of the Immediate Offset Method is that it completely resolves the issue of dividing the pension at the time of the divorce. The benefits are divided, and each party walks away from the table with their respective portion at the time of the divorce. Due to the often adversarial nature of divorce, divorcing parties are notoriously apt to pursue litigation and continue fighting over unresolved issues even after the divorce is final. Therefore, the battle could continue long after the parties are divorced, thus creating additional legal bills and litigation costs and occupying the court's time. By using the Immediate Offset Method all issues are resolved, thereby eliminating the possibility of future litigation.

The weakness of this method lies within the notion that the court must base its decision on assumptions rather than absolute fact. In order to use the Immediate Offset Method, the present value of the retirement benefits must be determined. The present value is determined using actuarial assumptions relative to the pensionholder's projected lifespan. These actuarial assumptions measure the probability that the pensionholder will reach retirement age, thus entitling him/her to benefits, and the length of time beyond his/her retirement date that benefits are expected to be received. These projections are based upon averages. Therefore, the

present value of the benefits will be correct based upon the average case. However, no case is exactly average. In the event that the pensionholder would die prematurely before he/she reaches retirement age, the spouse would have received his/her interest in the retirement benefits at the time of divorce, which due to the death of the pensionholder, were never actually received by the pensionholder. Therefore, one party received an interest in an asset which never flourished for the other party. Due to this pitfall, some court's have decided that the Immediate Offset Method places an uneven amount of risk on the pensionholder as compared to the spouse. The pensionholder ends up having to trade current dollars for future dollars which bare the risk of never being received.

However, this summation of an uneven balance of risk is inaccurate. Inherent in the present value analysis is a discount to reflect the likelihood that the pensionholder will not live long enough to retire and receive benefits. Following is a very basic example intended to illustrate the risk associated with Immediate Offset.

The present value of the pensionholder's retirement benefit is $50,000, assuming that he/she is currently age 65. However, on the date of the divorce the pensionholder is only 50, therefore, the present value is discounted to $25,000 to account for the 15 year deferred period until retirement. If the parties are going to divide the retirement benefits on a 50/50 basis using the Immediate Offset Method, the spouse would be awarded $12,500 at the time of the divorce, in lieu of his/her interest in the pension. If the pensionholder does not live to age 65 and begin receiving benefits, the spouse has been awarded a $12,500 windfall. However, if the pensionholder does live to age 65, the true value of the benefit was $50,000 of which

the spouse would have had a 50% interest or $25,000. Therefore, the pensionholder receives a $12,500 windfall if he/she lives long enough to receive benefits.

Therefore, as you can see, the real weakness of this method lies not in the balance of risk, but that the risk exists at all. As stated earlier, the present value analysis is based upon averages. A discount is applied to account for the probability that the pensionholder will not live to retirement. The likelihood of life after retirement is then based upon an average. The calculation of present value is exactly correct in the average case. However, the average scenario never exists. Therefore, the present value is never exactly correct relative to the case at hand. Based upon this, use of the Immediate Offset Method will always shortchange someone. However, who will be shortchanged is unknown. Therefore, both parties are wagering the benefits.

The Immediate Offset Method always has some mechanical problems. As discussed earlier, the court must decide on an appropriate present value of the retirement benefits. This can be difficult. The court must decide whether or not the assumptions used in the present value analysis are legitimate, and thereby, either accept or reject the final conclusions of value. Since many of the pieces involved in this analysis are assumptions and not fact, such can be the cause of arguments and litigation between the parties.

Strengths and Weaknesses of Deferred Distribution Method

The primary strength inherent in the Deferred Distribution Method is that it avoids the risk of harm to either party. Since this method distributes benefits as they are

actually received and not based upon an analysis of what would happen in the average case, there is no risk of awarding a windfall to one party or shortchanging the other party.

It is believed that under this method, the parties equally share the risk associated with receipt of benefits. If the pensionholder dies prior to retirement, in some cases, the spouse's interest in the benefit terminates. Therefore, each party receives nothing in the event of the pensionholder's premature death. However, the pensionholder is no longer alive to receive benefits, but the spouse is alive and left without a source of income. Therefore, it could be argued that this method of distribution does not necessarily protect both parties from harm since the spouse obviously bears all of the financial harm associated with the risk of the pensionholder's untimely death.

Another strength of the Deferred Distribution Method is that it allows each party to pay the appropriate income tax on the share of the benefits received. The assets traded in an Immediate Offset do not always have the same tax liabilities. The Deferred Distribution Method provides for benefit checks to be mailed to each party. Therefore, each party is responsible for the tax on the benefits they receive.

The Deferred Distribution Method has three primary weaknesses.

The nature of the Deferred Distribution Method provides for a division of retirement benefits at a date in the future. Therefore, there is not a complete and final division of property at the time of the divorce. The parties maintain a relationship, of sorts, until these benefits are distributed. This is in direct

opposition to the ultimate goal of a divorce, for neither party is truly able to make a fresh start free and clear of the other person.

Another problem found with the Deferred Distribution Method is that receipt of benefits by the spouse is contingent upon the survival of the pensionholder. In some cases, the unexpected death of the pensionholder will cause the spouse's rights to benefits to terminate. Therefore, the pensionholder's death can either jeopardize the spouse's retirement security or eliminate it all together.

The third and most significant flaw in this method is that, in reality, it is not always a simple task to determine the amount of the retirement benefits to be received by the pensionholder. In most cases, the plan will offer its employees a variety of benefit options to choose from at the time of retirement. Each of these options can generate a different monthly retirement benefit. Therefore, the pensionholder can make choices or not make choices, long after the divorce, which will affect the amounts to be paid to either party. These choices do not always directly relate to the honesty of the pensionholder. The pensionholder can unintentionally make choices which adversely affect the spouse's rights. Following is a summary of a list one court developed addressing these elections:

1 Pensionholder terminates employment, withdraws benefits, and does not reinstate benefits.

2 Pensionholder terminates employment, withdraws benefits, and subsequently does reinstate benefits upon reemployment with the company.

3 Pensionholder terminates employment, does not withdraw benefits, and leaves as a matured vested employee.

4 Spouse dies before pensionholder has either elected to terminate employment or retire.

5 Spouse dies after retirement but before the pensionholder.

6 Pensionholder dies before retirement.

7 Pensionholder dies after retirement but before the spouse.

8 Changes are made to the pension plan after the divorce but before retirement.

As you can see, some of the choices are made by the employer, can occur beyond the control of either party, can be viewed as being in good faith, deliberately in bad faith, or unintentionally. Nonetheless, all affect the manner in which benefits are distributed to both parties.

Reserved Jurisdiction Method

A small number of courts have recognized a variation on the Deferred Distribution Method for division of retirement benefits in divorce. This method, known as the Reserved Jurisdiction Method, provides the court with the ability to determine an appropriate award of benefits for the spouse, later, at the time of the

pensionholder's retirement, instead of establishing this award at the time of the divorce.

The advantages to using the Reserved Jurisdiction Method are similar to those discussed for the Deferred Distribution Method. That is the distribution of benefits to the spouse is based upon actual post-divorce facts and not upon an estimate of value predicated on assumptions about the average case.

However, there are serious problems associated with the Reserved Jurisdiction Method. The Court must hold a hearing at time of the employee's retirement to revisit this issue. Since the spouse's interest in the benefits would most probably be based upon only those benefits which accumulated during the course of the marriage, it does not seem necessary or advantageous to wait until a date in the future to decide an appropriate award. Holding a second hearing at a date in the future consumes the court's very valuable and precious time, and revisits issues that should have been addressed long ago. Further, the players involved in the case, such as the original attorneys, the judge, witnesses, may not be available at the time of the second hearing. This could lead to a rehash of old forgotten issues.

Given these problems, there is no suitable reason to choose the Reserved Jurisdiction Method over the Deferred Distribution Method.

CHAPTER 6
MECHANICS OF DEFERRED DISTRIBUTION

A number of important decisions must be made when developing the mechanics of a deferred distribution.

Method of Payment

The ideal method of paying both parties their share of the benefits is to have the pension plan itself send payment checks directly to both parties. This can be accomplished by using a Qualified Domestic Relations Order (QDRO).

The court can also order the pensionholder to pay the spouse his/her share directly as such benefit checks are received by the pensionholder. However, structuring payment this way can cause future enforcement problems. For this reason most courts tend to shy away from this type of arrangement. However, some state retirement systems do not permit court orders assigning benefits to the spouse. In this case, a direct payment from the pensionholder to the spouse is the only solution.

Time of Commencement of Benefits

Under the Deferred Distribution Method, benefit commencement to the spouse can occur either at the same time benefits commence to the pensionholder or at any time after the pensionholder is eligible to commence benefits. Using the actual date

the pensionholder commences benefits as a benchmark coincides with the notion that this method attempts to award the spouse a portion of benefits actually received by the pensionholder. However, restricting benefit commencement to the spouse until the actual date of commencement of the pensionholder gives the pensionholder complete control over commencement of benefits to the spouse. Therefore, if the pensionholder wanted to defer retirement for personal unknown reasons, commencement of benefits to the spouse would also be deferred. By deferring retirement, the pensionholder can inflict hardship upon the spouse.

To avoid this issue of control, benefit payments could begin being made to the spouse when the pensionholder reaches his/her earliest date of eligibility for retirement. In terms of this issue, the pensionholder's earliest date of eligibility would be the earliest date he/she could retire and receive full unreduced benefits. Using this date as a benchmark, eliminates the pensionholder's control over benefit commencement and removes his/her ability to inflict harm on the spouse.

Remarriage

As explained earlier, in most cases, deferred distribution of retirement benefits relates to division of property and not alimony or spousal support. It is therefore incorrect to restrict distribution of benefits based upon the marital status of the spouse.

Modification of the Award

Similarly, since distribution of retirement benefits is not typically done for alimony or spousal support, but instead represents payment for distribution of property, such distribution should not be eligible for modification under any circumstances.

Taxes

When a Qualified Domestic Relations Order (QDRO) is used to accomplish a deferred distribution, the Plan will send separate benefit checks to each party. Therefore, each party is responsible for the tax liability on the amounts received.

If a deferred distribution is accomplished by requiring the pensionholder to send checks to the spouse after the benefits are received from the Plan, the pensionholder pays all of the taxes associated with the benefits.

Death

From the standpoint of the terms of a pension plan, the death of the pensionholder under a deferred distribution can either terminate the distribution of benefits to the spouse or initiate payment of a survivor benefit to the spouse in lieu of the retirement benefits. The cause of action after the death of the pensionholder is dependant upon the agreement of the parties or the instruction of the court.

Obviously, the Plan will stop paying benefits to the pensionholder upon his/her death. This can also trigger the same termination of benefits for the spouse.

However, in order to eliminate the termination of benefits for the spouse, there are a few options that can be exercised:

* Pre- and/or Post- Retirement Survivorship rights can be established for the benefit of the spouse.

* An actuarially equivalent separate interest can be established for the spouse using a QDRO.

* The pensionholder can maintain a life insurance policy for the benefit of the spouse.

* The pensionholder can execute a contractual will providing the spouse with a claim against the pensionholder's estate.

Interest

It is incorrect to award interest on a deferred distribution award from a defined benefit plan. Typically, a defined benefit plan does not maintain a separate account which would be inclined to accumulate interest. Therefore, an award of interest would not be consistent with the style of the plan.

It is appropriate to award interest on a deferred distribution award from a defined contribution plan. For example, the spouse could be awarded 50% of the pensionholder's account as of the date of the parties divorce. However, the funds are not actually distributed to the spouse until a year later. The pensionholder has

had the advantage of using these funds, and the spouse has had the disadvantage of not being able to use these funds. If the funds belonged to the spouse as of the date of divorce, but were not distributed to him/her on that date, it is logical that the spouse should receive some compensation, in the form of interest, until he/she takes physical ownership of the funds.

Future Pension Options

As mentioned earlier, one of the major problems with a deferred distribution is the possibility that the pensionholder will elect or not elect certain benefit options available under the Plan which could jeopardize the spouse's interest in the pension. For example, the pensionholder remarries and elects to provide a survivor annuity for his/her new spouse. Maintaining this survivor annuity reduces the amount of pension benefits paid by the Plan on behalf of the pensionholder. Therefore, the amount paid to the spouse is also reduced. Further, the pensionholder could cancel his/her preretirement survivorship coverage assuming it is not necessary since he/she is no longer married. The premature death of the pensionholder could eliminate the spouse's claim for any benefits from this plan. To prevent the pensionholder from having the ability to either intentionally or unintentionally harm the spouse's interest in the benefits, the Court can dictate the choices to be made by the pensionholder.

Loss of Pension Benefits

Opinions are divided relative to what happens when the pensionholder loses his/her right to pension benefits due to termination of employment based upon grave

misconduct. If the pensionholder commits an act after the divorce which justifies the pension plan to revoke all retirement benefits, is it fair that the spouse should also suffer these same consequences? If benefits are revoked, the Plan will not be able to pay the spouse his/her share, since all benefits payable on behalf of the pensionholder are terminated. However, the pensionholder could be ordered by the court to compensate the spouse directly for his/her loss of benefits.

Using Present Value to Set a Maximum Amount Payable

Some Courts have attempted to use a present value figure to establish a maximum amount payable to the spouse under a deferred distribution. For example, the present value of the pensionholder's benefit was $60,000, of which the spouse has been awarded 50%. A court may award the spouse 50% of each pension payment until a total of $30,000 has been sent to the spouse (50% of $60,000 equals $30,000).

Using this approach results in a substantially inaccurate award to the spouse. Present Value, in its very nature, relates to the value of something at the present time. However, a deferred distribution pays benefits at a point in the future. Structuring an award in this manner equates $30,000 payable right now with monthly installments that total $30,000 beginning at some point in the future. These two payment arrangements are not equal. For example, if a borrower owed a bank a total of $10,000 on an outstanding loan, would the bank offer the borrower the choice of either a payment schedule where the total $10,000 is repaid in cash now or monthly payments starting 5 years from now until the bank receives the total $10,000? There is not a bank in the world that would offer such a deal to its

customers. The $10,000 in cash now is worth more than monthly installments that equal $10,000 in excess of five years from now.

The proper method of fashioning a deferred distribution award to the spouse is to pay him/her a portion of each benefit check received by the pensionholder with no limitation. The very nature of the Deferred Distribution Method is to distribute between the two parties the actual benefits that are payable to the pensionholder.

CHAPTER 7
USE OF A QUALIFIED DOMESTIC RELATIONS ORDER (QDRO) TO ACCOMPLISH A DEFERRED DISTRIBUTION

Introduction

What is a Qualified Domestic Relations Order (QDRO)?

