PENSIONS IN NEVADA DIVORCE CASES

Marshal S. Willick, Esq.
330 South Third Street, Ste. 960
Las Vegas, NV 89101
(702) 384-3440

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[1] These materials are an update of materials developed for a seminar for the Nevada State Bar delivered at Tonopah, Nevada, in April, 1993.

I. IDENTIFICATION OF PENSION PLANS IN DIVORCE ACTIONS

A. Why Bother? Duty and Liability

1. Generally

Many practitioners fail to pay sufficient attention to pension and retirement plans when evaluating the community or other property available for distribution upon divorce. This is a mistake; more and more often, retirement benefits are the most valuable asset of marriages, often exceeding the value of all other assets combined, including the equity in the marital residences. For purposes of illustrating the impact of failing to allocate retirement benefits in divorces, a summary of the values involved in the first 14 "omitted military retirement" cases is set out as Exhibit 1. As shown by that Exhibit, the former spouses had missed out on average distributions (up to 1988) of some $200,000.00, and were *not* receiving any portion of the average $1,800.00 per month. The numbers for other types of retirement systems are often comparable.

Divorce lawyers are obliged to deal with these assets, and there is little excuse today for failing to do so. The landmark case recognizing the importance of pension benefits as community property was decided almost 20 years ago. *See In re Marriage of Fithian*, 517 P.2d 449 (Cal. 1974). That case was followed up shortly thereafter by an extension to unvested and unmatured pensions in *In re Marriage of Brown*, 544 P.2d 561 (Cal. 1976). Statutes and case law throughout the country now recognize that pension benefits are marital property. The rationales for that recognition vary, but usually include the fact of accrual during marriage, the necessary deferral during marriage of present enjoyment of income, or the possibility of alternative employment which would have paid more in current wages.

2. Nevada Practice

In Nevada, the duty to provide for disposition of pensions is clear. NRS 123.220 defines community property as "all property" acquired after marriage, with certain exceptions, and NRS 125.150 directs that the court *shall* make disposition of the community property of the parties. The first Nevada case explicitly noting that retirement benefits are divisible property was apparently *Ellett v. Ellett*, 94 Nev. 34, 573 P.2d 1179 (1978). There was no contrary law before *Ellett*; the case declared the law as it was, not as the court wished to change it. Accordingly, the law of Nevada has *always* been that pension benefits are divisible upon divorce. *See also Walsh v. Walsh*, 103 Nev. 287, 738 P.2d 117 (1987) (retirement benefits earned during marriage are community property).

As a practical matter, it may be necessary to deal with pensions during the divorce itself, instead of deferring the matter to be dealt with "later." Nevada, alone among the community property states, does not clearly permit a spouse who does *not* receive a portion of pension benefits to bring a partition action at a later date to divide those benefits. *See Taylor v. Taylor*, 105 Nev. 384, 775 P.2d 703 (1989) ("we do not recognize a common law cause of action to partition retirement benefits not distributed as part of the property agreement at the time of divorce"); *Tomlinson v. Tomlinson*, 102 Nev. 652, 729 P.2d 1363 (1986).

A very old line of authority, however, permits post-divorce partition of omitted assets. *See Bank v. Wolff*, 66 Nev. 51, 202 P.2d 878 (1949). Recently, that case was re-affirmed and the *Taylor* line of authority was put into significant doubt. *See Amie v. Amie*, 106 Nev. 541, 796 P.2d 233 (1990) (omitted wages divisible by partition action where mistake, not fraud, caused absence of asset from decree; "After the divorce, the parties to the divorce suit become tenants in common in the omitted property"); *see also Williams v. Waldman*, 108 Nev. ___, ___ P.2d ___ (Adv. Opn. No. 81,

July 13, 1992) (separate suit to set aside property terms of divorce for omitted asset (ownership share of law firm) upheld).

Additionally, the Nevada Supreme Court has even more recently approved the use of a separate suit in rescission as a means of rectifying property inequities in the original divorce judgment. *See Blanchard v. Blanchard*, 108 Nev. ___, ___ P.2d ___ (Adv. Opn. No. 140, Oct. 23, 1992) (complaint after divorce, seeking rescission based upon intentional misrepresentation, approved; district court's dismissal under NRCP 12(b)(5) reversed).

Since the *Taylor\Tomlinson* line of authority cannot be reconciled with the much earlier cases, or with the very recent cases, the practitioner should exercise extreme caution at the time of the original divorce, and should be prepared to defend the decisions made if questioned by a disenchanted client. *See* Willick, *Partition of Omitted Assets After Amie: Nevada Comes (Almost) Full Circle*, 7 Nev. Fam. L. Rep., Spr. 1992, at 8.

3. **The Specter of Malpractice**

Because our law may well not provide a mechanism for correcting the omission of such assets from the decree, a shortchanged spouse is sometimes left with only a malpractice suit against her[2] attorney as a possible mechanism for recovery. The shaky state of the law governing partition of omitted assets therefore makes it imperative for counsel to seek out pension benefits during the pendency of a divorce as a matter of defensive practice. (The appalling public policy of encouraging spouses to defraud one another by deliberate omission of assets from decrees is explored elsewhere. *See* Willick, *Res Judicata in Nevada Divorce Law: An Invitation to Fraud*, 4 Nev. Fam. L. Rep., Spr. 1989, at 1.)

Awards against attorneys in these cases can be significant. From the landmark case of *Aloy v. Mash*, 696 P.2d 656 (Cal. 1985) to the fairly recent case of *Bross v. Denny*, 791 S.W.2d 416 (Mo. Ct. App. 1990) ($108,000.00 malpractice award against trial attorney for not knowing that he could seek division of military retirement after change in the law), it has been made clear that any attorney practicing divorce law is charged with knowing about the existence, value, and methodology of division of any retirement benefits that might exist. The potential liability is the value of the foregone benefit to the defrauded spouse. *See also Carlson v. Carlson*, 108 Nev. 358, 832 P.2d 380 (1992) (in NRCP 60(b) case, Supreme Court noted that "Arguably, Trudy's counsel should have more diligently pursued information about the pension or, at least, moved for a continuance until she determined the actual value of the pension").

It is a sad reality that many non-wage earner spouses have no idea what forms of deferred compensation are associated with their spouses' employment. Since Nevada law apparently places the burden of bringing such items before the court on the party seeking to divide it,[3] counsel must

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[2] While, theoretically, either spouse could perpetrate this form of fraud by omission upon the other, all known cases to date have involved wives seeking portions of property held by husbands. Presumably, this is a result of the fact that, historically, more husbands than wives have had careers giving rise to the creation of such deferred compensation interests.

[3] This may finally be changing. In Washoe County, the new Family Court rules mandate a financial disclosure statement with each initial filing. *See* WDCR 40. A judges' committee in Clark County rejected a similar requirement suggested by a committee of the State Bar Family Law Section in 1991, but the new Family Court has not yet issued its new proposed rules.

take care to actively seek out these assets. One recent attorney malpractice case in Nevada was predicated on the attorney's imputed knowledge of the pension: the attorney was put on notice that a pension fund existed by the fact that the parties had a *checking account* administered by the employee spouse's union.

Publications of the Law Practice Management Section of the American Bar Association have predicted that family law malpractice will be a "growth field" for the 1990s. It would seem that an increasing degree of attention to ferreting out possible concealed assets, including retirement benefits, is not only advisable, but necessary.

B. **Means of Acquiring Information**

1. **The Client Interview**

The easiest means of starting the search for pension benefits is asking for the full employment history of both spouses during the initial client interview. Further investigation is warranted if either party has apparently worked for the United States government (i.e., the Civil Service, including the Post Office), the United States Armed Forces (including the Reserves or National Guard), a state or local government, a corporation of any appreciable size, an employer that reasonably should have used union labor, or a professional corporation.

2. **Informal and Formal Discovery**

Most private pension plan administrators will gladly provide a copy of all plans offered by the employer, and summaries of those plans, upon a telephone or written request. Information about a specific employee, however, will usually not be released without a release from that person, or under subpoena. A sample information request form is attached as Exhibit 2.

The United States Civil Service also generally requires a release form. In military cases, the pay centers should release, upon request, past and current gross pay, including gross military retirement benefits to date. *See* 32 C.F.R. § 505, 50 Fed. Reg. 42163-01(c)(1). Recent internal "reconsiderations" of the law have made obtaining such information a hit-or-miss proposition, however, and sometimes a release or subpoena is necessary. A sample military request form is attached at Exhibit 3. Those dealing with the military should note that they will not respond to a subpoena issued by the Clerk's office, but will probably require a judge's signature.

Once litigation has begun, all public and private pension plans will apparently send information concerning the plan participant in response to a subpoena. Note that private pension plan information requests should be directed to plan administrators (not just employers), and that military information requests must be directed to the proper branch of service.

It is a good practice to request all materials relating to pension or retirement benefits (and, perhaps, a release form to obtain back-up and supplemental documentation) at the joint case conference. Later, interrogatories or requests to produce can be sent for updated information. Recent cases indicate that this is another area where failing to affirmatively seek out information could lead to liability on the part of the lawyer.[4]

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[4] *See* T. Harrison, "IRS Grabs Ex-Wife's Pension Share; Malpractice `Warning Bell' for Divorce Lawyers," Lawyers Weekly USA, Sept. 27, 1993, at 1.

C. **Knowing It When You See It**

1. **The Basics to Watch For**

In dealing with any retirement program, the practitioner should pay attention to the following essential elements:

a. The *amount* to be available (and the form -- whether a monthly annuity, or with a lump sum option), and whether there might be more than one plan connected with a particular wage-earner;
b. *When* that sum is to be *first available* for distribution, and what steps might be taken by either party to accelerate or delay that availability;
c. What, if any, *survivor benefits* might be accorded to the former spouse in addition to or in place of the retirement benefits (note that Joint & Survivor Annuity is now the standard default of most plans);
d. Whether any ancillary benefits are available (medical, etc.; *always* try to find out cost of COBRA benefits);
e. *Effect* on wage-earner spouse of award of benefits to the non-earning spouse (i.e., whether the former spouse's benefits reduce those payable to the retiree;
f. What *notices* are required to be given, within what time limits, to which authorities, in order to make sums payable to the spouse or permit the transfer of other interests;
g. What effect a present or future *disability* claim by the retiree or the former spouse could have on payment of benefits (and what, if anything, you can do about it in advance);
h. Whether and *what* post-divorce actions of either of the parties (such as nomination of the wage-earner of a second spouse as beneficiary, or remarriage of the former spouse) could affect the property distribution.

Failure to deal with all of these factors in litigation or negotiations could lead to unforeseen, and unfortunate, results for at least one of the parties, and/or counsel.

The practitioner should distinguish benefits from values, and both terms from "contributions." The value of a pension interest is generally considered to be equal to the cost, at any given time, of acquiring an annuity that would pay equivalent benefits. Benefits, on the other hand, are what the retiree will actually receive upon retirement,[5] usually phrased as a right to receive certain sums on a certain schedule. Contributions, whether from the employee, the employer, or both, do not necessarily have any correspondence to the *benefits* of a plan, or its *value* at any given time. Failure to perceive these distinctions can lead to gross over- or under-valuation of the assets at issue.

It is important to note that pension interests are property and not alimony. The Nevada Supreme Court has expressed its intention to stress the distinction based upon the non-modifiability of pension awards, whereas alimony is generally modifiable. *See Carrell v. Carrell*, 108 Nev. ___,

[5] Except in certain contexts (see discussion below of peculiarities of new Civil Service definitional scheme), "retirement" means that an employee has stopped working *and* that retirement benefits are payable to that individual. Given the many ways in which an employee may stop working prior to eligibility for retirement benefit payments, care must be taken in definitions when engaging actuaries or accountants, or negotiating these cases.

___ P.2d ___ (Adv. Opn. No. 116, Sept. 1, 1992) (award to wife of specified sum as "spousal support" instead of property reversed). *See also Walsh, supra*.

The logic of the court's holding in *Carrell* is open to some question, since the court in other contexts has had no trouble with the proposition of awarding alimony in compensation for, among other things, a superior property position of the paying spouse. *See Heim v. Heim*, 104 Nev. 605, 763 P.2d 678 (1988) (husband, whose future earning capacity was a community asset that could have been made the subject of trial proceedings, ordered to make permanent alimony payments).

While *Carrell* makes it appear that the divorce court cannot convert pension interests to another form during disposition of the case, there is little Nevada authority on the question of recharacterization of a pension interest to another form by the *wage-earner*. In *Powers v. Powers*, 105 Nev. 514, 779 P.2d 91 (1989), a three-to-one majority of the Nevada Supreme Court sided with California authorities in acknowledging that a "disability pension" generally has two components, retirement and disability. While the latter is sole and separate, the retirement component of a disability pension is divisible community property. *Powers* is remarkable because the disabled worker had not yet qualified for payment of *any* regular retirement benefits when he was retired for disability. It thus seems that *any* disability award stemming from employment has *some* retirement component that can be traced out and counted as community property in this state.

Cases from other jurisdictions are divided as to whether severance pay received in lieu of retirement benefits is divisible in place of the pension. *See*, *e.g.*, *Lawson v. Lawson*, 208 Cal. App. 3d 406, 256 Cal. Rep. 283 (1989) (listing factors for evaluating severance pay to see if it is marital or non-marital property).

There does not appear to be a published Nevada opinion on the precise question, but the Nevada Supreme Court dropped a hint in an unpublished order[6] in 1989. In *Banta v. Banta*, No. 19756 (Order Dismissing Appeal, Mar. 9, 1989), the court upheld the Referee's determination that severance benefits received by a fired worker constituted receipt of "pension benefits" sufficient to require payment to the former spouse, who was to get her share of benefits when the worker received them. *Banta* provides an indication that transmutation of pension benefits, even when involuntary, will not defeat the interest of the non-earning spouse.

This line of reasoning is consistent with the *Gemma*, *infra*, line of authority, but will eventually have to be reconciled with a worker's "freedom to agree to terms of retirement benefits" under *O'Hara*, *infra*.

2. **Vestedness and Maturity; Nevada Red Herrings**

A "vested" pension is one in which the employee has met certain conditions (usually, length of service) which stop an employer from arbitrarily preventing the employee's enjoyment of benefits. A "matured" pension is one in which a particular employee is eligible for present payments from a plan. In some jurisdictions (the number of which continues to decline), lack of vestedness or maturity causes pensions to be considered "mere expectancies" or otherwise non-divisible. It is therefore most important to consider these factors when involved in multi-jurisdictional cases.

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[6] Unpublished orders of the Nevada Supreme Court "shall not be regarded as precedent and shall not be cited as legal authority" except in certain narrow circumstances. *See* SCR 123. Like IRS "Private Letter Rulings," however, they often indicate the thinking on a subject that could manifest itself in later formal proceedings.

Nevada is in line with the apparent majority and clear trend in this area. The Nevada Supreme Court has explicitly stated that retirement benefits are generally divisible as community property "to the extent that they are based on services performed during the marriage, whether or not the benefits are presently payable." *See Forrest v. Forrest*, 99 Nev. 602, 668 P.2d 275 (1983). These concepts do, however, have an impact on valuation of pension benefits, which is discussed below.

The Nevada Supreme Court has confirmed that a spouse is entitled to begin receiving her share of a pension upon her husband's *eligibility* to begin receiving payments (i.e., upon its maturity), so that the wage-earner's unilateral actions could not deprive her of sums that she was otherwise eligible to receive. *See Gemma v. Gemma,* 105 Nev. 458, 778 P.2d 429 (1989); *Fondi v. Fondi*, 106 Nev. 856, 802 P.2d 1264 (1990).

It had appeared from language in *Gemma* that Nevada was simply adopting the law of California as set out in *In re Marriage of Gillmore*, 629 P.2d 1 (Cal. 1981), and *In re Marriage of Luciano*, 164 Cal. Rptr. 93 (Ct. App. 1980). Those cases made it clear that in California a spouse has to make an "irrevocable election" at the time of divorce as to whether begin receiving the spousal share of the retirement benefits upon maturity, or to wait until the wage-earner actually retires, thus enjoying a "smaller piece of a larger pie" by getting a shrinking percentage of a retirement based upon post-divorce increases in the wage-earner's salary and years in service.

Specifically, the court adopted and quoted the core holding of the California courts:

> The employee spouse cannot by election defeat the nonemployee spouse's interest in the community property by relying on a condition within the employee spouse's control.

Gemma, supra, 105 Nev. at 463-64, *quoting Luciano, supra*, 164 Cal. Rptr. at 95.

Fondi, however, contains language going further and indicating that our court is *mandating* application of the spousal share against the retirement benefits *ultimately received* by the wage-earner (deemed the "wait-and-see" approach). Of course, it is not possible to actually calculate this sum before the amount of benefits is known (i.e., at the time of retirement). The court *also* reiterated its position that the spousal share is distributable upon maturity.

3. **Unresolved Questions Under *Gemma* and *Fondi***

It is not possible to both distribute a spousal share of a retirement upon eligibility despite the wage-earner's continued employment, *and* to base the spousal share paid on the amount that the wage-earner ultimately receives. This leaves the trial courts with no practical means of accomplishing these conflicting directives except to have the parties return to court periodically to adjust the distributable spousal share, which would work a hardship on the parties and the court. Of course, it is possible that the court will reconcile these contradictory directives in later cases. For the moment, the problem defies logic.