Simply stated, a QDRO is a written set of instructions that explains to the administrators of a pension plan that a portion of one of its member's pension benefit is subject to division pursuant to a divorce. The QDRO provides the Plan Administrator with all of the factual information about the two parties, such as names, addresses, dates of birth, and social security numbers, as well as, any and all information required by the Plan in order to determine how to distribute the benefits. This may include a formula for the Plan to determine how much is to be paid to the spouse, when it should be paid, how it should be paid, what happens if the member dies, what happens if the spouse dies, and so on.

The formal definition of a QDRO is as follows: The term Qualified Domestic Relations Order refers to a judgment, decree or order that creates or recognizes the existence of an alternate payee's right to receive all or a portion of a plan participant's benefits payable under an ERISA-qualified employee benefit plan.

ERISA, REA and the Antialienation Provision

The Employee Retirement Income Security Act of 1974, as amended (ERISA) was established to protect the interests of employees who participate in employer sponsored pension plans. In basic terms, this federal law enacted guidelines for employers to follow relative to the retirement plans being offered to their employees. Such guidelines include, but are not limited to, set funding standards and reporting and disclosure requirements. ERISA also contains language which prevents plan participants' benefits from being assigned to another party, such as in a bankruptcy or creditor situation. The Retirement Equity Act of 1984, as amended (REA) opened the door for a new interpretation of the antialienation provision contained in ERISA. A limited exception to this antialienation provision was created which provides for the existence of QDROs. This exception provides that benefits accrued by an employee may be paid to another person provided such person meets the definition of an alternate payee, and the order issuing such payment meets the criteria of a QDRO.

A QDRO can be drafted for the following reasons: (i) equitable distribution of marital property; (ii) child support; or (iii) spousal support or alimony. The definition of a qualified alternate payee is a spouse, former spouse, child or other dependent of the plan participant.

Criteria for a QDRO

There are specific requirements that must be included in all proposed domestic relations orders before they can be considered a QDRO. The criteria in basic terms are as follows:

1.) The name and last known mailing address of the participant and alternate payee.

2.) The amount or percentage of the participant's benefits to be awarded to the alternate payee, or the manner in which the amount or percentage is to be determined by the plan.

3.) The number of payments or period to which the order applies.

4.) The name of each plan to which the order applies.

5.) The order must relate to the provisions of child support, spousal support/alimony or marital property rights for a spouse, former spouse, child or other dependent of the participant.

6.) The order must be made in accordance with a state domestic relations law (including a community property law).

7.) The QDRO may not require the plan to provide any type or form of benefit, or any option not otherwise provided under the terms of the plan.

8.) The QDRO may not require the plan to provide increased benefits determined on the basis of actuarial value.

9.) The QDRO may not require the payment of benefits to an alternate payee that are required to be paid to another alternate payee under another order previously determined to be a QDRO.

Types of Plans

QDRO Issues under ERISA Defined Contribution Plans

A Defined Contribution plan is a pension plan which has an account specified for the individual employee where a defined amount is being contributed to the plan by the individual, the employer or both. Examples of this type of plan are 401(k), 401(a), Employee Stock Ownership Plan (ESOP), Savings Plans and Profit Sharing Plans.

An Alternate Payee can be awarded a portion of the Employee's account pursuant to a QDRO. The Plan will establish a separate account for the Alternate Payee, and offer the Alternate Payee the same investment opportunities that are available for other participants. If the Alternate Payee chooses, it is usually possible to transfer the funds awarded to an IRA or other tax qualified account of his/her choice. By using a QDRO to award funds from this type of plan, early withdrawal penalties are avoided, and the Alternate Payee will be held responsible for the taxes on any distribution he/she receives from the Plan.

Under most plans, it is possible to award the Alternate Payee a portion of the Employee's account balance as of a specific date (i.e. 50% of the account balance as

of July 7, 2000), plus any investment gains or losses attributable thereon from that date until the date the Alternate Payee receives a distribution from the Plan.

Since this type of plan affords for an Alternate Payee to receive an immediate lump sum distribution, the terms of the QDRO are much simpler than the provisions contained in QDROs for other types of plans.

QDRO Issues under ERISA Defined Benefit Plans

Defined benefit pension plans provide retirees with a predetermined monthly retirement benefit upon reaching a specific age. The retirement benefit paid to a retiree is typically calculated using a formula which often employs years of credited service under the plan and salary information. The retirement benefit is typically payable to the employee upon attainment of their normal retirement age for the remainder of his/her lifetime. Benefits under this type of plan are often referred to as accrued benefits. This type of plan does not maintain individual accounts for employees.

It is important to remember that under this type of plan, the Alternate Payee is typically not awarded a lump sum cash payment from the Plan. It is usually a requirement of the Plan that the amount awarded to the Alternate Payee be expressed in terms of a monthly benefit payable for either the lifetime of the Participant or the Alternate Payee.

When writing a QDRO for this type of Plan there are two approaches that may be followed:

Shared Interest Approach: Under this type of QDRO, the Participant and the Alternate Payee "share" the benefit paid from the Plan. The Alternate Payee may not begin to receive benefits until the Participant actually retires and begins receiving benefits. The Plan will only pay the amount awarded to the Alternate Payee for the lifetime of the Participant. If it is the intention of the parties that the Alternate Payee receive benefits after the Participant's death, the Participant must elect a joint & survivor annuity upon his/her retirement and designate the Alternate Payee as the survivor annuitant for this benefit.

There are three disadvantages for following this approach to dividing the benefits.

* The Alternate Payee cannot begin to receive benefits under the Plan until the Participant actually retires and begins receiving benefits. Therefore, if the Participant chooses not to retire, the Alternate Payee never receives the amounts awarded.

* By forcing the Participant to elect a joint & survivor annuity with his/her ex-spouse as the designated survivor annuitant, any subsequent spouse of the Participant could be left without any share of the Participant's benefits after his/her death.

* The joint & survivor annuity will reduce both parties' share of the benefits.

Separate Interest Approach: Under this approach, the Alternate Payee and the Participant receive "separate" benefits. The Alternate Payee may begin receiving

benefits, at his/her election, anytime after the Participant reaches earliest retirement age. The Plan may perform various actuarial adjustments to the Alternate Payee's benefit in order to convert it to an amount that may be paid to him/her for life. Therefore, after benefits commence, the death of the Participant will have no affect on payment to the Alternate Payee.

There are three advantages for choosing this approach to dividing the benefits.

* The Alternate Payee does not have to wait for the Participant to retire to begin receiving benefits.

* The Participant does not have to make any choices that could jeopardize a new spouse in order to protect the interest of an ex-spouse.

* This separate interest approach provides more flexibility to both parties without a financial impact for either party.

Whenever possible, Pension Appraisers, Inc. promotes and follows the Separate Interest Approach in the QDROs drafted by our analysts.

DRO Issues under State and Local Government Plans

State, local government and municipality pension plans do not fall under the rules and regulations of the Employee Retirement Income Security Act of 1974, as amended, ("ERISA"). Therefore, most of these plans do not offer the same flexibility

in structuring the payment of benefits to an Alternate Payee pursuant to divorce. The two primary issues inherent in these plans are as follows:

1.) Benefits are payable to an Alternate Payee when the Participant actually retires and begins receiving benefits from the Plan. Unlike those plans which are qualified under ERISA, it is not possible for a governmental plan to provide for payment to an Alternate Payee when the Participant reaches earliest retirement age. Therefore, if the Participant decides to stay employed beyond his normal retirement date, the Alternate Payee will not be eligible to receive payment until the Participant actually retires.

2.) Benefits are typically payable to the Alternate Payee for the lifetime of the Participant. In the event the Participant predeceases the Alternate Payee 2 weeks after retirement or 20 years after retirement, at such time, payments to the Alternate Payee from the Plan will stop. Under certain plans, a court order can provide that the Participant must choose a specific benefit option which provides a survivor annuity to the Alternate Payee. However, this survivor annuity can sometimes be in excess of the amount awarded to the Alternate Payee as a division of the marital or community property, and most of the time will preclude the Participant from providing survivor benefits to a new spouse.

Before negotiating a settlement of pension issues, it is important to investigate the possibilities provided for division of benefits under the particular Plan in question. It is also important to remember that not all state and local governmental plans allow court orders distributing benefits to an Alternate Payee.

Court Ordered Benefits Issued under the Military Retirement System

The Uniform Services Former Spouse's Protection Act (Public Law 97-252) became effective on February 1, 1983. This permitted a former spouse to receive a portion of a member's retired pay through a court order. This act recognized the right of a state court to require the military to make direct payments to a former spouse of up to 50% of the member's disposable retired pay for purposes of division of property.

A court order directing the Defense Finance and Accounting Service (DFAS) must follow a shared payment approach. Therefore, payments will be made to the former spouse when the member actually retires and begins receiving benefits. These benefits will be paid to the former spouse for as long as the member is alive. Upon the member's death, all payments to the former spouse will stop. However, it is possible to designate the former spouse as the beneficiary of the Survivor Benefit Plan. In this case, upon the member's death, the former spouse would begin receiving the survivor benefit available under the survivor benefit plan.

SPECIAL RULES

***10 Year Rule**

In order for a former spouse to receive payments directly from the (DFAS), the member and former spouse must have been married for 10 years during which the member was performing military service creditable towards his/her retirement. In other words, if the marriage did not last for 10 years which coincide with 10 years of

military service on the part of the member, DFAS will not honor an order awarding benefits to the former spouse.

However, just because the 10 Year Rule is not met does not mean that a former spouse does not have a claim against retired pay. According to the laws of most states, retirement benefits accumulated during the period of marriage are deemed marital or community property. Therefore, it is possible for a former spouse to be awarded a portion of the member's retirement. However, the former spouse would have to receive his/her interest in the retirement benefits elsewhere (i.e. equity in the home, cash, payment made directly from the member, etc.).

***Remarriage**

In order to maintain eligibility for the survivor benefit plan, the former spouse must not remarry prior to reaching age 55. If the former spouse remarries prior reaching age 55, the former spouse may still be entitled to receive a portion of the member's retirement benefit, however, eligibility for the survivor benefit will be forfeited.

***One Year Rule for Survivor Benefit Election**

In order for the former spouse to remain eligible for survivor benefit plan coverage, the member must make an affirmative election for such coverage within one year of the date of the decree of divorce, dissolution or annulment. If the member neglects or refuses to make such affirmative election it is possible to protect the former spouse's entitlement to the SBP coverage by having the former spouse make a "deemed election" for such coverage within the one year time limit. Accordingly, the

member shall be deemed to have made the necessary elections thereby preserving the former spouse's entitlement to the SBP coverage.

Court Order Acceptable for Processing Issued under the Civil Service Retirement System (CSRS) and the Federal Employees Retirement System (FERS)

All employees of the federal government participate in either the Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (FERS). The plan in which an employee participates is usually based upon the Employee's employment date. Since these plans are administered by the federal government, they do not fall under the rules and regulations of the Employee Retirement Income Security Act (ERISA), and instead are dictated by federal statute. The title used by the Office of Personnel Management (OPM) of a court order directing payment of benefits to a Former Spouse is a "Court Order Acceptable for Processing" (COAP).

A court order directing the Office of Personnel Management to award benefits to a Former Spouse must follow a shared payment approach. Therefore, payments will be made to the former spouse when the employee actually retires and begins receiving benefits. These benefits will be paid to the former spouse for as long as the employee is alive. Upon the employee's death, all payments to the former spouse will stop. However, it is possible to establish the right of the Former Spouse to receive a Former Spouse Survivor Annuity. This Former Spouse Survivor Annuity would then be paid to the former spouse after the employee's death for the remainder of his/her lifetime.

SPECIAL RULES

*Remarriage

In order to maintain eligibility for the Former Spouse Survivor Annuity, the former spouse must not remarry prior to reaching age 55. If the former spouse remarries prior to reaching age 55, such former spouse may still be entitled to receive a portion of the employee's retirement benefit, however, eligibility for the survivor benefit will be forfeited.

*Health Benefits

A Former Spouse may be entitled to Federal Employees Health Benefit (FEHB) coverage if the Former Spouse is awarded, pursuant to a COAP, a portion of the Employee's retirement annuity after retirement or a survivor annuity upon the Employee's death, and applies for FEHB coverage within 60 days after the divorce. Such application should be submitted to the employing office where the Employee worked at the time of the divorce.

Deferred Offset Awards

In some cases, the Court or the parties have settled upon a Deferred Offset Award. This is a combination of an Immediate Offset and Deferred Distribution. The award is based upon an immediate offset, but is paid in installments. For example, the present value of the pensionholder's retirement benefit was $20,000. The spouse is awarded 50% or $10,000. However, in an attempt to preserve some of the cash

assets in the possession of the pensionholder, a payment plan is set up for payment to the spouse of his/her share of the pension.

However, this type of award possesses some problems. Present value provides the current lump sum value of the benefits. If benefits are going to be paid in the future, the present value is no longer relevant, and should not be used as the basis of an award. Is $10,000 in cash payable right now equal in value to $100 per month for the next 100 months? No. Fashioning an award using the present value in this manner substantially short changes the spouse.

To avoid this problem and stay within the confines of a Deferred Offset Award the court can implement an interest factor. Instead of paying the spouse $100 per month for the next 100 months to payoff a $10,000 obligation, the pensionholder can pay $138 per month for the next 100 months. This increase in the installment payment accounts for 8% interest per year on the amounts owed to the spouse.

Another problem with this type of award is that the parties are limited by the amount of liquid funds available to the pensionholder. If it is decided that the pensionholder is to pay $5,000 now and another $5,000 in 3 months to the spouse, in order for this to be feasible, the pensionholder has to have these funds available.

In order to avoid these issues, it may be easier to choose either the Immediate Offset or Deferred Distribution Method, instead of trying to implement parts of both principles.

Other Division Options

Liquidation

Another option would be to liquidate the plan and divide the proceeds between the parties. This option is only possible in cases were the plan allows for a liquidation of benefits. However, most plans either do not permit liquidation or assess substantial penalties against the benefits during the liquidation process. In addition, liquidating the benefits can cause severe tax implications, further exhausting the benefits. For these reasons, liquidation is not typically used as a reasonable method of division of benefits.

Informal Offset

When the parties retirement benefits are practically equal, the Court may avoid some of the complexities involved in division by doing a simple offset. Each party could be ordered to retain their interest in their own pension, and a small payment can be made to make up for any differential.

CHAPTER 8
MECHANICS OF IMMEDIATE OFFSET

Valuing Pensions for Equitable Distribution

When using the Immediate Offset Method of distribution, the pensionholder is awarded sole interest in his/her retirement benefits, and the spouse is given cash or another asset of equal value in lieu of his/her interest in the pension. In order to use this method, the present value of the retirement benefits must be determined.

Valuation of Defined Benefit Plans - Present Value

In order to determine the value of a benefit under a Defined Benefit Plan as of a specific date, the appraiser determines the present value (worth) of receiving a future pension benefit. This present value is determined using an appropriate interest rate and actuarial tables to measure lifespan.

Following is a step-by-step analysis of the present value process.

Step 1: Determine the Amount of the Benefit

Step 1 requires the appraiser to determine the amount of the retirement benefit that will be received by the pensionholder in the future. If the pensionholder has already retired, the actual amount being received can be used in the analysis. However, if the pensionholder has not retired, it is necessary to estimate the

amount the pensionholder will probably receive in the future. The amount to be received by the pensionholder can be affected by a number of different options. Therefore, the appraiser must make certain assumptions concerning the manner in which the benefits will be paid at a later date.

* Date of Retirement: One of the more important assumptions to be made in the analysis is the pensionholder's date of retirement. The assumed date of retirement should be an estimate of the most likely date the pensionholder will retire based upon the circumstances of the individual.

The most commonly used date is the actual normal retirement date used by the plan in question. However, any other date could be used if such other date is deemed to be a more appropriate date relative to the facts of the case in question. For instance, some courts have ruled that the earliest possible retirement date available under the plan should be used as the retirement date.

* Tax Consequences: Opinions are divided on the extent to which future tax consequences should be included in the valuation process. Retirement benefits are taxed when distributed to the pensionholder. Therefore, there is no question that the tax consequences associated with these benefits can play a role in the valuation process. The question, however, relates to the manner in which tax liability should be considered.

Most court's have concluded that it is inappropriate to apply a hypothetical tax that would be applicable to liquidation of the plan benefits. Since the plan benefits are not actually liquidated, such a tax could be excessive and would most likely not

reflect the actual tax that will some day be paid on these benefits. The Court may attempt to determine the tax that will actually be paid in the future or use a tax rate applicable to the facts at hand at the time of the valuation. A unanimous rule of thumb has not been established with respect to adjusting these value relative to future tax consequences. However, it is indisputable that such should play a role in the valuation process.

* Duration of Benefits: In addition to making assumptions concerning the options that will be exercised by the pensionholder, the valuator must also determine the length of time to which benefits will be distributed. Most defined benefit plans pay a retirement benefit beginning on the date of retirement and ceasing on the date of death. Therefore, actuarial tables can be used to estimate the total lifespan of the pensionholder, which in turn will illustrate the total period of time benefits will be received.

Step 2: Discount to Present Value

Step 2 employs the mathematics involved in discounting the expected future stream of income to present value.

Step 3: Mortality Discount

Step 3 employs a discount for mortality. This discount reflects the chance that the pensionholder will not live long enough to retire and actually begin receiving benefits. Obviously, this step is unnecessary if the pensionholder has actually

retired and begun receiving benefits. This discount is based upon the statistics found in actuarial tables.

Step 4: Discount for Vesting Status - If Applicable.

In a case where the benefits are not fully vested, the value must be further reduced to reflect the fact that if the pensionholder were to leave employment, he/she would not actually be entitled to the benefits being valued. If the benefits are partially vested, this discount should only be applied against the unvested portion.

Step 5: Apply a Coverture Fraction - If Applicable

In cases which take place in states which support a Dual Property Model for asset distribution, it is necessary to determine which part of the present value of the pension benefit is attributable to the period of marriage. This is accomplished by using a coverture fraction. Such fraction compares the period of time married and employed to the total period of time employed as of the date the marriage ended. The resulting percentage would be applied to the present value to determine that portion of the present value figure which can be attributed to the period of marriage.

In cases which take place in states which support an All Property Model for asset distribution, this step is not necessary. Under this model, all property owned by either party on the date the marriage ended would be considered marital property subject to distribution. Therefore, differentiating between that portion of the

pension which was attributable to only the period of marriage would be unnecessary.

Methods of Determining the Present Value of Defined Benefit Plans

Pension Appraisers, Inc. offers two methods of determining the present value of defined benefit pension plans for equitable distribution. Following is a brief description of the steps involved in each method.

GATT Method

(1.) Calculate the amount of the monthly pension benefit assuming the pension holder is at retirement age with a fully vested pension based upon compensation and plan provisions as of the date the marriage ended.

(2.) The present value analysis of this monthly pension benefit is conducted using Group Annuity Mortality Tables to gauge lifespan and the 30-Year Treasury Bill rate for discounting.

(3.) The present value is reduced to account for the vesting status of the pension holder (if applicable).

(4.) A coverture fraction is applied (if applicable based upon property model of the state which has jurisdiction over the divorce case).

PBGC Actuarial and Mortality Table Method

(1.) Calculate the amount of the monthly pension benefit assuming the pension holder is at retirement age with a fully vested pension based upon compensation and plan provisions as of the date the marriage ended.

(2.) The present value analysis of this monthly pension benefit is conducted using Group Annuity Mortality Tables to gauge lifespan and the Pension Benefit Guaranty Corporation interest rates for discounting.

(3.) The present value is reduced to account for the vesting status of the pension holder (if applicable).

(4.) A coverture fraction is applied (if applicable based upon property model of the state which has jurisdiction over the divorce case).

Other Techniques for Valuing Defined Benefit Plans

The most preferred method of determining the value of a defined benefit plan is to use the mathematical formulas which derive present value. However, there are some other ways to determine the value of these types of plans.

Valuation Formulas found within the Plan

Some plans have formulas in place which determine the value of the employees benefits. The result determined using this type of formula would certainly provide an indication of the value of the benefits.

Total Contributions to the Plan

The value of the benefits is equal to the total contributions made to the plan by or on behalf of the employee. This method does not consider the fact that these contributions increase in value over time. Using this method will always result in a lower value than would be determined using the present value method. Therefore, this method is typically not acceptable.

However, in some cases, this is the only method available. In certain instances, if an employee's benefits do not vest, the only money offered is the total of the contributions to the plan. In such a case, the total contributions would provide an accurate picture of the value of the benefits.

Total Offset

Under the total offset method, the value of the pension is equal to the expected annual benefit times the owner's life expectancy after retirement. This sum is not reduced to present value, on the assumption that the gain after divorce through interest and appreciation will be exactly offset by the loss due to inflation. This assumption is untrue, however, as interest rates have generally exceeded the inflation rate. As a result, the cases uniformly reject the total offset method.

Withdrawal Value

The withdrawal value of the pension is the amount which would be received if the employee decided to liquidate his/her interest in the plan. This withdrawal value would include various taxes and/or penalties which would not normally be incurred under the plan. Therefore, this is not an appropriate reflection of value unless the employee actually does liquidate his/her rights to the benefits.

Valuation of Defined Contribution Plans

The value of a Defined Contribution Plan on any date is the sum of the market values of all investments in the plan on that date. The services of a pension appraiser normally would not be required to determine the value of this type of plan, unless the pension holder was participating in the plan prior to getting married or opposing council needs confirmation of the value. In most cases, the administrator of the plan can advise the employee as to the market value of his/her share of the investments in the plan on any specified date.

TYPICAL SCENARIO: On April 1, 2000 Mr. and Mrs. Jones ended their marriage. Mr. Jones started participating and had been enrolled in a Defined Contribution Plan a few years after they were married. The benefit he was entitled to receive had vested but not matured. On June 1, 2000, the plan administrator informed Mr. Jones that the value of his plan on April 1, 2000 was $40,000. For equitable distribution purposes, the present value of Mr. Jones' plan on April 1, 2000 was $40,000. In this case the services of a pension appraiser would not be required unless a confirmation of the value is required by the court.

However, if the pension holder was participating in a defined contribution plan prior to getting married the process may not be as straightforward. If the state which has jurisdiction over the case is a Dual Property Model state, then it may be necessary to hire a pension appraiser to determine the portion of the plan which is subject to equitable distribution. The pension appraiser may employ one or all of the following methods.

Segregation Method

The account balance on the Date of Marriage, plus all interest and investment growth attributable to these monies is subtracted from the account balance on the Date the Marriage Ended. The difference is the value of the account for equitable distribution. This approach assumes that any growth in separate property during the marriage is considered separate property. Most Dual Property Model states view this growth as separate property. However, this is not true for all Dual Property Model states, and should be researched before using this method.

If the Immediate Offset Method is chosen for division of this asset, this method can be used to track the growth on the marital portion of the plan from the date the marriage ended to the date of distribution.

Subtraction Method

The account balance as of the Date of Marriage is subtracted from the account balance as of the Date the Marriage Ended. The difference in the account balances is the value of the account for equitable distribution. This approach assumes that

any growth in separate property during the marriage is considered marital property. Only a few Dual Property Model states view this growth as marital property.

Coverture Method

The account balance as of the Date Marriage Ended is multiplied by a coverture fraction to determine the value of the account for equitable distribution. Because proration by contributions is always more accurate than proration by time, it is an error to use a coverture fraction to determine the marital interest in a defined contribution plan. However, if the information is not available to track the growth of contributions and interest by the Segregation Method this method should be utilized.

CHAPTER 9
DISCUSSION OF SPECIAL ISSUES

BANKRUPTCY

Definition: Bankruptcy is a legal proceeding in which a person who is financially insolvent requests the Federal Bankruptcy Court to determine the extent of his or her debts and how his or her assets should be used to pay those debts. Property in bankruptcy is usually administered for the benefit of the bankrupt person's creditors.

General Discussion: There is a general consensus that bankruptcy does not impact the equitable distribution of pensions in divorce cases.

While courts have taken a number of different paths, the destination reached is usually the same. A spouse should not be able to defeat or delay the effect of a property division order by filing bankruptcy. The following quote has been cited frequently to sustain this result:

"We doubt that Congress ever intended that a former wife's judicially decreed sole and separate property interest in a pension payable to her former husband should be subservient to the Bankruptcy Code's goal of giving the debtor a fresh start."

Classification: Pension benefits are generally considered marital property and their classification remains unaltered during bankruptcy proceedings.

Valuation: Valuation of the benefits should be performed as it normally would be in accordance with the type of pension benefit in question.

Distribution: Distribution should likewise remain unaffected.

EARLY RETIREMENT SUBSIDY

Definition: An early retirement subsidy (early retirement incentive or severance package) is a benefit or bonus offered by a corporation to employees with the intent to induce them to retire prior to their normal retirement age.

General Discussion: The age of downsizing and the increased use of computer technology has made the offering of early retirement subsidies a common occurrence in corporate America. Companies offer these bonuses for early retirement as a method of eliminating outdated job positions, unproductive employees, and long time highly paid employees in obsolete jobs.

The early retirement subsidy comes in a variety of forms:

1. Those employees who have attained a set amount of years of service, maybe 30 years, are able to retire at an earlier age without penalty to their benefits.

2. Those employees who have achieved a set amount of years of service are given the opportunity to retire immediately and the corporation will add a set amount of years of service to their pension benefits.

3. A lump sum cash payment or severance package is offered to employees with a set amount of years of service in order to make early retirement more attractive.

4. Any combination of the above can be offered in one package to employees. Further, a corporation can offer anything that is perceived to have value to the employees in order to induce early retirement.

Classification: In order to determine if early retirement subsidies, incentives or severance packages are marital assets subject to distribution, the critical issues revolve around the corporations reasoning for developing the benefit package, how such package is intended to compensate the employee, and when it is received by the employee.

The Courts have looked at the following specific issues:

1. Is the early retirement subsidy a reward to the employee for work performed in the past or is it a severance package designed to compensate the employee for the loss of future earnings?

Many early retirement subsidies are calculated based upon an employee's years of tenure with the company. Various Courts have viewed this enhancement to the pension benefit of any employee as a bonus for work performed in the past, thus classifying it as deferred compensation. The enhancement is merely a modification of the pension, not a new benefit, and therefore, marital property subject to distribution.

Many Courts have viewed the severance package as compensation for the loss of future earnings. Therefore, the bonus is intended to assist the employee until new employment can be found. Since it can be viewed as replacement of income, the Courts have considered it the separate property of the employee.

2. Was the early retirement subsidy commonly offered by the corporation, thereby, making it a benefit package that the employee expects to receive?

Many Courts have declared that if the parties had an expectation prior to the date the marriage ended that an early retirement package or subsidy would be received later, such benefit would be considered marital property and thereby distributable.

Conversely, Courts have decided that if a lump sum payment/severance package/early retirement subsidy is offered by a corporation at its discretion, and therefore, not available to all employees, such benefit, if received after the date the marriage ended, should be considered the separate property of the employee. This benefit is not a reward for prior service, nor was it expected, therefore, cannot be classified as jointly owned property.

Courts in community property jurisdictions have tended to analyze the classification issue, whether the subsidy is for past or future service, an expected benefit or unexpected bonus, in more detail than courts in equitable distribution jurisdictions. The Courts ability to classify the individual benefit received in each case has dictated its consideration as marital or separate property.

The Two Arguments:

When representing the spouse of an employee, the primary goal is to argue that the severance package or subsidy is deferred compensation. In making this argument it is helpful to show that the subsidy is directly linked to the employee's years of service and salaries achieved with the company during the marriage. It is also helpful to illustrate that the parties expected to receive such a subsidy upon the employee's retirement.

When representing the employee, if an early retirement subsidy has not been offered at the time of divorce, it is important to stress that the possibility of receiving an early retirement subsidy or severance package at some time in the future is too speculative to quantify. Further, it should be argued that such a subsidy or severance package is strictly compensation for the loss of future income rather than a form of deferred compensation.

Valuation: The Court has discretion in its choice of method of valuation. However, the most commonly used approach would be the Time Rule or Coverture Fraction. This method compares the employee's length of service during the period of marriage with the employee's total length of service with the company.

Distribution:

Immediate Distribution (Immediate Offset): If the early retirement subsidy has been offered to the employee at the time of divorce, the present value of the early retirement subsidy can be quantified, and offset by other assets acquired

during the period of marriage. If the subsidy or enhancement has not been put into place at the time of divorce, it is impossible to attribute value to it.

Deferred Distribution: In a scenario where the subsidy or enhancement has not been offered or realized at the time of the divorce, a deferred distribution is the more preferable method of distribution. It can be provided that in the event such a subsidy is offered and accepted by the employee, at that time the former spouse shall be entitled to a portion of such subsidy. Therefore, it is divided among the parties if, as and when it is actually received.

NON-VESTED PENSION BENEFITS

Definition: A non-vested pension plan is one in which the employee has not completed the required years of creditable service in order to earn the right to receive benefits under the terms of the plan. Most pension plans require members to achieve a set number of years of creditable employment before being entitled to pension benefits under the terms of the plan (i.e. 3 years, 5 years, 10 years, etc.). Vesting occurs when the employee completes the number of years of service required to receive benefits under the plan at some point in the future.