There is also the question of what is meant by "first eligibility." Under the Nevada PERS plan (explained *infra*), for example, an employee can choose to take early retirement almost any time after vesting, paying a 4% penalty for each year before regular retirement age that the benefits are accepted. *See* NRS 286.510. It could be argued that this makes every vested PERS participant "eligible" for retirement benefits, and thus every former spouse eligible for immediate payments (at a sum taking into effect the penalty, of course). There have been no further appellate decisions in this area, but certain trial court opinions indicate that the cases will be interpreted as referring to the

earliest date of *regular* retirement under the plan (i.e., the time at which an employee can retire without penalty).

Gemma and *Fondi* are landmark cases, but it is difficult to reconcile them with the 1988 holding in *O'Hara v. State ex rel. Pub. Emp. Ret. Bd.*, 104 Nev. 642, 764 P.2d 489 (1988). In *O'Hara*, the employee spouse had chosen the maximum monthly annuity, which provided no survivor's benefits.[7] She died shortly after retirement. Finding that the "community property interests of a nonemployee spouse do not limit the employee's freedom to agree to terms of retirement benefits," the court ruled that the employee may choose any available options so long as "the community property interest of the nonemployee spouse is not defeated."

It is easy to construct a hypothetical collision between these two lines of cases. One reason for the likelihood of conflict is the variety of options are available to a retiring PERS participant. *See* Exhibit 4 (PERS retirement options selection form). Suppose an employee divorces before retiring, and the former spouse is awarded "50%" of the benefits paid upon eligibility for retirement. *O'Hara* indicates that, upon retirement, the employee can choose any available option. If the employee chooses option 2 rather than option 1, however, nominating as the survivor a second spouse, the amount of benefits that the first former spouse gets "50%" of will be greatly reduced. Additionally, if the survivor beneficiary is anyone other than the former spouse, that election could greatly reduce the value of the former spouse's interest (depending upon who lives longest).

It is clear that there are a great many options and elections that an employee can make that would "by election defeat the nonemployee spouse's interest in the community property by relying on a condition within the employee spouse's control." The question is whether the courts will enforce the goal of *Gemma* and *Fondi* by prohibiting employee elections that devalue spousal interests. Until and unless the courts specifically permit post-divorce motions regarding elections that an employee might take which could have such an adverse impact on the nonemployee spouse, counsel for non-employee spouses must specifically anticipate and deal with such possibilities in original divorce decrees.

It appears that at least one more case will be needed for guidance in reconciling the conflicts between an employee spouse's right to choose plan options and the substantive right to collection by non-employee spouses. In the meantime, counsel for such spouses must try to be both prescient and omniscient when it comes to possible elections under plans at issue upon divorce.

4. **Place of accrual**

A significant gap has arisen between Nevada law as declared and as applied. Nevada may be the last community property state without some type of quasi-community property statute.[8] Theoretically, Nevada still follows the "pure borrowed law" approach, whereby our court determines the divisibility of assets according to the law of the state in which those assets accrued. *See Braddock v. Braddock*, 91 Nev. 735, 542 P.2d 1060 (1975).

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[7] PERS did *not* mandate either a joint and survivor annuity *or* have any provision for spousal consent to another form of benefit, before the changes to its statutory framework in 1987. *See* NRS 286.541, 286.545.

[8] Such laws provide that property acquired outside the state is deemed to be community property if it would have been community property if acquired within the state.

It would appear that the parties are burdened with apportioning retirement benefits according to the law of each jurisdiction in which the parties lived (or were residents) while the benefits accrued. Naturally, that can be difficult undertaking.

For example, suppose a case involved a military family. The military lifestyle makes regular moves from jurisdiction to jurisdiction a way of life. If the parties had lived in Mississippi for several years, then moved to California, and then to Nevada, where they divorced, the tracing and apportionment problem could be quite daunting. Until very recently, Mississippi was the single remaining adherent to the "title" form of property ownership. California has a strict equal division statute. Presumably, the Nevada divorce court would have had to award the entire pension accrued while in Mississippi to the service member, would have been required to *equally* divide that portion accumulating in California, and (until October, 1993, when the changes to NRS 125.150 created a presumption of equal division Nevada law), would have then had to *equitably* divide the remainder.

Our courts, however, often resort to a quasi-community property approach without explicitly acknowledging that they are doing so. In *Heim v. Heim*, 104 Nev. 605, 763 P.2d 678 (1988), the Nevada Supreme Court simply noted without comment the equal division of a Michigan state retirement fund in a Nevada divorce court. *Id*. at n.1. The court will not allow the law of the state where the benefits accrued to be raised as an issue on appeal if not argued by a party at trial. *See Powers v. Powers*, *supra*. The unstated policy of adopting a quasi-community property approach in pension cases at the trial level appears to be nearly universal, at least in southern Nevada.[9]

It is possible that substantive law could encourage this approach for certain kinds of pensions. The federal statute governing division of military retirement benefits, for example, indicates that the court with appropriate jurisdiction should treat the retirement "in accordance with the law of the jurisdiction of such court." *See* 10 U.S.C. § 1408(c)(1). Of course, it could also be argued that the reference to the law of this jurisdiction is not to our substantive law of property division, but to the procedural law of how to accomplish such a division, including the *Braddock* rule.

There does not appear to be a Nevada case considering the divisibility of an unvested (or unmatured) pension that was largely accrued in a state where those factors are still relevant. In theory, at least, the bulk of such benefits would apparently not be divisible here.

For now, attorneys representing non-earning spouses are probably best served by simply applying Nevada law, despite the mandate of *Braddock*, unless opposing counsel or the court requires an analysis of out-of-state law. Attorneys for wage-earners would appear to have a significant malpractice risk if they do not check on the possibility that a portion of the retirement benefits accrued elsewhere are non-divisible under the law of that state, although it is uncertain whether our trial courts would entertain the analysis even if put forward by counsel.

Prospects for change are uncertain; the 1989 Assembly Judiciary Committee had a proposal before it to adopt a quasi-community property provision (among other changes), but allowed it to die in committee without ever considering it. Since that time, similar proposals have been discussed, but no specific enactment has surfaced.

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[9] Only one statutory area seems to anticipate a quasi-community property approach, and that is somewhat oblique. NRS 125.420 provides that the law of any other state, if implicated in a Nevada annulment, is presumed to be the same as Nevada law "unless and until" proven otherwise. Coupled with the court's power to divide property as if it was community property between unmarried cohabitants, this appears to give the court a "soft" power of quasi-community property in annulment cases. *See Michoff v. Michoff*, 108 Nev. ___, ___ P.2d ___ (Adv. Opn. No. 144, Nov. 5, 1992).

5. **Forms of Private Pensions**

Many attorneys find the various forms of benefits available from private employers to be confusing. Generally, private plans come in two varieties -- defined benefit plans and defined contribution plans. The differences are most important for valuation, which is discussed separately below.

Private pensions, after the Retirement Equity Act (REA) and Employee Retirement Income Security Act (ERISA), must be divided by means of a Qualified Domestic Relations Order (QDRO). *Any* judgment, decree, or order dealing with alimony or support for a spouse, former spouse, child, or other dependent made according to local domestic relations law is a "domestic relations order" under federal law. *See* 29 U.S.C. § 414(p)(1)(B). It becomes a "qualified" order, or QDRO, when it creates or recognizes one of the listed classes of persons as an "Alternate Payee" with a right to receive all or any portion of the benefits normally payable to a participant in a pension plan that is a "qualified plan."

An order is *not* "qualified" if it requires a plan to provide a type or form of benefit not otherwise available under the plan, or requires the plan to provide a greater (actuarially computed) sum of benefits, or requires payment of benefits to an Alternate Payee that are required to be paid to *another* Alternate Payee under a prior QDRO. *See* 29 U.S.C. § 414(p)(3), 29 U.S.C. § 1056(d)(3)(D). QDROs need not necessarily be long or complex; the question is what you are trying to accomplish, and what safeguards are reasonably necessary given the parties, the background factual situation, the kind of plan involved, and the desired distributions.

a. **Defined Benefit Plans**

A defined *benefit* plan (often called a pension plan) is usually funded by employer contributions (although in some plans employees can contribute) and is intended to provide certain specified benefits to the employee after retirement, usually for life. Often, the benefit is determined by a formula taking into account the highest salary received and the total number of years worked for the employer (such as a "high-three" or "high five" plan).

For example, a plan might pay one-tenth of an employee's average monthly salary over the three years before retirement, multiplied by one-fourth the number of years that the employee worked. A twenty-year employee earning an average of $2,000.00 per month during his last years would get $1,000.00 per month (i.e., $2,000.00 x .1 x 20 x .25).

Generally, no lump-sum distributions (other than certain nominal amounts in some plans) can be distributed from defined benefit plans. The IRS apparently considers $3,500.00 the measure of "nominal" for this purpose.

b. **Defined Contribution Plans**

A defined *contribution* plan (often called a profit sharing plan) is one in which the employee has an individual account made up of contributions made by the employee (and, if any, by the employer), plus investment gains. Employers are not required by law to contribute, although many such plans contractually bind the employer to add some formula percentage of the amount the employee puts into the plan. *See* 29 U.S.C. § 1002(34).