General Discussion: Non-vested pensions, though not entirely earned, represent a form of deferred compensation for service performed over the course of a number of years. Although vesting occurs on one day, it is not logical to assume that the pension benefit for all years of employment up to that day was entirely earned on that one day. For example, an employee's benefit may vest after completion of 5 years of service, however, the employee could not achieve vested status without

being employed for the 4 years and 364 days prior. Therefore, part of the value of the vested pension after 5 years must have been attributable to the first 4 years and 364 days of employment.

Classification: There seems to be a general consensus that non-vested pension rights, to the extent that such rights accrued during the period of marriage, are considered marital property. A non-vested pension should not be considered entirely marital property, but such portion of the non-vested benefits which are attributable to service performed during the marriage should be included in the marital estate.

Valuation: Determining the value of the marital portion of a non-vested pension can be difficult. The following facts should be examined in determining value:

* the time left before the benefits become vested
* the length of the parties marriage
* the contributions of both parties (primarily and secondary) to the pension

The difficulty of determining the exact value of the plan can be avoided by deferring payment of the other spouse's share until the time pension benefits begin.

Distribution: Non-vested pension rights which accrue during the marriage constitute marital property and may be divided using either the immediate offset method or the deferred distribution method.

The most appropriate method of distributing a non-vested pension between divorcing parties is using the deferred distribution method. At the time the pension becomes payable the appropriate portion of the benefits are distributed to each party. Using the deferred distribution method eliminates any uncertainty about the vesting status and/or maturity of the benefits which would play a role in determining value for an immediate offset.

When using the immediate offset method of distribution it is necessary to establish a value for the non-vested benefits and award another asset in lieu of the non-vested benefits. However, inherent in this approach is the uncertainty of the vesting status of the benefits. If another asset is awarded to the spouse in lieu of the non-vested benefits, and the benefits never reach vested status, the employee is short changed. If the employee is willing to assume the risk that the benefits will never vest, it is possible to determine a value for immediate offset. Such value should reflect a calculation based upon the contingency of the benefit.

It should be noted that delaying distribution of pension benefits is not the same thing as delaying a decision about each spouse's share of a retirement plan. Some courts have found that a possible solution to the problem of distributing non-vested benefits is to wait until such benefits vest to make a decision about how to divide the property. However, most courts have condemned this notion of postponing a decision about pension distribution.

PASSIVE APPRECIATION

Definition: In the context of this discussion, passive appreciation is the term being used to describe any increase in value that occurs in a defined contribution plan from the date of the marriage until the date the marriage ended that is a result of only investment experience and market fluctuations.

General Discussion: Passive appreciation describes the growth experienced on the account balance of a defined contribution plan as of the date of the parties marriage until the date the marriage ended. For example, Jane Doe had a 401(k) Plan with her employer that had an account balance of $10,000 on the date of her marriage. On the date her marriage ended, the account value had grown to $15,000. Over the course of the marriage, no additional sums were contributed to this account. Therefore, the passive appreciation experienced in her 401(k) Plan totaled $5,000. This appreciation is termed as "passive" due to the fact that the growth in the account is not a direct result of the efforts of the employee, but rather the effect of market fluctuations and positive investment experience.

Classification: Some states have determined that passive appreciation is marital property subject to distribution. Other states have decided that this passive appreciation is not marital property, but rather the separate property of the employee.

Valuation: Determining the actual amount of passive appreciation experienced in an account can be an difficult process. The actual investment experience which occurs in the account over a period of time must be traced using all of the relevant statements and/or other information supplied by the plan.

Distribution: If the passive appreciation is determined to be marital property subject to distribution, such amounts can be distributed using either Immediate Offset or Deferred Distribution.

POST-RETIREMENT COST-OF-LIVING ADJUSTMENTS

Definition: A post-retirement cost-of-living adjustment is a small incremental increase made to a retiree's benefit on or after the date of retirement.

General Discussion: Cost-of-living adjustments, if available, are typically given to retirees on an annual basis, and are often dictated by the CPI or the specific provisions of the pension plan. This increase in benefits should not be confused with an increase in benefits due to continued employment or increases in salary in the form of a raise provided while still employed. These increases are granted after retirement in an attempt to ensure that retirees' benefits will remain in line with the inflationary swings of the economy.

Classification: There seems to be a general consensus that cost-of-living adjustments should be considered marital property to the same extent that the pension itself is marital. The argument for inclusion of any COLA in the marital estate provides that any increase in the marital portion of the retirement benefit that is not a direct result of the efforts of the employee after the divorce would be considered marital property. Since cost-of-living increases are granted in the same amount and at the same time to all retirees under a given plan, it is easy to determine that such increase does not relate to the job performance or efforts of the employee.

Valuation: The variability of the cost-of-living adjustment is not sufficient to eliminate present valuation of such increases. Most authorities support discounting the current value of the cost-of-living increases to reflect any uncertainty and avoid potential unfairness. Most courts have ruled that future cost-of-living increases should be included when calculating the present value of a pension that will be subject to such increases.

Distribution: Cost-of-living adjustments can be included in an immediate offset when the COLA is included in the present value of the pension. Further, award of a portion of such COLA increase can be included in a deferred distribution by incorporating the appropriate language in a domestic relations order.

RETIREMENT INCENTIVES/SEVERANCE PAY

Definition: Compensation paid by a company to an employee upon termination. This is commonly referred to as a "severance package" which is offered to employees in case of layoffs or corporate downsizing.

General Discussion: Many states have not addressed the issue of severance pay as it relates to division of property incident in divorce. However, those states that have addressed this issue find that the cornerstone of classifying severance pay as marital property relates to whether or not such compensation is designed to compensate the employee for future loss of employment, thereby replacing future earnings, or is intended to compensate the employee for efforts made while employed during the period of marriage.

Classification: The argument that most states that have examined this issue find compelling is that severance pay is a form of compensation for future economic hardship due to loss of employment. Severance pay is designed to ease the financial conditions during an employment transition and to compensate the employee for the losses attributable to an untimely dismissal. Therefore, the very nature of severance pay as replacement for wages that would have been earned by the employee after the marriage supports a classification as separate property.

Further, although at times a severance package may be based upon the length of service an employee had with the company, receipt of such package is conditioned upon termination of employment. Therefore, it can be considered a mere expectancy that has no value until termination of employment. Many courts have established that when termination does not occur during the marital partnership and the right to severance pay is not established during the marriage, severance pay is separate property.

Opponents to this argument reason that severance pay is marital property where the amount is based on the employee's past services to the employer and can be quantified as compensation for past labor.

Further, it is argued that severance pay that is considered compensation for past labor, rather than replacement for future earnings, and was acquired during the marriage is a marital asset subject to equitable distribution, even if it is obtained after filing of divorce complaint.

Valuation: Unless the employee has been terminated and offered a severance package, it is impossible to place a value on such benefits. As stated earlier, the possibility of receiving a severance package does not have any value unless the package itself is received by the employee. Once a severance package is offered, the value may be apparent, as is common with a one time lump sum payment (ex.: $50,000.00) or may be calculated using the methods developed for determining present value, as is common with an annuitized payment schedule (ex.: $1,000.00 a month for 24 months).

Distribution: The only appropriate method of distributing a severance package is by using the deferred distribution method. This will ensure that the nonemployee spouse does not receive compensation upon divorce for property that is never technically earned or received by the employee.

SOCIAL SECURITY OFFSET

Definition: A Social Security Offset is a reduction in the value of pension benefits subject to equitable distribution due to an adjustment based upon hypothetical or actual Social Security benefits.

General Discussion: Numerous courts are struggling with the question of how Social Security benefits should be treated in equitable distribution. By Federal statute, Social Security benefits are not subject to equitable distribution in divorce proceedings. However, employees who participate in many of our governmental plans do not contribute towards Social Security, and instead make contributions towards their government pension plans. For these employees, a portion of their

pensions constitutes replacement for Social Security. Therefore, in theory, the retirement benefits payable under these governmental plans could be described as being made up of two parts; (i) actual pension, and (ii) "hypothetical" social security.

Considering the federal statute which exempts social security benefits from equitable distribution in divorce, an argument can be made as to whether or not a portion of these types of government pensions should be sheltered from equitable distribution to the extent that such portion represents a replacement for social security. Conversely, there is some controversy as to whether of not actual social security benefits should be considered and/or divided in equitable distribution.

There are essentially two viewpoints on the issue.

1.) One argument advocates the consideration or reduction of either spouses' pension benefits based upon hypothetical or actual Social Security in determining the equitable distribution of the parties' property. This argument appears to work best in equitable distribution states. Unlike community property states, equitable distribution states do not require an equal split of all property acquired during the marriage, but instead give the court discretion to consider all of the parties' property in order to arrive at a just and reasonable division.

2.) Alternatively, the opposition argues that consideration or a reduction based upon hypothetical or actual Social Security is not appropriate. Several courts have concluded that a pension which is a substitute for Social Security may nonetheless be treated as marital property subject to division.

Classification: According to Federal statute, Social Security benefits are not divisible in divorce proceedings, and therefore cannot be considered a marital asset. However, Federal Law does not prohibit the division of pension benefits that are received in lieu of Social Security; thus allowing these plan to be divided.

Valuation: If it has been determined that one or both spouses' hypothetical or actual Social Security benefits will be considered in determining the equitable distribution of the parties' property, then the method of valuation of the benefit(s) will depend upon the parties intent to do an immediate offset or deferred distribution of their other property.

Social Security is the Federal Government's version of a defined benefit plan. A defined benefit pension plan is a plan that promises to pay a specified benefit at retirement. When a spouse's rights under a defined benefit plan are valued for equitable distribution in divorce, it is necessary to reduce the benefits to present value. This present value is used in determining an appropriate credit under an immediate offset division of assets.

Distribution: Actual Social Security benefits are not divisible in divorce proceedings, and therefore, cannot be distributed as a marital asset. However, a pension which is a substitute for social security may, nonetheless, be treated as marital property and distributed upon divorce. The present value of such benefit may be determined for use in calculating an appropriate credit under an immediate offset. In addition, such benefits could be distributed under the deferred distribution method.

STOCK OPTIONS

Definition: A stock option is the right given to an employee by a corporation to purchase a set number of shares of the corporation's stock during a specific period of time at a fixed purchase price.

General Discussion: If an employee is given a stock option he/she is not required to purchase the stock, but can or may elect to exercise the option at his/her choice. Stock options are either statutory or nonstatutory.

Statutory options give the employee the ability to take advantage of special federal tax treatment that is accorded to incentive stock options. If the federal statutory regulations are met, the employee will not have to pay ordinary income tax on the options when they are granted or exercised. After they are exercised and sold they are taxed at the appropriate capital gains rate, provided they are held for the required amount of time. On the other hand, nonstatutory options usually are taxed as regular income when the option is granted (when the stock is purchased).

Why do corporations offer employees stock options? In order to determine the answer, each stock option should be analyzed on a case by case basis. The more common reasons are as follows:

1. The corporation wants to provide an incentive for the employee to remain with the company. This would represent compensation for services to be rendered in the future.

2. Options are offered to attract new employees who are usually then paid below the going rate in return for part of the future growth of the corporation. This would represent deferred compensation for services rendered in the present.

3. The corporation wants to give the employee a bonus for having done a good job. This would represent compensation for services rendered in the past.

Classification: In order to determine if stock options should be considered a marital asset subject to distribution, the critical issue revolves around the reason the corporation granted the stock options. Were they granted for past, present or future service? The courts generally follow a four step process to determine the marital portion.

Step 1: The court must determine the number of shares granted for past and future service.

Step 2: The number of shares granted for past service is deemed to be marital to the extent that the marriage coincides with the period of employment until the granting of the options.

Most states apply a coverture fraction (time rule) to determine the marital portion. The numerator of the fraction would represent the later of the beginning of employment or the beginning of the marriage to the date

the options were granted, and the denominator the date of employment to the date the options were granted.

Step 3: A second coverture fraction (time rule) would be applied to the number of shares granted for future service to determine the marital portion. This would represent the growth from the date the options were granted to the date the marriage ended (cut off date) and any additional growth due to contributions of the non-employee spouse.

Step 4: All options found to be marital could be divided between the parties. Any options not deemed marital property would remain the sole property of the employee spouse.

Most equitable distribution states have adopted the following positions relative to the classification of stock options:

Stock options which are exercisable upon the date the marriage ended or which may not be cancelled, and which may, therefore, be said to be vested as of the date the marriage ended, are viewed as marital property. Any stock options which are not exercisable as of the date the marriage ended and which may be lost as a result of events occurring thereafter (not vested), would be treated as the separate property of the employee spouse, even though they may vest at some time in the future.

Stock options that are designed to vest and become exercisable over a period of time should be considered both compensation for the employee's past services and

incentive for the employee to continue employment in the future. The options which have already vested would be a reward for past service rendered during the marriage, and, therefore would be marital property. Those options which have not vested represent a future right contingent upon continued service, and therefore would be considered non-marital property.

Most community property states take the opposite position. They have determined that unvested stock options constitute a contingent interest in property, and therefore are a community asset.

Valuation: The valuation of stock options is not difficult. The option is valued at the market value of the stock on the date of valuation less all costs associated with exercising the option. However, this simple calculation can be complicated by other factors such as:

1. Tax liability to the optionee;
2. The optionee may have to continue employment in order to exercise the option;
3. After exercising the option the optionee may be prevented from selling the shares;
4. The options may not be vested on the date the marriage ended;
5. The optionee may have to borrow money to exercise the option; and
6. There could be other contingencies.

Distribution:

Immediate Offset: Some courts take the position that this is the most equitable approach to use if the options can be valued. This is true even for options that have not been exercised. The optionee bears all risk relative to loss due to any cause. The optionee is awarded all the options and the non-employee spouse receives property of equal value.

Deferred Distribution: Because the possibility exists that the options might not be exercised most courts retain jurisdiction until they expire or are exercised to make a distribution between the parties.

SURVIVOR BENEFITS

Definition: A survivor benefit is a benefit which is paid by a pension plan to the designated beneficiary of an employee (usually a spouse) upon the death of the employee. Survivor benefits can be placed in two categories: pre-retirement survivor benefits and post-retirement survivor benefits. A pre-retirement survivor benefit is paid to the designated beneficiary of an employee in the event of the employee's death prior to retirement. A post-retirement survivor benefit is paid to a designated beneficiary upon the death of the employee after retirement. In most cases, the employee must make an affirmative election to establish these survivor benefits, and must always keep a current beneficiary designation on file with the Plan.

General Discussion: The issues surrounding the classification and division of survivor benefits as marital property can be very complicated. The intention of the

information provided herein is to shed some light on the basic issues. Certainly, the issues inherent in a particular case may be more complicated than the context of the information provided, and further research may be necessary to arrive at a suitable solution. Therefore, the information provided herein is intended as a general discussion.

Survivor benefits are typically elected to protect a spouse's interest in a pension. They can be viewed as a type of "insurance policy" relative to the pension. In many cases, once parties are divorced, and all property is divided, a former spouse no longer has an interest in the pension of the other spouse. Certainly this is true if the pension is divided using an immediate offset. Under such a case, the employee keeps his/her interest in the pension and the other spouse takes another asset of equal value in lieu of his/her interest in the pension. Therefore, each party receives his/her fair share of the property at the time of the divorce. In such a case, survivor benefits would be unnecessary since the Alternate Payee received his/her full interest in the pension at the time of the divorce.

On the other hand, if the parties decide to divide the pension using deferred distribution, it may be necessary to protect the former spouse's interest in the pension until such time as he/she can receive payment for their portion of the property. When drafting a Qualified Domestic Relations Order (QDRO) to divide a pension at the time the benefits have reached maturity for distribution, it may be necessary to establish the former spouse's entitlement to a pre-retirement survivor annuity, in the event the employee should die between the time the QDRO is drafted and the date the former spouse receives a distribution. Establishing this survivor annuity protects the former spouse's awarded share of the pension.

Further, under some plans it may be necessary to establish post-retirement survivor benefits for the former spouse to protect his/her interest in the pension plan if the employee dies prematurely after the monthly pension payments commence.

This discussion thus far has covered the reasons a survivor benefit may or may not be necessary in the context of a divorce. Certainly, if a survivor benefit has already been established at the time of the divorce, such is the case if the employee is retired, the issues dealing with this survivor benefit may be different than previously discussed. In this scenario, the survivor benefit could be considered the property of the former spouse, therefore, subject to distribution.

Classification: For purposes of this discussion, the classification of survivor benefits is addressed as such relates to an immediate offset and a deferred distribution.

Survivor Benefits and Immediate Offset

Addressing a survivor benefit in an immediate offset is only applicable if the employee has retired and elected a post-retirement survivor benefit for the non-employee spouse. Under most pension plans, once an election for post-retirement survivorship benefits is made, such election is irrevocable, even in cases of divorce. Therefore, even though the parties are divorcing, the nonemployee spouse is still guaranteed to receive a survivor annuity upon the death of the employee. This guaranteed right of the nonemployee to a benefit upon the death of the employee can be viewed as the property of the nonemployee under both the dual property and

all property models. Since such survivor benefit could be viewed as the property of the nonemployee/former spouse, it would be subject to distribution upon divorce.

Unless the employee makes an election for survivor benefits for the nonemployee spouse that is viewed by the plan as irrevocable, a guaranteed right to benefits has not been created for the nonemployee spouse. Therefore, if the absolute right to a survivor benefit has not been created, a survivor benefit would not meet the definition of "property" under either the dual property or all property models, and therefore would not be subject to distribution.

Pre-retirement survivor benefits are paid to the designated beneficiary upon the death of the employee while still employed. These survivor benefits are typically not viewed as property of either party under either of the property models. Such survivor benefits are paid instead of the actual pension in the event the employee should die prematurely during employment. If the employee dies during the divorce process, negotiation of property distribution could become a moot point.

Survivor Benefits and Deferred Distribution

In most circumstances, the courts have ruled that if it is necessary to provide survivor benefits in order to protect the former spouse's full property interest in the pension, such designation is appropriate. The courts have not viewed the election of pre-retirement survivor benefits and/or post-retirement survivor benefits under such a circumstance as an additional piece of property being awarded to the former spouse, but instead as a mechanism to protect the former spouse's already awarded property interest.

It is important to note that it is not always necessary to establish survivorship rights for a former spouse in order to protect his/her property interest. The nuances of any plan subject to deferred distribution should be investigated before any irreversible elections are made on behalf of the former spouse.

Valuation: As mentioned earlier, if a survivor benefit has met the definition of property under either of the property models, it is possible to determine an estimate of the present value of such benefit by using various assumptions. Included in this analysis would be all of the assumptions normally made when computing the present value of retirement benefits, as well as, an estimate of the date of death of the employee and the life expectancy of the former spouse after such date.

Distribution:

The only possible method for distributing property rights in a survivor benefit which has already been established for a former spouse at the time of the employee's retirement is through an immediate offset. ERISA does not allow assignment of survivor benefits to another party, and in many cases the right of the former spouse to the survivor benefit is irrevocable.

However, sometimes it is necessary to establish a right to survivor benefits when using deferred distribution. Establishing these survivorship rights protects the former spouse's interest in his/her already awarded property.

TAX CONSEQUENCES

Issue: Should the court take into consideration future tax consequences when distributing pension benefits?

General Discussion:

The states are mixed with regard to the propriety of reducing the value of a retirement plan to account for taxes that eventually may be owed on income received from the plan. Some courts have taken the view that income taxes should be subtracted when valuing a retirement plan, since the income will definitely be taxed when received. Others have held it improper because future tax rates are unknown and thus speculative.

When a retirement plan is distributed through a qualified domestic relations order (QDRO) which provides each spouse with a share of the plan as it is paid, the future income tax liability does not have to be deducted from the current value of the Plan. When the Plan distributes the benefits to each party, the appropriate deduction will be made from the benefits to account for income tax liability. However, if the court requires the participant to withdraw funds from the account, early withdrawal penalties and income taxes are normally taken into account.

APPENDIX I

GENERAL PENSION VALUATION FAQS

1. Why do I need to know the value of my pension?

If you intend to divide the retirement benefits using the Immediate Offset Method, it is necessary to establish a value for the pension.

2. What is the Immediate Offset Method?

The Immediate Offset Method of dividing a pension compares the value of the pension to the value of the other marital property. The employee will end up keeping his/her pension, and the spouse receives another asset of equal value in lieu of his/her interest in the pension. If the value of the pension is unknown, it is impossible to use the Immediate Offset Method to come up with an accurate property division.

3. What is the Deferred Distribution Method?

The Deferred Distribution Method of dividing a pension provides for the division of benefits to take place at a later date, when the benefits are actually being paid by the plan. This type of distribution is usually accomplished using a court order or Qualified Domestic Relations Order (QDRO).

4. If it is decided that the pension benefits will be divided using the Deferred Distribution Method, is it necessary to determine the value of the benefits?

In most cases, the answer would be no. If it is possible to divide all of the other property of the parties, and the pension is being distributed at a later date, when benefits are actually paid by the plan, it is unnecessary to know the value of the benefits at the time of the divorce. Since the benefits are not being distributed at the time of the divorce, knowing the value at such time would not be required in order to ensure a proper division of property. However, in some cases part of the pension will be included in an Immediate Offset and part will be distributed using a QDRO at a later date. In this case, knowing the value of the pension would be essential. Therefore, it is sufficient to say that in the typical case it is not necessary to know the value of the benefits if such benefits are to be divided using a Deferred Distribution. However, if you are not dealing with the typical case, certain calculations of value may be necessary in order to properly divide the benefits between the parties.

5. Which method of distribution is better, the Immediate Offset Method or the Deferred Distribution Method?

Both methods have their strengths and weaknesses. The appropriate method to be used in a particular case depends upon the circumstances involved in that case.

6. When valuing retirement benefits (either defined benefit or defined contribution plans) are the tax consequences associated with such benefits incorporated into the analysis?

When benefits are distributed by the plan to the employee, taxes will be assessed just as they are against a regular pay check. Therefore, it makes sense that taxes should be examined when valuing future retirement benefits. However, how much tax is appropriate and at what tax rate? Since the answers to these questions are presently unknown, most appraisers and courts, alike, are wary of applying a reduction to the value for future taxes.

FAQs FOR DEFINED BENEFIT PLANS

7. What is a defined benefit plan?

A defined benefit plan provides a retiree with a monthly payment beginning at retirement for the remainder of the retiree's lifetime. The benefit that is payable upon retirement is calculated using a formula. Such formula is defined within the context of the Plan. A defined benefit plan is the type of plan most commonly thought of when talking about pensions. It is paid monthly for the lifetime of the retiree starting at retirement.

8. What is present value?

Present Value is the current worth of a stream of income to be received in the future. In basic terms, the present value, as it applies to pensions, describes the

amount of money which would have to be invested or set aside by the pension plan today, so that sufficient funds would be available to pay out the pension amount throughout the employee's years of retirement. In order to determine present value, the appraiser will employ an appropriate discount rate and estimate the length of time the payments will be received by the pensionholder.

9. How is a present value appraisal used in the divorce process?

An estimate of the present value of a pension is essential when divorcing parties are attempting to divide the benefits using the Immediate Offset Approach. The present value of the pension can be compared to the other marital assets subject to distribution in an attempt to make a "trade-off." In such a case, the pensionholder would keep his/her pension and the spouse would take another marital asset of equal value to balance off the distribution. In order to be in a position to make a "trade," the value of the assets must be known. The present value report presents the current value of the pension for this purpose.

10. Are there different methods of determining the present value of a pension? How are the methods different?

Yes. There are two commonly recognized methods for determining the present value of a defined benefit plan for use in equitable distribution. These methods are referred to as: (i) the PBGC Actuarial and Mortality Tables Method; and (ii) the GATT Method. Pension Appraisers, inc. offers both of these methods of valuation to their clients.

A brief description of the methods and their differences follows:

The PBGC Actuarial and Mortality Tables Method uses the Group Mortality Tables to measure the employee's projected lifespan, and the interest rates published and used by the Pension Benefit Guaranty Corporation as discount rates.

The GATT Method uses the Group Mortality Tables to measure the employee's projected lifespan, and the 30-Year Treasury Bond rate as a discount rate.

As you can see, the differences in these methods lies within the interest rates used to discount to present value.

11. Which method will furnish the highest/lowest value?

There is no general rule of thumb that one method always produces a higher or lower value. There is an inverse relationship between interest rates and present value - the higher the interest rate, the lower the present value, and vice-versa. Since the interest rates utilized in all three methods fluctuate, any one can be higher or lower than any other one at any given time. Therefore, any of the three methods can generate a higher or lower present value on any given day.

12. Which method is the most valid?

Each of the methods are valid, and would be accepted in a court of law. They are basically just different ways of looking at the same issue. However, one method may be preferred in your state or county.

13. What is the "Valuation Date"?

The valuation date dictates the interest rate to be utilized in the analysis. For example, if the GATT Method of valuation is being used to generate a present value, and the valuation date is August 1, 2001, the interest rate utilized would be 30-Year Treasury Bond Rate in effect in the market on August 1, 2001. By using the interest rate in effect on the valuation date, the present value of the benefits corresponds to the value of the dollar (in the market) as of that particular date.

14. What is meant by the "Cut-Off Date," "Date of Classification" or "Date Marriage Ended"?

For purposes of the present value analysis, the cut-off, date of classification or date the marriage ended date refers to the date that marital property rights relative to the pension terminate. This date can be the separation date, the actual date of divorce, or some other date that may be mutually agreed upon by the parties. This date is different in every state, and is usually dictated by case law.

15. What is meant by "Normal Retirement Age"? What is meant by "Earliest Retirement Age"?

The normal retirement age of an employee is the age, based upon the terms of the plan, at which such employee could retire and begin receiving an unreduced benefit based upon the years of service earned by the employee as of the cut-off date. Normal retirement age may vary from plan to plan. Further, some states prefer

that the employee's earliest retirement age be used in the analysis of present value. An employee's earliest retirement age is the earliest age at which the employee can retire and receive a reduced benefit. This age may also vary from plan to plan.

16. What is an "Accrued Monthly Pension Benefit"?

The accrued monthly pension benefit is the amount that would be paid to the employee as a monthly pension benefit based upon the years of service earned by the employee as of the cut-off date payable when the employee reaches retirement. In other words, assuming the employee terminated his/her employment as of the cut-off date, the accrued monthly benefit is the amount that would be paid as a pension when the employee retires. Most plans have the ability to calculate this amount as of any cut-off date requested. Further, in many cases, employees are given annual benefit statements that illustrate their accrued monthly pension benefit as of December 31 of the given year.

17. What is a cost-of-living adjustment (COLA)?

A cost-of-living adjustment is a small incremental increase made to a retiree's monthly pension benefit in an attempt to keep his/her benefits in line with inflation. COLA increases are not applicable to every plan. Therefore, adjustments for COLAs would only be applicable in a present value analysis of benefits that have COLA adjustments guaranteed under the terms of the plan.

18. What is meant by "vested"?

All plans have vesting requirements. Such requirements dictate the period of time an employee must be employed before being guaranteed retirement benefits upon retirement. For example, under some plans the vesting requirement is 5 years. Therefore, an employee must work for 5 years before earning a guaranteed pension under the Plan. If the employee terminates employment after 6 years, such employee will still be eligible to receive a pension based upon the 6 years he/she was employed. However, if the employee terminates after 4 years, all benefits are forfeited.

19. Does an "unvested" pension have value for purposes of equitable distribution?

In most states, the answer is yes. If an employee's benefits are not fully vested as of the cut-off date, the present value of such benefits would be reduced to reflect the probability that the pension will not vest.

20. How is a disability pension treated during the division of assets in a divorce?

All states handle the issue of disability differently. In some cases disability is viewed as replacement of income, and therefore, not considered an asset until such time as it is converted to a retirement benefit. Some states do not make this distinction, and view the entire disability benefit as property. The specific standards set forth in a particular state should be examined before making a decision relative to handling disability.

21. Would an employee's status as "disabled" effect the present value process?

Yes. The present value would be calculated using special tables. Since a disabled person's projected lifespan may not be the same as a healthy person's life expectancy, special tables would have to be used which relate to people with disabilities.

22. If I participated in my pension plan before I got married, will this be taken into consideration during the present value analysis?

Whether or not benefits earned prior to marriage are included or excluded in the present value process depends upon the type of property model followed in a respective state.

In an All property Model state, typically, all property owned by one or both parties on the cut-off date is included in the marital estate, even if some of that property was actually acquired prior to marriage.

In a Dual Property Model state, only that property which was actually acquired during the period of marriage would be included in the marital estate. Therefore, any portion of the pension which was earned prior to the marriage would be excluded during the present value analysis. Typically, the appraiser will apply a coverture fraction against the present value of all benefits earned by the employee in order to differentiate that portion which was actually accumulated during the period of marriage.

23. What is a coverture fraction?

A coverture fraction is a tool used by an appraiser to separate that portion of the benefits which was earned during the marriage, from that portion of the benefits which were earned outside of the period of marriage. The coverture fraction represents that portion of the value of the benefits attributable to the marriage. The numerator of the fraction represents the total period of time the pensionholder participated in the plan during the marriage, and the denominator is the total period of time the pensionholder participated in the plan as of the cut-off date. The following example illustrates the mechanics of a coverture fraction:

Marriage Date: June 30, 1978
Date Employment Started: January 30, 1970.
Cut-Off Date: June 30, 1998.