These plans come in many varieties, including profit-sharing plans (employer contributions vary according to company performance), stock bonus plans (the plan invests in the securities of the

company itself), "401k" plans (employee chooses either taxable salary or nontaxable contribution to plan), and money purchase plans (like profit-sharing, but with a fixed employer contribution). The key concept for such plans is that they have a specific balance of funds belonging to each particular employee.

c. **Individual and Self-employed Plans**

Individual Retirement Accounts ("IRAs"), and "Keogh" plans are private retirement plans that do not really fit in with the above two varieties. Keoghs are essentially like the above plans but for sole proprietors, partnerships, or "S" corporations. Note that an IRA can be divided in a divorce action without incurring any tax penalties (but see section below on tax considerations).

6. **Forms of Civil Service Benefits**

There is an "old" system (Civil Service Retirement System, or CSRS, for those who began service before January 1, 1984) and the "new" system (Federal Employees' Retirement System, or FERS, for those who began service on or after January 1, 1984). *See* 5 U.S.C. §§ 8331, 8401.

Under both systems, federal statutes permit the division and direct payment to the former spouse of *all* or a portion of a retiree's benefits in conformity with a state court's decree or approved property settlement agreement. Voluntary allotments may also be put in place by the retiree. There is no minimum age for the former spouse, but the marriage must have lasted at least nine months. The former spouse's payments end when the retiree dies.

There is also a "Thrift Savings Plan" created by the FERS statute (but also available to CSRS participants). It is payable in a number of ways, but requires spousal consent if taken in any form other than a joint and survivor annuity. Loans can be taken out by the retiree against the Plan account, unless the court order prohibits it.[10]

Things to watch out for in Civil Service cases include the survivor annuity election (automatic for current spouses at retirement unless both spouses "opt out"), the possibility of lump-sum withdrawals from the system, rules terminating survivor annuity payments upon a spouse's remarriage before age 55, and rules prohibiting enforcement of certain post-divorce orders modifying the terms of the original order, if made after retirement or death of the employee.

An argument that can be (but is not often) made in cases involving CSRS participants is an argument by the employee to not consider part of the retirement, since such participants are not covered by Social Security (as opposed to FERS participants, who are). The argument is that Social Security is exempt from state court distribution, and this retirement plan was deliberately set up *outside* of the Social Security system by the federal government, so courts should subtract from the pension before the court some portion of value assigned to represent the value of the Social Security benefits built in by Congress. A significant amount of projection and guesswork is necessary to

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[10] Note that the Thrift Savings Plan is *not* addressed in the clause set provided by Office of Personnel Management (and attached in the Exhibits to these materials). The practitioner must find out whether a Civil Service employee is or has been a participant in the Thrift Savings Plan, and if so whether any funds have been withdrawn or borrowed from the plan. Those wishing further information on the Thrift Savings Plan can call the administering agency (Federal Retirement Thrift Investment Board) in Washington, D.C., at (202) 942-1600.

compute the value of the non-contributions, but it can be done. *See* M. Snyder, The Value of Pensions in Divorce: What It Is and How to Use It, *infra*, 1993 Supp. at 22-24.

7. **Forms of Military Benefits**

Former spouses have no statutory entitlement to a portion of military retirement benefits, but federal law requires the military pay centers to comply with certain state court orders. *See* 10 U.S.C. § 1408 (the Uniformed Services Former Spouses Protection Act, or "USFSPA"); 32 C.F.R. § 63 (implementing regulations).

a. **Retirement Benefits**

Essentially, federal law assists in collection of up to fifty percent of disposable retired pay payable to a retired military service member (65% when certain arrears are being garnished in addition to present payments). Military retirement benefits can be treated as property to be divided between the parties, or as a source of payment of child or spousal support, or both.

Property divisions may be made by percentage or dollar sum, and it is possible (with most service branches) to provide for cost-of-living adjustments (COLAs) either way.[11] Note that it is critical to explicitly provide for COLAs if a dollar sum is used, as inflation will otherwise greatly reduce the intended award over time. More than fifty percent of disposable pay may be paid (up to 65% of "remuneration for employment" under the Social Security law, 42 U.S.C. § 659) if there is a garnishment for arrears in child or spousal support, or in payments of money as property *other than* for a division of retired pay. In other words, and counter-intuitively, about the only part of a divorce judgment that cannot be satisfied by garnishment from retired pay is arrearages in retired pay.

Practitioners should note recent changes. As of February 4, 1991, parts of the USFSPA were amended. The definition of "disposable pay" was altered to eliminate the deduction of income taxes from gross retired pay in figuring the sum which may be divided between the spouses. The changes *only* affect divorces which are final on or after February 4. All prior cases continue to be governed by the older rules (i.e., the sum payable under divisions of disposable pay as previously defined stay in effect). This is discussed in greater detail *infra* in the income tax section of these materials, on page 41. Certain other changes were also put into place, among them a prohibition on partition actions (for omitted pensions) if the underlying divorce decree was dated prior to June 25, 1981, and did not divide the pension or reserve jurisdiction to do so.

The so-called "ten year" limitation is much misunderstood. To qualify for *direct payment* from the military pay center, the spouse must have been married to the service member at least ten years during active duty. If the marriage overlapped service by less than that, the right still exists, but the spouse will have to obtain payment from the retired member. There is no presumptive share, and no limit (other than the fifty percent cap) on the court's division of the asset.

It is important for the spouse to begin receiving payments as soon as possible once the right to do so accrues. Military retirement is not like a defined contribution plan with a specific balance. Rather, it is a like a defined benefit plan in that it provides a stream of payments that can be tapped for a present spousal share, but which has no mechanism for collecting property payments once they

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[11] This matter is in a state of flux at the moment. The pay centers are consolidating, and many policies on which the various pay centers disagreed over the years are being re-examined in the process. It is impossible to say which views will ultimately prevail.

are missed. In other words, arrears in military retirement benefits payments must be collected from the member directly; the military will not garnish for such arrearages.

If there is any chance that the member might have a disability at the time of retirement, or divorce, or later, much care must be taken to provide for the situation. Under present law, such disability benefits are not divisible community property. *See Mansell v. Mansell*, 490 U.S. 581, 109 S. Ct. 2023 (1989). While *Mansell* has made it clear that the "disposable" limitation is upon substantive state court jurisdiction, it remains unclear what scope there may be to state court recognition of disparate allocation to spouses of amounts that *would have been* divided between them but for the recharacterization of retirement benefits as disability benefits. *See Powers v. Powers*, *supra*. This is explored in greater detail in the "special problems" section of these materials, on page 24. Courts are apparently free to take the disability benefits into consideration when determining need and ability to pay alimony.

b. **Survivor's Benefits**

The Survivor's Benefit Plan (SBP) pays a percentage of the member's retirement to the surviving spouse or former spouse. Since 1986, courts have been empowered to order the election of a former spouse as beneficiary of the SBP. Premiums are paid from the monthly retirement benefits payable during the member's life. It is possible to allocate the burden of those premiums by adjusting the percentages of the retirement benefits paid to each party. The benefit, however, is not divisible between a current and former spouse, or between two former spouses.[12]

Federal law has very stringent service requirements for electing an SBP beneficiary which, if not precisely followed, cause the benefit to be lost regardless of the court order. This is a severe malpractice trap, and case law is mixed as to whether there is a way for the intended beneficiary spouse to return to court to get an order that can re-start the one-year election period. In now appears that if the original court order did *not* provide for an allocation of the SBP, a return to court and resulting new order will be honored, but if the original decree *did* allocate the SBP, the later order will have no effect. This makes no sense, but it is the current interpretation.

c. **Medical Benefits**

One thing to watch closely in military cases is the time restrictions for former spouse qualification for ancillary benefits (medical, etc.) For full benefits, the member must have served twenty years, the marriage must have lasted twenty years, and the service and marriage must have overlapped by twenty years (the "20/20/20" rule). Lesser benefits are available for 20/20/15 spouses. A special, congressionally-mandated insurance program, called US-VIP, is available for former military spouses married at least one year, but the terms and restrictions vary according to the same three factors. In an appropriate case, deferring the divorce could prove to be in the parties' mutual best interest.

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[12] The military retirement system, like the Nevada PERS system, has no provision for division of a survivorship interest. The absence of such a provision works the same hardships of unjust enrichment and dispossession. At the 1990 hearings on the USFSPA, the members' political pressure groups, the former spouses' political pressure groups, the Pentagon representative, and the American Bar Association representatives all agreed that this required correction, but Congress has taken no action to date.

d. **Special Caution for Military Cases**

A peculiarity of military cases is the special jurisdictional rules that must be followed in order to get an enforceable order. In other public and private plans, a valid state court judgment is generally enforceable. In a military case, however, acquisition of jurisdiction over a military member must be obtained by reason of his residence (other than for military assignment), domicile, or consent. In Nevada (as in most places), making a general appearance usually constitutes consent to trial of the entire action, but one case from California indicates that a service member may "un-consent" to court jurisdiction over the retirement issue alone. *See Tucker v. Tucker*, 277 Cal. Rptr. 403 (Ct. App. 1991).