The total number of years of participation in pension plan during the marriage equals 20 (from June 30, 1978 to June 30, 1998).

The total number of years of participation in the pension plan as of June 30, 1998 equals 28.5 (from January 30, 1970 to June 30, 1998).

Therefore, 20.00 Years = 0.7018 or 70.18%
28.50 Years

This means that 70.18% of the present value of the pension as of June 30, 1998 would be attributable to the marriage. For example: The total present value of the employee's pension plan was $100,000.00 as of June 30, 1998. The $100,000.00 would be multiplied by 70.18% to give a value for the marital portion of $70,180.00.

24. Does a coverture fraction always use time as its benchmark to determine what portion of the pension accumulated during the marriage?

No. In some cases measuring the period of time the employee participated in the plan against the total period of time the employee was a participant in the plan as of the cut-off date does not provide an accurate picture of the benefits which were accumulated during the marriage. Based upon the mechanics of the plan itself, it may be more appropriate to use contributions or actual service credit, instead of months or years. For instance, military reserve members receive a pension based upon the number of points earned during their service with the reserves. Due to the nature of being a reservist, more points may be earned in one year than was earned in another. Therefore, a coverture based upon the number of points earned during the marriage would provide a much better picture of the marital property portion of the benefits than just using the number of years the parties were married in the coverture.

25. How are Social Security Benefits handled in the divorce process?

According to federal statute, social security benefits are not typically included in the division of assets at the time of divorce. This is due to the very nature of social security. When social security benefits become payable, the social security

administration will give divorced spouses credit for each others social security benefits. Such calculations are built into the process of calculating an individual's social security benefit. If credit is given at the time of the divorce for a difference in social security benefits, and then again at the time social security is payable, division of these benefits will be made twice.

26. What if I do not contribute towards social security, but instead make a contribution towards my pension?

The large majority of those in the workforce pay into social security. However, there is a small population of those who instead of paying into social security, make a contribution towards their pension benefits. These individuals include members of the Civil Service Retirement System, certain policemen and firemen, some teachers and certain state employees. Whether you contribute towards social security or towards your retirement benefits depends upon the provisions set forth in your pension plan.

If you do not contribute towards social security, you may want to consider having a social security offset analysis done on your pension. In basic terms, this analysis will separate your actual pension benefits from what could be considered your "hypothetical social security benefit." This will enable you to remove any benefits you will receive in lieu of social security from the picture, thereby, providing a value of just the pension benefits to be used in the division process.

Certain courts have recommended that such an offset is appropriate, and other courts are still examining this issue.

27. Will every appraiser arrive at the same present value for an individual's pension benefits?

No. If appraisers use different assumptions, they will arrive at different answers. Following is a list of assumptions, that if different, can drastically effect the present value conclusion:

Valuation Date/Interest Rate
Date of Birth
Cut-Off Date
Normal Retirement Age/ Commencement of Benefits
Accrued Monthly Benefit
Cost-of-Living Adjustment
Vesting Status
Method of Valuation

The effect of a difference in some of these assumptions is obvious. For example, if one appraiser assumes you are older or younger than you really are, your projected lifespan will be different. Further, if the cut-off date is different, it is assumed that marital property rights stop at two different dates. Therefore, you will obviously get two different answers. If different monthly benefit amounts are used in the analyses, the answers generated will be different. However, some of the other assumptions are more effected by the mechanics of the mathematics. Therefore, the effect of the difference is not as obvious.

28. How does a difference in interest rate effect the present value?

A higher interest rate will result in a lower present value, and vice-versa. This is due to the principles of Time-Value-of-Money. Therefore, if two appraisers use two different valuation dates, thereby employing two different interest rates, they will arrive at two different answers. This is true even if all of the other assumptions made by the appraisers were the same.

29. How does a difference in retirement age effect present value?

The closer an individual is to retirement, the higher the resulting present value, and vice-versa. This is also due to the principles of Time-Value-of-Money. Therefore, if two appraisers use two different retirement ages, they will arrive at two different answers. This is true even if all of the other assumptions made by the appraisers were the same.

30. How does use of a Cost-of-Living Adjustment effect the analysis?

Use of a cost-of-living adjustment in a present value analysis reduces the interest rate employed. As mentioned earlier, a lower interest rate will result in a higher present value, and vice-versa. Therefore, if one appraiser uses a COLA in their analysis, and the other does not, they will arrive at different answers. This is true even if all of the other assumptions made by the appraisers were the same.

31. How does an individual's vesting status effect the present value?

If it assumed by one appraiser that all benefits of the employee are fully vested, but the other appraiser makes a reduction in value because it is assumed that such benefits are not fully vested, they will result in different answers. This is true even if all of the other assumptions made by the appraisers were the same.

FAQs FOR DEFINED CONTRIBUTION PLANS

32. What is a defined contribution plan?

A defined contribution plan is a retirement plan whereby the employer, employee or both make contributions towards an individual account established on behalf of the employee. Such funds can be invested, and upon retirement, the employee will receive either a lump sum payment of the amount held in the account or such balance will be converted to a monthly annuity payable for the lifetime of the employee. Examples of some defined contribution plans are as follows:

- 401(k) Plan
- Savings and Investment Plan
- Profit Sharing Plan
- Money Purchase Pension Plan
- Employee Stock Ownership Plan (ESOP)
- Tax Reduction Act Stock Ownership Plan (TRASOP)

33. How is a defined contribution plan valued for division in a divorce?

The value of a defined contribution plan is the total account balance maintained for an individual under the Plan as of any given date. Certainly the manner in which such an account is viewed as property will depend upon the property model followed in your state. Depending upon the property model followed, the entire account balance could be subject to division or, depending upon the circumstances of the employee's participation, only part of such account could be subject to division.

If an individual began participating in the defined contribution plan prior to marriage, the entire account balance maintained by the plan on his/her behalf may not be considered marital property. In this case it is the job of the appraiser to determine what part of such account balance is attributed to the period of marriage and which should remain the sole property of the employee.

Pension Appraisers, Inc. offers three methods of determining the portion of a defined contribution plan which accumulated during the period of marriage. It is important to remember that determining such a value is not always an exact science. The value of these accounts can change on a daily basis and some individuals may have participated in such plans for many years. Following is a brief explanation of the three methods:

Segregation Method: The account balance on the Date of Marriage, plus all interest and investment growth attributable to these monies is subtracted from the account balance on the Date the Marriage Ended/Cut-Off Date. The difference is the value of the account subject to division. This approach assumes that any growth in pre-marital account balance which occurred during the marriage is considered separate property. Most Dual Property Model states view this growth as separate

property. However, this is not true for all Dual Property Model states, and should be researched before using this method.

Subtraction Method: The account balance as of the Date of Marriage is subtracted from the account balance as of the Date the Marriage Ended/Cut-Off Date. The difference in the account balances is the value of the account subject to division. This approach assumes that any growth in the pre-marital account balance which accumulated during the marriage is considered marital property. Only a few Dual Property Model states view this growth as marital property.

Coverture Method: The account balance as of the Date Marriage Ended/Cut-Off Date is multiplied by a coverture fraction to determine the value of the account for equitable distribution.

34. Is one method more or less accurate or acceptable than another?

The method of valuation chosen would certainly depend upon the property model followed in a particular state. The Segregation Method can be very complicated, and typically requires a substantial amount of information about the account in order to perform the analysis. The Subtraction Method and the Coverture Method are much less complicated and do not require the volume of information about the account that is required for the Segregation Method. As stated before, determining the value of a defined contribution plan is not an exact science. It is important to understand the method of valuation being utilized. Understanding the mechanics of the method will help you understand the value being presented

APPENDIX II

GENERAL QDRO FAQS

1. What is a Qualified Domestic Relations Order (QDRO)?

In basic terms, a QDRO is a written set of instructions that explains to a plan administrator that two parties are dividing pension benefits due to equitable distribution. The instructions set forth a method for the plan administrator to determine how much of the benefits are to be paid to each party, when such benefits can be paid, how such benefits should be paid, etc.

2. What is a Domestic Relations Order (DRO)?

A DRO is the same set of instructions as a QDRO except it is written against a plan that is not qualified under certain federal statutes. DROs are typically written against governmental plans.

3. Can I write my own QDRO or DRO?

We do not recommend it. The true definition of these two documents is a lot more complicated than the definitions recited above. A QDRO must contain certain information which is outlined in the Employee Retirement Income Security Act of 1974, as amended (ERISA) and the Internal Revenue Code (IRC). Plans which

require DROs do not fall under the rules a regulations of ERISA, and therefore, must follow a different set of standards.

4. Who is the "Participant" under a QDRO or DRO?

The Participant is the person who has earned the pension.

5. Who is the "Alternate Payee" under a QDRO or DRO?

The Alternate Payee is the person that is being awarded a part of the pension. An Alternate Payee can be a spouse, former spouse, child or other dependent of the Participant.

6. Is a QDRO or DRO always an impartial document?

No. Depending upon who writes the order, certain provisions can be more beneficial to one party rather than the other. Therefore, it is important to address the important issues inherent in QDROs when negotiating property division. By knowing and agreeing on how certain issues will be addressed, the ability of the person drafting the order to make choices that benefit one party over the other is removed. The end product is a QDRO that does not contain any surprises.

7. Is it appropriate to use a "Model" QDRO provided by a plan administrator?

It depends. "Model" QDROs are often drafted to best benefit the employee. Therefore, caution should be exercised when using a model.

8. Why is the division of pensions such a complicated matter?

When dividing a pension using a QDRO, it is necessary to incorporate the applicable provisions of both state and federal laws which pertain to equitable distribution of pensions. Therefore, a comprehensive knowledge of both state and federal laws as they pertain to equitable distribution of retirement benefits is essential.

9. When should a QDRO be drafted?

Immediately. The process of obtaining the appropriate information and drafting of the QDRO should take place early in the divorce process, and occur at the same time the parties negotiate the other terms of their settlement. Since it sometimes takes several weeks to obtain the necessary information, it is important to begin this process early so that the provisions regarding the retirement benefits can be included in the agreement of the parties. The ideal situation would be to have the court certify the QDRO at the same time the decree of divorce is entered. If the divorce has already occurred, it is important to begin and complete this process as soon as possible.

10. Is it possible for an Alternate Payee to lose his/her rights to the pension?

Yes. If the participant dies before the QDRO is finished and approved by the Plan, the alternate payee runs a substantial risk of losing his/her interest in the pension.

11. Is it better to draft a QDRO or to take another asset as a trade?

This depends on the needs of the parties. What is important to one person is not always important to another. Before making this decision, the parties should consult with a financial expert.

QDRO FAQS FOR DEFINED BENEFIT PLANS

12. What is a Defined Benefit Plan?

A defined benefit plan is a pension plan which a pays a monthly benefit to the employee after retirement. The benefit is usually calculated using a formula which often employs his/her years of credited service and final average salary. This benefit is typically paid when the employee reaches his/her normal retirement age for the remainder of his/her lifetime.

13. Is it possible to receive a lump sum cash payment when drafting a QDRO against a defined benefit plan?

Typically, no. Most defined benefit plans will only pay both participants and alternate payees benefits on a monthly basis. However, the provisions of the plan itself should be examined before ruling out this possibility.

14. Can I get my benefits from a defined benefit plan right away?

Under a defined benefit plan, the benefit awarded to the alternate payee may begin, at his/her election, when the participant reaches his/her "earliest retirement age" under the Plan. This is the earliest point in time benefits may begin being paid to the alternate payee. In some cases, the QDRO could be drafted to only allow commencement of benefits to the alternate payee to begin when the participant actually retires.

15. Is it always necessary to elect post-retirement survivor benefits for an Alternate Payee?

No. Most plans will allow the use of a separate interest approach to dividing the benefits. Using this type of QDRO, the Alternate Payee's share of the benefits are actuarially adjusted and therefore, payable for the lifetime of the Alternate Payee. In such a case, the death of the Participant after benefits have commenced will not affect payment to the Alternate Payee.

16. If I am the participant and I remarry, how will the QDRO affect my new spouse?

If a separate interest approach is used in drafting your QDRO, you will be able to provide survivor benefits to your new spouse based upon the portion of the benefits that remained your property. Therefore, after your death, your spouse will still be able to receive a survivor benefit relative to the portion of your pension which was not awarded to your ex-spouse. If a shared interest approach is used to draft your

QDRO, it is possible to jeopardize your new spouse's survivor benefits. Therefore, by using the shared approach, you new spouse could receive nothing and your ex-spouse could receive everything after your death.

17. What is a Qualified Preretirement Survivor Annuity (QPSA)?

The Qualified Pre-retirement Survivor Annuity is a benefit that is paid to an employee's surviving spouse in the event of the employee's death prior to retirement.

18. Can an ex-spouse receive all or a portion of a Qualified Pre-retirement Survivor Annuity if the participant dies before retirement?

Yes. It is possible to include a provision in a QDRO that states that the ex-spouse is to be considered the "surviving spouse" for purposes of all or a portion of the Qualified Preretirement Survivor Annuity payable on behalf of the Participant in the event he/she should die prior to commencement of benefits. The ex-spouse can be the surviving spouse for all of this death benefit or for just the portion of the death benefit attributable to the portion of the pension awarded in the QDRO.

19. Can an ex-spouse receive both a part of the pension and a Qualified Preretirement Survivor Annuity?

Typically, no. Under most plans, the death of the employee before commencement of benefits would cause the pension to be forfeited, and the only benefit payable would be a qualified preretirement survivor annuity.

20. If an Alternate Payee is awarded part of the pension, but not the Qualified Preretirement Survivor Annuity, what happens if the Participant dies prior to retirement?

The Alternate Payee will probably get nothing from the Plan.

21. What are post retirement cost-of-living increases (COLAs)?

These are small incremental increases that keep retirees' benefits in line with inflation. A COLA is usually based upon the increase in the Consumer Price Index. Not all plans offer COLAs.

22. What is an early retirement subsidy?

Early retirement subsidies can come in a variety of different forms and are sometimes offered for different reasons. An early retirement subsidy can be a package deal to encourage early retirement in an effort by the company or union to downsize their workforce or can be a bonus for completion of a certain amount of years of service. Not all plans offer early retirement subsidies.

QDRO FAQS FOR DEFINED CONTRIBUTION PLANS

23. What is a Defined Contribution Plan?

A defined contribution plan is a pension plan which has an account specified for the individual employee. A defined amount is contributed to the plan by the individual, the employer or both. These plans are usually called 401(k) Plan, Savings Plan, Thrift Plan, etc. Funds can usually be transferred or withdrawn from the plan in a lump sum

24. Can I have the plan write a check directly to me for the amount that I have been awarded from my spouse's defined contribution plan?