The essential lesson of this jurisdictional point is to *never* take default against an out-of-state military service member in a divorce case in which division of the retirement benefits is sought. The resulting judgment will not be enforceable, and will almost certainly result in untoward consequences. If valid jurisdiction according to the provisions of both state and federal law cannot be achieved, then the action may have to be dismissed and re-filed in the state in which the military member resides.

The jurisdictional caution is even more applicable in partition cases. According to the Nevada Supreme Court, the jurisdictional test is to be applied in the *present* (i.e., when the current action is commenced) as opposed to considering what jurisdiction was established during the original divorce. *See Messner v. District Court*, 104 Nev. 759, 766 P.2d 1320 (1988); *contra*, *Lewis v. Lewis*, 695 F. Supp. 1089 (D. Nev. 1988).

Failure to acquire jurisdiction over a military member under both state *and* federal law will leave the former spouse with no rights and an unenforceable judgment. *See* 10 U.S.C. § 1408(c)(4). NRS 14.065 (our "long-arm" statute) is effectively overridden in military cases; while the case can go forward, it will not result in an enforceable order.

8. **Forms of State Government Pension Plans (PERS)**

Nevada, like most states, has its own pension program. PERS (the state "Public Employees Retirement System"), was established by statute and is codified at NRS 286.010 *et seq*. Essentially, the system is a defined benefit retirement program, crediting 2.5% of a member's highest average salary during any three years (usually, a member's last three years). NRS 286.551. Benefits vest after five years; survivor's benefits vest upon the member's eligibility for retirement or completion of ten years of service. NRS 286.6793.

If the member started service before July 1, 1985, and works 36 years, a maximum 90% of salary can be paid. Members starting after that date have a maximum 75% of salary, reached at 30 years. NRS 286.551. Certain workers have paid in to a "member's contribution" account from the days when PERS had employee as well as employer-paid funding. That amount is refundable in certain circumstances, and may be applied to the (divisible) retirement in others, so it is important to know in any PERS case if there have been any employee contributions.

Most state government employees are eligible for retirement at 65 with five years of service, or 60 with 10 years of service, or any age with 30 years of service. This is an important point, as the practitioner may have to calculate more than one possible retirement date for any employee still in service. For example, a teacher beginning work in Nevada at age 26, who divorces at age 34, will have only eight years in service. Accordingly, the earliest *certain* retirement is at age 65 -- 31 years

in the future. If he continues employment for just another two years however, he would be eligible to retire at age 60 -- only 27 years in the future. If he managed to work 30 years, he could retire at age 56 -- only 22 years in the future. These differences greatly change the actuarial assumptions going into present value calculations.

Certain state government employees operate under separate rules. Police and fire-fighters have their own rules, which differ somewhat from those governing other employees. Instead of retirement at 65 with five years of service, or 60 with 10 years of service, or any age with 30 years of service, those members can retire at 65 with five years of service, 55 with 10 years of service, 50 with 20 years of service, and any age with 30 years of service.

Additionally, the survivor's benefits payable for police and fire-fighters are different than those of other employees. Most employees, to get the full, unreduced amount of monthly benefits at retirement, must give up all survivor's interests. *See* Exhibit 4, Option 1. Police and fire-fighters, however, get both the full monthly retirement *and* a 50% survivorship interest, if the same spouse is married to the member at both retirement and the member's death. *See* Exhibit 5, Option 1.

Since 1987, PERS has required spousal consent to the form of retirement chosen. *See* NRS 286.541. As currently enacted, however, the absence of spousal consent only prevents the member from choosing any desired retirement option for 90 days. *See* NRS 286.545. Apparently, the burden is on the spouse to get a court order prohibiting the member from choosing a different retirement option within the 90 day period. Essentially, a spouse for whom no survivor designation is made who is unhappy with that fact has 90 days to choose to divorce his or her spouse and get a court order mandating a different option. Further, PERS is statutorily immune from suit for benefits paid because of a member's falsification of marital status on a retirement option selection form. NRS 286.541.

Current, but apparently informal, policy at PERS is to honor to the degree possible all Nevada court orders, or at least those that comply with the statutory restrictions of the plan and are issued before a member retires. For example, PERS could not honor an order for payment to a former spouse of a putative pension share under *Gemma*/*Fondi*, since the statutes prohibit any payment prior to actual retirement; the spouse's collection would depend upon direct payment of such a putative share from the member. There does not appear to be any movement in the legislature to change the PERS statutes to allow the system to comply with those Nevada Supreme Court cases.

There have been recent changes to PERS, however, and more are likely in the near future. The Nevada Legislature, in the 1993 session, approved AB 555, which basically patterned the state PERS statutes after the rules governing private Qualified Domestic Relations Orders.

Specifically, the new rules require court orders dividing PERS benefits to be signed by a district court judge or supreme court justice, and explicitly provide for enforcement of an alternate payee, who may be a spouse, former spouse, child, or other dependent of a member or retired employee. Enforceable orders include "a judgment, decree or order relating to child support, alimony or the disposition of community property" and extends to "all or a portion of the allowance or benefit of a member or retired member from the system." The implications of the language used are significant. Apparently, an interim order is enforceable. The "other dependent" language appears to clear the way for "palimony" or other such awards. There does not appear to be *any* payment limitation, so even 100% of the benefit could be transferred from the employee to the other party in an appropriate case.

The new rules allow an order to be enforced if it satisfies five requirements:

- It must clearly specify the names, Social Security numbers, and last known mailing addresses, if any of the member and the alternate payee.

- It must clearly specify the amount, percentage, or manner of determining the amount of the allowance or benefit of the member or retired employee that must be paid by the system to each alternate payee.

- It must specifically direct the system to pay an allowance or benefit to the alternate payee.

- It must not require the system to provide an allowance or benefit not otherwise provided under the state statutes governing PERS.

- It must not require payments to an alternate payee before the retirement of a member or the distribution to or withdrawal of contributions by a member.

The last two provisions are almost certain to foster litigation. It is likely that the language used was simply modeled on portions of ERISA, 29 U.S.C. § 1055(c), but the language appears to be in direct conflict with the Nevada Supreme Court's mandates in *Gemma* and *Fondi*.

For example, it would probably be malpractice, after *Fondi*, to *not* provide for payments to the former spouse upon the employee's eligibility for retirement. By its own words, however, the new statute appears to hold such an order invalid -- it should be noted that the provision does *not* just reference orders requiring the *system* to make payments before retirement, but appears directed at any *orders* that provide for pre-retirement payments.

It is possible, of course, that the provision was only intended to provide that the *system* not make pre-retirement payments. Assuming the words used were not an oversight, however, and the provision means what it says, a clear equal protection problem is created if only PERS benefits are to be shielded from distribution to a former spouse upon eligibility of the member for retirement. It seems clear that further case law development is necessary.

It had commonly been believed that PERS was not *able* to honor orders issued after payments began. Cutting against this interpretation of the statutes was the reality that the statutory scheme itself calls for re-computation of the amount payable in certain circumstances. *See* NRS 286.545(2). Under the new rules, the previous belief is even more in doubt, since it specifically references a "member or retired employee" as the payor. Again, the language may be ambiguous, and agency practice or a court case may be necessary to determine if the language means what it appears to say.

The new rules are likely to change many aspects of practice. For example, PERS has long sought "releases" from members in order to make direct payments to spouses. That procedure does not appear to be necessary any longer.

Under PERS, it is possible to both provide a survivor annuity and to modify its amount to reflect only the share of the pension awarded to the former spouse. Option 6 permits the specification of the sum that is guaranteed to the spouse irrespective of the member's death.[13] The practitioner should note, however, that any absolute sum may be illusive, since PERS provides for

[13] Note in negotiating any such sum that the amount of the survivor annuity will have a *direct* impact on the amount of the monthly benefit available for division between the parties during the life of the member. PERS will, upon request, analyze how much would be paid under each option.

post-retirement cost of living adjustments, based either upon a CPI average or at 2% after the third year, 3% after the sixth year, and 3.5% after the ninth year.[14] *See* NRS 286.575, 286.5756. Survivor beneficiaries only receive COLAs under options 2, 3, 4, and 5. *See* NRS 286.5775(3). Another informal PERS policy, however, has permitted COLA adjustments to fixed survivorship sums under Option 6, despite the absence of clear statutory authority to do so.

As currently phrased, the survivorship interest is non-divisible. In other words, if a former spouse is awarded 25% of the retirement, and Option 2 is selected, the former spouse would actually gain an *increase* in payments after the member's death. What cannot easily be done is to *divide* the survivorship interests (between a current and former spouse, for example). Anecdotal accounts suggest that some creative counsel have accomplished this result anyway, by having the relevant court order call for such a division, and having PERS pay the survivorship interest (in one of the beneficiary's names) to a trustee who then divides the benefit.