Usually, not immediately. There are three options available when drafting a QDRO against a defined contribution plan. One option is to have the Plan Administrator establish a separate account within the Plan in the name of the Alternate Payee. The amounts awarded are deposited into this account and the Alternate Payee is given the same options as the participant has as a member of the plan with regard to investment choices, designation of beneficiary(ies), etc.

A second option is to provide, within the body of the QDRO, the name and other pertinent information relative to a tax qualified account (i.e. IRA, 401(k)) which is eligible to house the funds by way of a direct rollover. The plan will then transfer the money directly to this account.

The third option is to have the Plan issue a check (CASH) directly to the Alternate Payee for the sum awarded in the QDRO. This check will be issued after any mandatory waiting period required by the Plan and after the appropriate tax and distribution forms have been completed by the Alternate Payee and returned to the Plan Administrator.

25. What are the tax implications of taking an immediate cash distribution from a defined contribution account?

Usually, the Plan will withhold 20% of the amount requested for distribution for Federal income tax purposes. This is a withholding and should not be considered actual tax paid. At the end of the year, the Alternate Payee may receive a refund of part of this withholding or may be required to pay an additional sum depending upon the annual tax obligation of the Alternate Payee.

26. What about the interest and/or investment gains and losses that may happen from the time it is agreed that the account is to be divided until the Alternate Payee receives a distribution?

The QDRO can provide that the portion of the account awarded to the Alternate Payee be credited with any interest and/or investment gains (or losses) attributable thereon from the date the account is divided until the date the Alternate Payee receives a distribution.

QDRO FAQS FOR THE MILITARY RETIREMENT SYSTEM

27. Is it possible to write a QDRO against the Military Retirement System?

In general terms, yes, except it is not called a QDRO.

28. Is it true that the Member and Former Spouse must have been married for 10 years during which the Member was earning points towards retirement in order for the Former Spouse to receive court ordered benefits directly from the Military Retirement System?

Yes. In order for a former spouse to receive payments directly from the Defense Finance and Accounting Service (DFAS), the member and former spouse must have been married for 10 years during which the member was performing military service creditable towards his/her retirement. In other words, if the marriage did not last for 10 years which coincide with 10 years of military service on the part of the member, DFAS will not honor an order awarding benefits to the former spouse.

However, just because the 10 Year Rule is not met does not mean that a former spouse does not have a claim against retired pay. According to the laws of most states, retirement benefits accumulated during the period of marriage are deemed marital or community property. Therefore, it is possible for a former spouse to be awarded a portion of the member's retirement. However, the former spouse would have to receive his/her interest in the retirement benefits elsewhere (i.e. equity in the home, cash, payment made directly from the member, etc.).

29. Is it possible to use the number of points earned by the Member during the marriage to determine the portion of the military benefits earned during the marriage?

Yes. It is common for members of the reserves to use points rather than time to determine the amount of his/her benefits which accumulated during the period of

marriage. Since reservists earn a point for each day served, it is possible for someone to serve more days in one year than they do in another year. Since the number of points earned dictates the amount of the retirement benefit payable, it is not entirely accurate to assume that the same amount was earned towards retirement each year. Therefore, it is possible to write an Order which determines the marital portion by comparing the number of points earned during the marriage to the total number of points earned at retirement.

30. When can a former spouse receive benefits under the Military Retirement System?

The Military Retirement System will begin distributing benefits to the Former Spouse when the Member retires and begins receiving benefits.

31. Can the former spouse receive a lump sum payment from the Military?

No. Benefits are only paid on a monthly basis.

32. How long will payments be made to the former spouse from the Military Retirement System?

Benefits will paid by the Military to a former spouse for the lifetime of the member. Therefore, upon the member's death, all payments to the former spouse will stop. However, if the former spouse was awarded a survivor benefit plan annuity (SBP), then upon the death of the member, the survivor annuity will become payable to the former spouse.

33. Can a member have more than one person listed as the beneficiary for the survivor benefit plan annuity (SBP)?

No. Only one person can be designated as the beneficiary for the survivor benefit plan annuity. Therefore, only one person can receive the entire survivor benefit plan. It is not possible to designate a former spouse as beneficiary for part of the survivor annuity and a new spouse as beneficiary for the remainder of the survivor annuity.

34. Are there any forms which must be completed and sent to the DFAS with the Court Order?

Yes. Accompanying the Order should be a completed application form entitled "Request for Former Spouse Payments from Retired Pay" (DFAS Form 2293).

35. Are there any time restrictions relative to awarding benefits to a former spouse under the Military Retirement System?

There are no restrictions relative to the retirement benefit. However, there is a time restriction with respect to the survivor benefit plan annuity (SBP).

In order for the former spouse to remain eligible for survivor benefit plan coverage, the member must make an affirmative election for such coverage within 1 year of the date of the decree of divorce, dissolution or annulment. If the member neglects or refuses to make such affirmative election it is possible to protect the former

spouse entitlement to the SBP coverage by having the former spouse make a "deemed election" for such coverage within the one year time limit. Accordingly, the member shall be deemed to have made the necessary elections thereby preserving the former spouse entitlement to the SBP coverage.

QDRO FAQS FOR THE CIVIL SERVICE RETIREMENT SYSTEM (CSRS) AND FEDERAL EMPLOYEES RETIREMENT SYSTEM (FERS)

36. Is it possible to write a QDRO against the CSRS or FERS?

In general terms, yes, except it is not called a QDRO. The Office of Personnel Management uses the title "Court Order Acceptable for Processing" (COAP).

37. When can a former spouse receive benefits under the CSRS or FERS?

The CSRS and FERS will begin distributing benefits to the Former Spouse when the Employee retires and begins receiving benefits.

38. Can the former spouse receive a lump sum payment from the CSRS or FERS?

A Former Spouse may not receive a lump sum distribution of retirement benefits, but may receive a lump sum payment of any withdrawal of contributions elected by the Employee. The COAP has to clearly illustrate the payment of benefits when a withdrawal of contributions is requested by the Employee.

39. How long will payments be made to the former spouse from the OPM?

Benefits will paid by the OPM to a former spouse for the lifetime of the employee. Therefore, upon the employee's death, all payments to the former spouse will stop. However, if the former spouse was awarded a former spouse survivor annuity, then upon the death of the employee, the survivor annuity will become payable to the former spouse.

40. Can an employee have more than one person listed as the beneficiary for survivor annuities?

Yes. The employee may have a former spouse survivor annuity established for a former spouse and a survivor annuity in place for a current spouse. Under the CSRS the total of these survivor annuities cannot exceed 55% of the Employee's gross monthly retirement benefit, and under FERS cannot exceed 50% of the Employee's gross monthly retirement benefit.

STATE AND LOCAL GOVERNMENT FAQs

41. When can the Alternate Payee receive benefits from the Plan?

When the Participant actually retires and begins receiving benefits.

42. How long will the Alternate Payee be entitled to receive benefits from the Plan?

The Alternate Payee will receive benefits from the Plan for the lifetime of the Participant. In most circumstances, benefit payments will stop upon the death of the Participant.

43. Do all state and local government pension plans accept court orders awarding benefits to an Alternate Payee?

No. Before distribution of benefits using a court order is negotiated, it is important to determine that such method of distribution is permitted under the terms of the Plan.

44. Does an Alternate Payee have the same options under a pension plan administered by a state or local government as are available under a private company or union?

No. State and Local governmental pension plans do not fall under the guidelines of ERISA. Therefore, many of the options available to Alternate Payees under a company or union plan are not available under the government plan.

45. Can benefits be paid in the form of a lump sum benefit?

No, but with one exception. The portion of the Participant's monthly retirement allowance awarded to the Alternate Payee may not be paid in the form of a lump sum payment. However, if for some reason, the Participant makes a withdrawal of contributions and interest to the Plan, in some cases, the Alternate Payee may

receive a portion of those contributions and interest in the Plan paid in the form of a lump sum.

APPENDIX III

IMMEDIATE OFFSET V. DEFERRED DISTRIBUTION

IMMEDIATE OFFSET - PROS FOR THE PENSIONHOLDER

1. Control over all benefits earned when the pension matures.

2. Freedom to select from alternative benefit packages when pension matures.

3. Allows pensionholder to enjoy all benefits earned due to future increases in salary and continued years of service.

4. Allows pensionholder to take full advantage of future liberalized pension rules or conditions.

5. May simplify issues addressed in the divorce decree.

6. Avoids of joinder of pension.

7. May be more acceptable to employer, who will not have to enforce a court order.

8. Avoids potentially protracted litigation over future pension issues.

9. Gives pensionholder an increased ability to provide for a subsequent spouse and/or children.

DEFERRED DISTRIBUTION - PROS FOR THE PENSIONHOLDER

1. Pension may never mature, therefore, division of benefits is contingent upon maturity of benefits.

2. Avoids argument or discussion over assumptions and mechanics involved in present value analysis.

3. Avoids expense of a professional present value analysis.

4. Plan benefits may change and become less generous in the future.

5. Laws may become less liberal towards the nonowning spouse's interest in the plan.

6. Nonowning Spouse may die prior to commencement and never collect his/her share.

7. Pensionholder will not have to pay taxes on the amount of the benefits paid to the nonowning spouse.

8. May provide pensionholder with more liquid assets at the time of divorce.

IMMEDIATE OFFSET - PROS FOR THE NONOWNING SPOUSE

1. Avoids the possibility that the pension may never mature.
2. Provides nonowning spouse with more liquid assets at the time of divorce.
3. Plan benefits could become less generous in the future.
4. The law may become less liberal towards the interests of nonowning spouses.
5. Avoids possibility that the nonowning spouse could die and never receive any benefits under the pension.
6. Avoids joinder problems.
7. Avoids income tax liability to nonowning spouse on future payments.
8. Avoids potentially protracted litigation over future pension issues.
9. Avoids enforcement problems with the employer.

DEFERRED DISTRIBUTION - PROS FOR THE NONOWNING SPOUSE

1. May allow nonowning spouse to share in future salary and years of service earned by pensionholder.

2. Ability to have control over half of benefits when they reach maturity.

3. Avoids argument or discussion over assumptions and mechanics involved in present value analysis.

4. Avoids expense of a professional present value analysis.

5. May allow nonowning spouse to share in future liberalized pension rules.

6. Gives pensionholder an increased ability to provide for a subsequent spouse and/or children.

APPENDIX IV
PBGC ACTUARIAL AND MORTALITY TABLES METHOD
VS.
GATT METHOD

THE PBGC METHOD

The Pension Benefit Guaranty Corporation (PBGC) is a government agency which was established under the Employee Retirement Income Security Act (ERISA) of 1974 to oversee the financial stability of defined benefit pension plans by creating funding and reporting requirements. The PBGC derives their rates by surveying the interest rates used by annuity-writing insurance companies on a quarterly basis, and fine tunes them each month to reflect current rates used in the market. The PBGC Actuarial and Mortality Tables Method of valuation uses the interest rates prescribed by the PBGC and the Group Annuity Mortality Tables to chart mortality. The GAM Tables are updated mortality tables which reflect current actuarial practices in the insurance industry. By using the interest rates and mortality assumptions that are standard in the insurance industry, the PBGC Method of valuation measures the replacement value of any annuity in the insurance marketplace.

THE GATT METHOD

The GATT Method was established by the Retirement Protection Act of 1994 as part of the General Agreement on Tarrifs and Trade. This legislation set a new maximum interest rate for calculating lump sum payments under defined benefit plans that offer lump sum distributions to their participants. The maximum interest rate to be used for calculation of a lump sum distribution is the 30-Year Treasury Bond rate. Further the table used to chart mortality are the Group Annuity Mortality Tables (GAM) adjusted to be unisex.

The GATT Method used by Pension Appraisers, Inc. employs the 30-Year Treasury Bond rate and the gender specific Group Annuity Mortality Tables (GAM) not those designed to be unisex. We believe that using a unisex table will grossly undervalue those benefits earned by females and overvalue those of males. Therefore, in designing the GATT Method used by our analysts, we have incorporated the same gender specific tables as are used for the PBGC Method.

Since the GATT Method uses the interest rate that would be used by a plan administrator in paying a lump sum to a participant, this method more closely measures the actual lump sum that would be paid by the plan if a lump sum distribution was offered.

COMPARING THE RESULTS

The primary difference between the PBGC Method and the GATT Method, as set forth by Pension Appraisers, Inc., is the interest rate assumption employed. Interest rates and present value have an inverse relationship, therefore, a higher interest rate will result in a lower present value and vice-versa. Traditionally, the

30-Year Treasury Bond rate which is used in the GATT Method was consistently higher than the PBGC Rates. However, this is no longer a rule of thumb. Both the PBGC Rates and the 30-Year Treasury Bond Rate fluctuate on a monthly basis. It is possible for one rate to be higher in one month, and the other rate to be on top in the next month. Therefore, a standard has not been established for which method of valuation consistently produces a higher or lower present value.

Further, use of these different interest rates causes the present value calculations performed under each method to measure different things. As discussed earlier, a present value calculation performed using the PBGC Method measures the replacement value of an annuity in the insurance marketplace. A present value calculation using the GATT Method illustrates the actual lump sum that would be paid by the plan, if the plan offered a lump sum as a form of payment.

PBGC METHOD	**GATT METHOD**
*PBGC Interest Rates	*30-Year Treasury Bond Rate
*GAM Tables	*GAM Tables
*measures replacement value	*measures lump sum value

CONCLUSION

The difference in interest rates used in these two methods of valuation results in a difference in actual value measured, and the inverse relationship between interest rate and present value causes the discrepancy in the bottom line figure. In the past the PBGC Method has been the most widely recognized and accepted method of valuation in the country for establishing value for defined benefit plans in divorce.

However, new legislation brought change and the advent of a new method of determining the present value of defined benefit plans in the divorce arena. At the present time, we use the GATT Method of valuation as our default method in performing our valuations. In choosing the method of valuation to be used it should be kept in mind the preferred value to be measured; the replacement value of the annuity or the actual lump sum payable if such form of payment were an option.

APPENDIX V

SAMPLE AUTHORIZATION FORM

Dear Plan Administrator:

Consent is hereby given to you to provide

,

Esq. of the law firm of

Address:

(Phone: FAX:

)

with any and all information they may request or require concerning my retirement benefits, other employment benefits, and employment history (including dates of employment and salary history).

This authorization is strictly limited to my employment benefits and history, not to nonfinancial, nonbenefit personnel matters. In addition, this authorization will expire 365 days from the date of notarization. If not dated, this authorization will expire 365 days from your receipt of this request.