Given the large and increasing proportion of divorces involving multiple families, a change in PERS to explicitly allow division of the survivorship interest would be a beneficial change. The American Bar Association is on record as encouraging all pension plans to provide for such interests. It is possible that the statutes will be further amended in future years to provide for divisible survivorship interests.

9. **Forms of Other Government Pension Plans & Social Security**

Foreign Service and CIA pensions are not often involved in Nevada divorces, but it should be noted that the federal statutory provisions governing those retirement systems give a presumptive share of the retirement benefits to a spouse if the marriage lasted at least ten years, at least five of which overlapped service abroad. The presumptions can be overcome (either to increase or reduce them) by contrary court order or agreement. In other words, while a silent Nevada decree would divest a former *military* spouse of all claims to the retirement benefits, it would apparently not divest a similarly situated Foreign Service employee's spouse.

Railroad retirement has its own specialized rules, which provides a statutory benefit for divorced spouses who were married for at least ten years. *See* 45 U.S.C. § 231(a). Tier I benefits are similar to Social Security, and different from military or Civil Service plans, in that payments to the spouse do *not* reduce the benefit being received by the retiree. Tier II benefits, however, are apparently divisible as community property. *See Belt v. Belt*, 398 N.W.2d 737 (N.D. 1987).

All practitioners should note that if the marriage lasted at least ten years, the former spouse is eligible for certain benefits under Social Security upon attaining the age of 62 (if not remarried), based upon the spouse's own earnings, or those of the wage-earner spouse, whichever are greater. Such Social Security payments are statutory entitlements that do not reduce benefits paid to retirees. Essentially, the state courts are prohibited from ordering any assignment, transfer, execution, levy, attachment, or garnishment of amounts paid by Social Security. The Nevada Supreme Court has, however, indicated that the amounts received in Social Security may be taken into consideration in dividing property and awarding alimony. *See Anderson v. Anderson*, 107 Nev. 570, 816 P.2d 463 (1991).

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[14] A separate provision would add an *additional* increase "if adequate money is available which has been designated for that purpose" based on the years since a retirement went into pay status. *See* NRS 286.5775.

II. VALUATION OF PLANS IN DIVORCE ACTIONS

The biggest challenge for counsel in cases involving retirement plans appears to be in valuation. In Nevada, valuation is generally performed at the moment of divorce, rather than separation. *See Forrest v. Forrest*, 99 Nev. 602, 668 P.2d 275 (1983). The value of any retirement at an earlier time (*e.g.*, separation or filing of the complaint) is irrelevant under the law as it now stands, sparing Nevada practitioners the "value now of benefits then" problems that occupy courts elsewhere. *See* M. Snyder, The Value of Pensions in Divorce: What It Is and How to Use It § 17 (2d ed. 1992 & Supp. 1993).

Questions have been raised as to the equity of having post-separation accumulations and debts considered as part of the marital estate. For now, however, the task of Nevada attorneys valuing retirement benefits in divorce is fairly simple: obtain the value as of the date of divorce of all retirement benefits accumulated during the marriage.

A. Vestedness and Maturity Revisited

The *Gemma* approach (division "if, as, and when" received or receivable, pursuant to the "time rule") eliminates the need to perform actuarial computations, since the parties end up sharing the risk of non-payment (by premature death, plan failure, etc.) proportionately to their ultimately payable percentages in the benefits to be received.

Where the nonemployee spouse has a small interest, however, or where there are other significant assets in a case which could be exchanged for the pension, it might be necessary or advisable to place a value on a pension plan. Valuation for "cashing out" is particularly attractive for pensions that are neither vested nor matured. While *Gemma* and *Fondi* appear to block the employee spouse from requiring such a cash out, it is unclear whether the *non*-employee spouse could so insist. In either event, there does not appear to be any legal bar to the parties stipulating to such an arrangement.

If trial seems likely, it is probably necessary to retain an expert in such cases. Valuations in such cases are inherently subjective due to the uncertainty of the events that could cause the pension not to vest or mature. At the very least, the expert will need to have a copy of the plan in question (and the specifics of the participant's interest in it), and know the ages of the parties, the date the employee began work for the employer, the dates and amounts of all contributions (if any) made to the plan, prospects for early or late retirement, and the health of the parties.

There is always more room for negotiation when benefits are not vested or matured, since the employee spouse has the option of taking unilateral action that could prevent benefits from ever being payable to either party. Of course, if a party did take such a "cut off your nose to spite your face" approach, it is possible that the other party could argue "waste" and convince the court to enter an alimony award for the sum to compensate the party who would otherwise have received a sizeable property distribution. *See*, *e.g.*, *Siragusa v. Siragusa*, 108 Nev. ___, ___ P.2d ___ (Adv. Opn. No. 152, Dec. 3, 1992) (husband's bankruptcy of million dollar property award was partial grounds for award of permanent alimony).

B. Private Pension Plans

1. Defined Benefit Plans

Because the value of a participant's interest in a defined benefit plan depends upon numerous subjective factors, it is difficult to measure until after retirement. If the employee spouse is still working, assumptions must be made as to how many more years will be worked, whether (and how much) salary will increase, whether the employee might be fired or die before retirement, how long the employee will live *after* retirement, etc.

Expert assistance is almost always required for these plans, since life tables, discount rates, actuarial accounting, etc., are required in arriving at a valuation. There are several approaches to such valuations.

Both *Gemma*, *supra*, and *Fondi*, *supra*, involved PERS benefits, which are essentially defined benefit plan benefits. In *Gemma*, the court rejected an effort to ascertain the present value of the benefit and have the employee buy out the nonemployee's interest. Instead, the court adopted the "time rule," whereby early and late years have equal value. The spousal share is determined to be a portion of the benefits that are ultimately payable, although no particular value is placed on them (the usual formula is to divide the months of service during marriage by the total number of months of service, and divide that fraction in half). *Fondi* apparently made use of the "time rule" mandatory for all such divorces in Nevada.

Some critics have complained that where the divorce occurs while the employee is still working, such a formula actually gives the non-employee former spouse an interest in the employee spouse's post-divorce earnings. They argue that while the spouse's interest might be greater than an amount frozen at the earnings level at divorce, it should be less than a straight share of the benefits ultimately received.

The *Gemma* court elected to view the "community" years of effort qualitatively rather than quantitatively. The court added a hedge; the trial court can reserve jurisdiction to determine, after retirement, whether the benefits proved to be much greater than expected because of extraordinary "effort and achievement" (as opposed to "ordinary promotions and cost of living increases"), in which case the court could recalculate the spousal interest (but see the *caveat* below as to the two-edged nature of such reservations of jurisdiction).

Since Nevada has no quasi-community property rule, practitioners should be aware that certain other jurisdictions have expressed a policy preference for the present value/immediate offset method for dividing defined benefit plans. *See Pulliam v. Pulliam*, 16 Fam. L. Rep. (BNA) 1452 (Okla. Sup. Ct. No. 68011, July 17, 1990). Other courts have retreated from the time rule somewhat, ruling that lump-sum or other equivalent distributions are acceptable or preferred. *See*, *e.g., Ruggles v. Ruggles*, 19 Fam. L. Rep. (BNA) 1540 (N.M. Sup. Ct. Nos. 20547 & 20639, August 16, 1993). Even in the absence of a reconsideration of the issue by the Nevada Supreme Court, in multi-jurisdictional cases, our "pure borrowed law" approach could require addressing this argument in our courts.

2. **Defined Contribution Plans**

It is considerably easier to place a value on a participant's interest in a defined contribution plan, since it is a sum certain in a segregated account. Still, valuation in a divorce action may not be as simple as dividing up the balance according to the marital percentages.

Some commentators assert that the value of such plans should be reduced by the tax consequences of withdrawing the funds. There is some Nevada authority for this approach. In *Ford v. Ford*, 105 Nev. 672, 782 P.2d 1304 (1989), the court held that divorce courts must consider tax

consequences when dividing community property if there is proof of immediate and specific tax liability. It is probably a good idea to remember the existence of eventual tax liability on such an account if it is traded for another asset with no such burden.

The question for valuation in a particular case is whether the liability is "immediate and specific." An argument could be made either way, depending on the facts of the case, since some parties have no realistic choice but to liquidate such benefits because of the lack of other cash assets in the case. The penalties are significant (full taxes at 15-31%, depending on the recipient's marginal tax rate, plus 10% of the amount withdrawn) and greatly reduce the value of the fund considered in such a way.

Other authors have argued that a *tracing* analysis would be superior for defined contribution plans (as opposed to the "time rule") because it is possible to discover the source of all funds in the account. *See* Amado, *The Ubiquitous Time Rule -- A Responsa: An Argument for the Applicability of Tracing, Not the Time Rule, to Defined Contribution Plans*, 13 Family Law News, Sum. 1990, at 2 (California State Bar, Family Law Section Pubn.)