To facilitate handling this matter, I authorize you to reveal this information by phone, letter, or fax to my authorized agents. In addition, I ask that you honor faxed

transmissions of this authorization form or copies thereof, recognizing that the original will be forwarded, if
requested, for your records.

If there are any questions concerning this authorization, please contact me promptly at:

Signature: Date:

Name:
Print Name of Employee Social Security # of Employee

Phone: Fax:

Address:

PENSION QUESTIONNAIRE

(Duplicate this form for each Plan)

A. Plan Name:

B. Name of employer

C. Employer identification number for plan

D. Full name of plan. If other than above stated name.

E. Type of plan (defined benefit, defined contribution, etc.)

The following information should be determined

as of (mm/dd/yy)

(Attorney or Requestor: Enter cut-off date of marriage.)

FOR AN ERISA OR NON-ERISA DEFINED CONTRIBUTION PLAN

1. Total account balance

2. If this account balance is not as of the date listed above, list the account balance date.

3. Total employee contributions with interest

4. Total employer contributions with interest

5. Percent employee is vested in his/her own contributions

6. Percent employee is vested in employer contributions

7. If not 100% vested, the date vesting will begin assuming continuous service

8. Summary of the vesting schedule

9. Has participant taken any loans or made any withdrawals, excluding withdrawals on termination of employment that the participant has completely repaid under Internal Revenue Code Section 411(a)(7)(C)? Yes No

If yes, original amount ; date ; amount repaid ; amount currently owed ; current interest rate

10. Amount currently available for loan or withdrawal

11. Describe any prior qualified domestic relations orders affecting the participant's rights to benefits under this plan

12. IMMINENT PLAN ENHANCEMENTS: Please detail whether the participant will become entitled to any imminent plan enhancements, including, but not limited to, predetermined or pending contractual plan increases (e.g., union negotiations), upcoming early retirement window programs or buyout offers. (use separate sheet if necessary)

13. PLEASE ATTACH A COPY OF THE SUMMARY PLAN DESCRIPTION, which must be furnished on request to a plan participant as required by 29 U.S.C. Section 1024(b)(4) (ERISA § 104(b)(4).

14. MODEL QUALIFIED DOMESTIC RELATIONS ORDERS: Please send us any model QDROs that you may have developed or any written procedures for drafting QDROs in order to help us expedite the approval process.

FOR AN ERISA OR NON-ERISA DEFINED BENEFIT PLAN

1. Accrued monthly benefit based on salaries received and completed service to above date payable at the normal retirement age

Payable in the normal form of benefit of (e.g. single life annuity, 5 year certain, etc.)

How is this benefit calculated (i.e. detail the formula used to calculate the benefit)

List the data used to calculate the benefit (e.g. salary, years of service, pension credits, etc.)

2. The earliest date the employee is eligible to retire and receive any benefits is

Based on the accrued benefit shown above, what benefit amount would the employee be eligible to receive on this earliest date

3. How is the benefit on the earliest date calculated

4. What are the employee's total years of service as a plan participant and the exact dates of that participation.

List exact dates of any breaks in service

Has the employee purchased and received plan credit for any service prior to the date of hire. (e.g. military time). Yes No If yes, enter the amount of such service purchased

5. If not 100% vested, the date vesting will begin assuming continuous service

6. Summary of the vesting schedule

7. Has participant taken any loans or made any withdrawals, excluding withdrawals on termination of employment that the participant has completely repaid under Internal Revenue Code Section 411(a)(7)(C)? Yes No

If yes, original amount ; date ; amount repaid ; amount currently owed ; current interest rate

8. Amount currently available for loan or withdrawal

9. Normal retirement age

10. Early retirement age

11. Does the plan provide an early retirement subsidy? Yes No

If so, how is it calculated?

12. Does the plan provide post-retirement cost-of-living increases? Yes No

If so, how are they calculated, and when are they paid?

Are they compounding or non-compounding

13. Describe the forms of benefit payments that the plan provides and the procedure to elect benefits

14. Describe any reasons for which the plan would suspend benefits which are in pay status

15. Describe the available survivor benefits and election procedures:

16. Describe the current designated survivor beneficiaries with their full names and address(es):

17. Describe any prior qualified domestic relations orders affecting the participant's rights to benefits under this plan

18. If the parties divide rights to benefits in pay status, may the alternate payee elect a form of benefit payment different from that of the participant?

Yes No

If yes, state the election procedure

19. IMMINENT PLAN ENHANCEMENTS: Please detail whether the participant will become entitled to any imminent plan enhancements, including, but not limited to, predetermined or pending contractual plan increases (e.g., union negotiations), upcoming early retirement window programs or buyout offers. (use separate sheet if necessary)

20. PLEASE ATTACH A COPY OF THE SUMMARY PLAN DESCRIPTION, which must be furnished on request to a plan participant as required by 29 U.S.C. Section 1024(b)(4) (ERISA § 104(b)(4).

21. MODEL QUALIFIED DOMESTIC RELATIONS ORDERS: Please send us any model QDROs that you may have developed or any written procedures for drafting QDROs in order to help us expedite the approval process.

DATE COMPLETED:

BY:

TITLE:

GLOSSARY OF TERMS

Group Annuity Mortality Tables (GAM) - Probability tables used to measure the lifespan of the pensionholder during present value calculations.

Accrued Benefit - Benefit earned under a Defined Benefit Plan as of a specific date.

Actuarial - Calculation or analysis based upon expected lifespan of an individual.

Actuarial Adjustment - Used in Separate Interest QDROs to transform the amount awarded to the Alternate Payee to a benefit payable for his/her lifetime.

Alimony - Spousal support paid by one party to the other pursuant to the terms of the divorce.

All Property Model - All property owned by one or both parties on the date the marriage ended is subject to division in the divorce.

Alternate Payee - Term used in QDROs to distinguish the spouse who is awarded benefits under the Order.

Annuity - A payment made at specific intervals for a specified period of time. Example: Pension paid monthly for the life of the pensionholder.

Antialienation Provision - A clause contained in ERISA which prevents pension benefits from being assigned to another party, such as in bankruptcy or a creditor situation.

Asset - Another word for property.

Bankruptcy - A legal proceeding which can absolve a debtor of financial obligation.

Civil Service Retirement System (CSRS) - One of two defined benefit plans established for employees of the Federal Government.

Community Property - Another term that can be used to describe marital property. States which follow the guidelines for community property typically call for a 50/50 division of all marital property.

Contributory Plan - A pension plan in which contributions are made by both the employer and employee.

Cost-of-Living Adjustment (COLA) - A cost-of-living adjustment is a small incremental increase in retirement benefits, granted to retirees by a plan in an attempt to keep such benefits in line with inflation.

Court Order Acceptable for Processing - A court order directing payment of benefits to another person other than the employee under the Civil Service Retirement System or Federal Employees Retirement System. This is the title used instead of a QDRO.

Coverture Method - Method of valuing defined contribution plans.

Coverture Fraction - A tool used in valuing pensions to determine that portion of the benefits which were accumulated during the period of marriage.

(CPI) Consumer Price Index - A gauge used by the government to measure inflation.

Cut-Off Date - Another term for "Date of Classification" or "Date Marriage Ended." This is the date that marital property rights relative to the pension terminate. This date is usually dictated by case law in a particular state.

Date Marriage Ended - Another term for "Date of Classification" or "Cut-Off Date." This is the date that marital property rights relative to the pension terminate. This date is usually dictated by case law in a particular state.

Date of Classification - Another term for "Date Marriage Ended" or "Cut-Off Date." This is the date that marital property rights relative to the pension terminate. This date is usually dictated by case law in a particular state.

Defense Finance and Accounting Service (DFAS) - Benefits department of the military.

Deferred Compensation - Payment for service performed now, that is made at a date in the future.

Deferred Distribution Method - No immediate division of retirement benefits is made, instead, the Court determines the percentage or dollar share to be paid in the future when benefits are received by the employee.

Deferred Offset Award - Combination of the Immediate Offset Method and the Deferred Distribution Method.

Defined Benefit Plan - A pension plan in which the amount of benefits received by an employee is defined by a formula, usually considers years of service and salary.

Defined Contribution Plan - A pension plan in which the amount of benefits payable to an employee is determined by the amount contributed to the employee's account and any growth on such contributions.

Disability Benefit - A benefit paid to any employee due to a work-related injury.

Discount - The mathematical process which uses an interest rate to convert future payments to present worth.

Dual Property Model - Provides that only property which was accumulated by either party during the period of the marriage would constitute marital property subject to division.

Earliest Retirement Age - The age at which an employee may retire and begin receiving reduced benefits.

Early Retirement Subsidy - This is a bonus for retiring early. A subsidy may reflect additional years of service added to the pension or may provide for an early retirement due to satisfaction of a specific age and service requirement.

Early Withdrawal Penalty - Penalty assessed for plan distribution from a defined contribution plan which happens before the employee is eligible.

Employee Retirement Income Security Act of 1974, as amended (ERISA) - Federal statute established to protect the interests of employees who participate in employer sponsored pension plans.

Equitable Distribution - A term used to describe the process of dividing marital property. States which follow the guidelines of equitable distribution typically divide marital property in the manner deemed equitable based upon the circumstances of the parties.

ERISA-Qualified Plan - Any plan which falls under the guidelines, rules and regulations of ERISA.

Federal Employees Retirement System (FERS) - One of two defined benefit plans established for employees of the Federal Government.

Forfeiture Discount - A step in the valuation process of a defined benefit plan which adjusts the present value for the vesting status of the employee.

Future Benefit Plan - Any plan which provides benefits in the future as compensation for service performed at the present time.

GATT Method - As used by Pension Appraisers, Inc., it is a method of determining the present value of a defined benefit plan which employs Mortality Tables and the rate on the 30-Year Treasury bond.

Immediate Offset Method - The spouse is awarded cash or other property at the time of the divorce in lieu of a portion of the pension benefits as they are paid to the employee.

Individual Retirement Account (IRA) - An account established by an individual with a bank or other financial institution which is funded by the individual to save for retirement. IRAs are not employer related.

Informal Offset - The retirement benefits of the two parties are approximately equal, therefore, they are offset against each other.

Joint & Survivor Annuity - The pensionholder retires and receives less than the maximum monthly retirement benefit so that upon his/her death, a survivor annuity is paid to the designated survivor annuity for the remainder of that person's lifetime. This type of benefit option is often referred to as a Husband-and-Wife benefit and is typically payable under a defined benefit plan.

Liquidation - The process of cashing out a pension.

Marital Property - That property which is determined to have been accumulated during the marriage, and is therefore, divisible upon divorce.

Matured Plan - A plan which is presently providing benefits to the employee.

Mortality Discount - A modification to a present value figure to account for the chance that the pensionholder will die before receiving benefits.

Non-vested Benefit - A benefit which will not be paid by the plan unless the vesting requirements are met by the employee.

Noncontributory Plan - A benefit plan which is funded completely by contributions from the employer.

Normal Retirement Age - The age at which a pensionholder can retire and receive an unreduced benefit. This age is usually dictated by the terms of the Plan.

Office of Personnel Management (OPM) - The human resource department of the federal government.

Participant - Term used in QDROs to distinguish the spouse whose pension is being divided under the Order.

Passive Appreciation - An increase in the value of a defined contribution plan which is attributable to only investment experience, and does not include any contributions made to the account on the employee's behalf.

PBGC Actuarial and Mortality Table Method - As used by Pension Appraisers, Inc., it is a method of determining the present value of a defined benefit plan which employs Mortality Tables and the PBGC interest rates.

Pension Benefit Guaranty Corporation (PBGC) - A government agency which was established by ERISA to protect or guarantee a certain portion of a plan participant's benefits in case of voluntary or involuntary plan termination.

Pensionholder - The individual who has the pension plan. Also referred to as the employee or the Participant.

Present Value - Refers to the lump sum value of receiving a benefit at a specific point in the future for a specified period of time.

Property - Something that is certain and carries the characteristics of transferability.

Qualified Alternate Payee - Under ERISA, a "Qualified Alternate Payee" is a spouse, former spouse, child or other dependant of the Participant.

Qualified Domestic Relations Order (QDRO) - A written set of instructions which explains to the plan administrator that a portion of an employee's benefit is

subject to distribution due to a divorce. In order to qualify, it must be in the form of a court order and meet various other requirements.

Qualified Pre-Retirement Survivor Annuity - This is a benefit which is paid under a qualified plan to a beneficiary on behalf of the pensionholder/participant, in the event such pensionholder/participant should die prior to retirement. Often addressed in QDROs as a type of insurance for the alternate payee.

Reserved Jurisdiction Method - The Court decides the portion of the employed spouse's pension to be paid to the spouse at a later date.

Retirement Equity Act of 1984, as amended (REA) - Created a limited exception to the antialienation provisions of ERISA which provided for the creation of QDROs.

Segregation Method - A method of valuing defined contribution plans used by Pension Appraisers, Inc. which separates the pre-marital account balance and all growth on such account balance from the account balance on the date the marriage ended.

Separate Interest Approach - A way of drafting a QDRO against a defined benefit plan which establishes a "separate interest" for the Alternate Payee. This separate interest provides the Alternate Payee with the ability to choose a benefit commencement date, and to receive payment of benefits for his/her lifetime.

Separate Property - Property that is owned by only one party, and is not considered marital property subject to division.

Severance Package - Compensation given to an employee upon termination in an attempt to prevent financial hardship until other employment can be obtained.

Shared Interest Approach - A way of drafting a QDRO against a defined benefit plan which provides for the Alternate Payee and Participant to "share" the Participant's benefits. This shared approach provides the Alternate Payee with the right to commence benefits when the Participant actually retires and begins receiving benefits, and to receive payment for only the lifetime of the Participant.

Social Security Offset - A calculation that would be performed during a pension valuation if the pensionholder participates in a plan which does not allow for him/her to contribute towards social security.

Stock Options - The right given to an employee by a corporation to purchase a set number of shares of the corporation's stock during a specific period of time at a fixed purchase price.

Subtraction Method - A method of valuing defined contribution plans used by Pension Appraisers, Inc. which subtracts the account balance on the date of the marriage from the account balance on the date the marriage ended.

Survivor Annuitant - The designated person who will receive a survivor annuity upon the death of the employee.

Uniform Services Former Spouse Protection Act - This was effective on February 1, 1983, and established the former spouse's ability to receive a portion of the member's retired pay through a court order.

Unmatured Plan - A plan that has not begun paying benefits to an employee.

Unvested (Non-vested) Plan - A plan in which the employee would lose his/her rights to the benefits in the event of a termination of employment.

Valuation Date - The date which dictates the interest rate to be used in determining present value, thereby establishing value as of such date.

Vested Plan - A plan in which the employee would not lose his/her rights to the benefits in the event of a termination of employment.

Withdrawal Value - Similar to liquidation value or cash-out value.