Courts continually seek new solutions. One New York court tried to accommodate valuation arguments by fixing a present value on the spousal share of the retirement fund, and tacking a cost of living formula on the payments made to pay off the spousal share until paid. *See Sassano v. Sassano*, 16 Fam. L. Rep. (BNA) 1435 (N.Y. Sup. Ct., June 18, 1990). That approach has been successfully used in Nevada cases, at least at the trial level.

C. **Civil Service Benefits**

CSRS and FERS benefits are somewhat complex. Proper valuation of those plans should include consultation with an expert. There are easy-to-use guides available, however, that contain much of the information necessary to ballpark a case. *See* Exhibit 6. It is an annual publication called the "Federal Personnel Guide" (Key Communications Group, Inc., P.O. Box 42578, Washington, D.C. 20015-0578; (301) 656-0450). At least one dedicated software program has been developed for doing calculations of CSRS retirement benefits and its tax and other effects. It is called the "CSRS Federal Retirement Calculator and Retirement Planner," Decision Support Software, Dept. CY, P.O. Box 2368, Granite Bay, CA 95746; (916) 791-1002.

D. **Military Retirement Benefits**

Each year, the Department of Defense compiles a chart of non-disability retirement benefit values according to rank and years of service upon retirement. While the Department of Defense Office of the Actuary *does* publish "lump sum equivalency" charts for military retirements, using military-specific mortality tables, that office includes a much-ignored disclaimer that its figures should not be used for property settlements. The 1993 figures are attached as Exhibit 7.

The Actuary also produces disability and non-disability retirement life expectancy tables, from which a good estimate of present value for a military retirement can be independently calculated. A convenient annual source for much of this information is the annual "Retired Military Almanac" (Uniformed Services Almanac, Inc., P.O. Box 4144, Falls Church, VA 22044; (703) 532-1631).

E. **Special Problems and Considerations**

1. **Disability Pensions**

Probably the most common valuation difficulty involves a disability rating on the part of the employee spouse which alters the "normal" retirement otherwise payable. Usually, the change is replacement of a portion of (taxable) retirement benefits with (generally nontaxable) disability benefits in an equal amount, but sometimes a disability award supplements the retirement benefits with a separate payment relating to the disability.

In the military context, there are two forms of disability, under chapters 38 and 61, primarily distinguishable by whether they are granted at or after retirement, and by the difference in dollar equivalency to the same percentage rating. To receive tax-free disability pay upon retirement for disability, a member must waive an equivalent portion of retired pay. Currently, such waived pay is deducted from the definition of "disposable" pay that may be split with a former spouse in accordance with a court order. Ultimately, any disability claim increases the money flowing to the retiree at the expense of the former spouse, even to the point of eliminating the spousal share entirely. *See Mansell v. Mansell*, 490 U.S. 581, 109 S. Ct. 2023 (1989).

An interesting change that is supposed to go into effect soon will eliminate the waiver of regular retired pay for military members with 100% disability ratings. Presumably, while the former spouse still has no share in the disability award, the elimination of the offset means that the regular retired pay will still be fully available in such cases. Somewhat oddly, this means that the former spouse of a military member with a 90% disability may receive nothing, while the former spouse of a military member with a 100% disability may receive the entire appropriate spousal share of the retirement benefits. Practitioners must be attuned to the possibilities, and the possibilities that the law will continue to change in the future, to adequately protect their client on either side.

While usually not as draconian as the entire elimination of a spousal share in the event of a disability award, similar results occur in other pension and retirement systems. There are drafting techniques for anticipating such possibilities and compensating for them (but note the *caveat* stated above with respect to *Mansell, supra*.) One suggestion is a reservation of jurisdiction in the trial court for a post-divorce award of alimony if the payment stream anticipated in the order is interrupted due to an action by the wage-earner. An example of language intended to accomplish this goal is set out in Exhibit 8 (sample Decree dividing military retirement benefits).

While bankruptcy is the obvious example of such an action by the wage-earner, *see Siragusa, supra*; *Martin v. Martin*, 108 Nev. ___, ___ P.2d ___ (Adv. Opn. No. 65, May 18, 1992) ("hold harmless" provisions qualified as maintenance or support, since court found that without it "spouse would be inadequately supported"; alimony ordered), there is no obvious reason not to reserve jurisdiction in the event of *any* interruption in the payment stream, including one caused by a disability conversion of the retirement. Even if the benefits themselves are out of reach, the court would then be empowered to award alimony sufficient to deflect the impact of divesting of the spousal interest.

Since Nevada law now explicitly directs courts to derive the "retirement component" of awards that on their face are "disability retirements," *Powers v. Powers*, 105 Nev. 514, 779 P.2d 91 (1989), practitioners have room to argue about what valuation should be given to the retirement component of a disability pension as divisible community property. While military cases have special restrictions (*see* discussion of *Mansell, supra*), the military retirement cases provide good guidance as to the arguments that can be raised.

In a series of cases, various courts ruled that where a disability award simply replaced a retirement on a dollar-for-dollar basis, the conversion of the retirement to a disability form of award was irrelevant to the right of the former spouse to share in the benefits originally ordered by the court. *See*, *e.g.*, *In re Marriage of Mansell*, 265 Cal. Rptr. 227 (Ct. App. 1989), *on remand from* 490

U.S. 581, 109 S. Ct. 2023 (1989); *Toupal v. Toupal*, 790 P.2d 1055 (N.M. 1990); *Berry v. Berry*, 786 S.W.2d 672 (Tex. 1990). It can reasonably be predicted that the arguments in these cases will be repeated in the context of other kinds of pensions.

As a matter of public policy, it is probably a good thing to prevent the unilateral conversion of a stream of payment benefits from divisible to non-divisible by the employee. Making the employee's election irrelevant to the right of the spouse will prevent a great deal of gamesmanship and unjustifiable manipulation by retirees. They will be left with making a decision as to their benefits solely based on the impact the decision will have on them, without the strategic considerations of whether they can simultaneously divest their former spouses.

2. **Severance Pay and Transmutation**

As noted above, there is little to go on in this state as to divisibility of benefits received in lieu of the benefits actually awarded in a decree of divorce. The decision in *Banta v. Banta*, No. 19756 (Order Dismissing Appeal, Mar. 9, 1989), hints that the court supports a liberal interpretation of the awards in decrees.

Again, the military cases might lead the field. During the past two years, the services have responded to pressures to reduce the numbers of military members by devising programs rewarding members for leaving service prior to eligibility for regular retirement. Specifically, the military has adopted the Voluntary Separation Incentive (VSI) and Special Separation Incentive Benefit (SSB) programs, as well as a "15 to 20" year retirement plan. Certain members who have not yet achieved eligibility for regular retirement (i.e., 20 years of creditable service) have the option of electing benefits under one of the programs and being honorably discharged from service.

The programs have several differences, but are primarily distinct in that a member electing SSB benefits gets a single lump sum, while members choosing VSI get an annuity worth far more but paid over a number of years. *See* Exhibit 9A-9B. Members who are involuntarily terminated ("RIF-ed") are paid certain involuntary separation pay benefits. *See* Exhibit 10. The relative value of 15-year and 20-year retirements can be compared by looking at Exhibits 9C and 10. Since members only started leaving service under these programs in the recent past, there are apparently no appellate decisions addressing them. Anecdotal accounts from around the country, however, indicate that the exact words used in the original divorce decrees may determine whether spousal share are "translated" into separation benefits.

One special caution is warranted for practitioners whose clients are the spouses in these cases. Care should be taken to ensure that any "residuary" benefits surviving the conversion to severance pay, etc., is also divided by the court. In the military context, for example, members carry with them the potential to significantly increase the time credited for second retirement programs by counting military service. Many state governmental programs, including Nevada PERS, and many private retirement programs, grant credit in their retirement systems for military service, especially when no separate pension resulted from that service. *See* NRS 286.301, 286.303, 286.365, 286.479, 286.510(2).

Failure to make the resulting increase in benefits allocable to the former spouse is probably a mistake. A spouse seeking to share in a transmuted benefit or severance pay should also ask the court for a reservation of jurisdiction, at least, to enter such further order as is necessary to trace the spousal share of any later increase in benefits in another retirement system that is attributable to service during marriage.

3. **Valuation of Ancillary Benefits**

In most retirement plans, survivor's benefits may be divided proportionately among successive spouses. In military cases, Nevada PERS, and some private plans, however, only one person may be named as recipient of the survivor's benefits. Where the member wishes to nominate another person as recipient of those benefits, they may be worth more than their actuarial value.

Similar considerations apply to timing questions. For example, if the parties to a military marriage have been married for eighteen years during service, so that two additional years of marriage are required for full medical benefits, a member could probably exact some price for simply entering into a property settlement agreement and deferring the divorce itself. On the other hand, the negotiations could cut the other way: such deferral could be the only event preventing a spouse from making a claim for support sufficient to cover anticipated medical costs.

Counsel must be careful to know what benefits are accorded by virtue of the retirement programs at issue, or as a matter of federal entitlement. Under no circumstances should a spouse concede anything "in exchange" for COBRA[15] medical coverage, for example; federal law confers the right to such coverage as a matter of right.

4. **Miscellaneous**

Any large gaps between the ages of the parties can cause a skewing of the normal valuations for a pension plan, since the survivor's component will be so much larger. Various of the public and private plans take this into account in various ways. To make matters murkier, some plans use gender- and race-reflected tables, and some do not. The difference in life expectancies can lead to significant differences in valuation, and thus change strategy. For example, Exhibit 15 is a copy of the most recent (1989) United States "Life Tables."[16] If the client was a black male married to a white female, for example, and both were 30 years old, the difference in valuation would be significant. In a "blind" chart, both parties would be considered to have life expectancies of 47.2 years. If age and race were part of the evaluation, the husband would have a life expectancy of 38.5 years and the wife would have a life expectancy of 50.5 years. The "instant" twelve year gap in life expectancy has a significant impact on valuation.

Practitioners should be aware that there is some room for disagreement on the discount rate to be applied when reducing future benefits to present value. Six to eight and a half percent are typically seen, though certain types of plans (e.g., military) use far smaller discount rates due to the form of their security and investments (i.e., the government). Presently, interest rates are at a record low; the Pension Benefit Guaranty Corporation has issued calculations below *any* of the standard 21 sets of rates in their tables. As of October, 1992, the rate set was 5.75%, as opposed to 7.25%

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[15] Consolidated Omnibus Budget Reconciliation Act. Congress mandated that certain employers must provide transitional health coverage, at controlled premiums, to individuals whose right to participate in group health plans terminated for various causes, including divorce.

[16] Vital Statistics of the United States, 1989, Life Tables at 12 (U.S. Dept. of Health & Human Services, Public Health Service, Centers for Disease Control and Prevention, National Center for Health Statistics 1992) at 12.

just a year and a half earlier. The difference is significant, since the *lower* the presumed interest rate, the *higher* any "present value" calculation based on that rate.[17]

A problem that has cropped up in a series of cases recently involves prenuptial agreements that purport to waive spousal interests in retirement or survivorship interests in pension plans falling under ERISA (basically, all private retirement plans). The consensus of courts ruling in this area is that such purported waivers are invalid, on the basis that ERISA requires that only a "spouse," not an intended spouse, can make a valid waiver of benefits. *See*, *e.g., Howard v. Branham & Baker Coal Co.*, ___ F.2d ___ (No. 91-5913, 6th Cir., July 6, 1992); *Hurwitz v. Sher*, 789 F. Supp. 134 (S.D.N.Y. 1992); *see generally* J. Dam, "Most Prenuptial Agreements Invalid Under Federal Law, Malpractice Suits May Become Common," Lawyers Weekly USA, August 16, 1993 at 1.

The solution to the problem of invalid prenuptial waivers is not obvious. Some practitioners have included in pre-nuptial agreements a clause requiring the soon-to-be spouse to sign an additional waiver after the marriage. That approach has some enforceability problems. Alternatively, a damages clause could be inserted in the agreement (in favor of the intended beneficiary as a third party beneficiary of the agreement). Again, there is a question whether such a provision could be enforced, as a matter of public policy or otherwise, since the clear intention is to circumvent the ERISA restrictions.

Finally, all counsel should be aware that there is a split in the federal circuits as to the dischargeability in bankruptcy of one spouse's obligations to another for future pension payments (or accrued arrears). The rule in the Ninth Circuit, for the moment, appears to be that prospective payments are not dischargeable, but accrued arrearages may well be. *See In re Teichman*, 744 F.2d 1395 (9th Cir. 1985); *see also Bush v. Taylor*, 912 F.2d 989, *vacating* 912 F.2d 962 (8th Cir. 1990). This may change; Congress is entertaining various proposals by segments of the American Bar Association to prohibit the dischargeability of any obligation to a former spouse or child arising from a domestic relations order.

F. **Tools and Assistance**

There are a number of ways to estimate the value of the retirement, in deciding whether retaining experts is warranted, etc. Many service bureaus advertising in the ABA Journal and elsewhere will do a present value analysis of a pension plan for about $100.00, which usually includes a written report. It is, of course, important to check into the methodology used, and to ensure the reliability of the base data used for the calculations.

There are local firms and experts offering similar services for even less money. Such firms usually offer their own questionnaire for attorneys, perform retirement plan valuations, and offer expert testimony as to valuation if necessary. Geffert & Associates, (800) 365-7456, for example, charges $50.00, plus $10.00 per written report.

Alternatively, at least one book in the field has an estimator "slide rule" thrown in as a bonus. *See* Marvin Snyder, The Value of Pensions in Divorce: What It Is and How to Use It (2d ed. 1992

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[17] The reason for this is obvious, once analyzed. A present value calculation essentially asks the question of how much money would have to be invested on a given date, at a given interest rate, to yield a stream of payments in the future which over some anticipated period would consume all of the accrued interest and principal. The lower the rate of investment, the more money needs to be invested to yield the later payment stream.

& Supp. 1993) (PESI, P.O. Box 1208, 200 Spring Street, Eau Claire, WI 54702; (8005) 826-7155). For do-it-yourself types, there are a number of computer programs available for use in deriving present values, which require the basic figures about the benefit and the parties, and some input on discount rates, life expectancies, and COLAs. For example, Legal Math-Pac, Colorado Custom Legal Software, 3867 Paseo del Prado, Boulder, CO 80301 (303) 443-2634; or dPenval, dLegal System, 189 Jackson Ave., Salisbury Mills, NY 12577 (800) 331-9218.

III. **DIVISION OF BENEFITS**

A. **Public vs. Private Plans**

A very common misperception is that division of retirement benefits always requires a Qualified Domestic Relations Order, or "QDRO." In actuality, a QDRO is only required for plans established by private employers which seek to take advantage of certain tax deductions for contributions to the plans (i.e., "qualified" plans). *See* 29 U.S.C. § 401(a).

It was the Retirement Equity Act of 1984 that gave rise to the idea that the spouse of a wage-earner was entitled to distribution of a portion of the retirement benefits at the earliest date in which a plan participant was *eligible* to retire, whether or not the participant did so. A QDRO can treat the retirement benefits as an item of property for division, or a source from which child support or alimony can be paid, or both. Any portion of a private pension plan, up to 100%, can be awarded to a former spouse.

One new twist just added to litigation concerning ERISA and qualification of QDROs generally, is that at least one state court has found that it has concurrent jurisdiction with the federal courts to determine whether a state court order is a qualifying QDRO under federal law (ERISA). Overturning a Plan Administrator's rejection of a proposed order, the First District Court of Appeal in California found the court order to be a qualifying QDRO, and ordered the Plan Administrator's compliance with its terms. *See In re Levingston*, 16 Cal. Rptr.2d 100 (Ct. App. 1993). It appears that this ruling had the blessing of the federal court that otherwise would have heard the matter. *See Board of Trustees of the Laborers Pension Trust Fund for Northern California v. Levingston* , 1993 WL 76930 (W.D. Cal., Mar. 9, 1993).

Governmental plans (including PERS) are explicitly exempt from the legislative scheme constructed by ERISA (the "Employee Retirement Income Security Act of 1974") and REA (the "Retirement Equity Act of 1984"), which together establish the QDRO requirements.

For private plans, practice varies widely, but the modern consensus appears to be that a QDRO is best made a separate document from the Decree itself, although referenced in the Decree. In this way, any problems with getting the Plan Administrator to recognize and enforce the QDRO can be accomplished with amendments only to that order, rather than amendments to the Decree of Divorce itself. The Decree should anticipate the possibility of amendments to the QDRO being necessary, and reserve jurisdiction to do so.

For governmental plans (including military and Civil Service), the safest practice seems to be to include all critical terms in the Decree itself, although federal law generally allows the division of benefits to be pursuant to a document "incident to" such a Decree, such as a property settlement agreement. If a separate order is drafted, it should be expressly incorporated and referenced in the Decree.

B. **The Requirement of Service**

Amazingly, some practitioners continue to close their files upon entry of the Divorce Decree, without ever notifying the holder of funds of the existence of the order for allocation of a part thereof to a former spouse.

For private pension plans, the Plan Administrator must be notified, and must approve the Order submitted. All administrators will provide information as to how to do so upon request. Civil Service pension division orders go to the Office of Personnel Management ("OPM"). Orders relating to military retirement benefits go to the pay center for the appropriate branch of service (and per federal law must be sent by certified mail, return receipt requested), but practitioners should note that the military is consolidating its operations, and the pay centers' titles and mailing addresses are in a state of flux.

C. **Reservations of Jurisdiction**

Many practitioners seek reservations of jurisdiction for enforcement of attempted divisions of retirement benefits until certain that the language used in the order accomplishes its intended purpose. That strategy has received tacit approval from the Nevada Supreme Court, but the cautious practitioner should note that it is now a two-edged sword, as the reservation could allow the employee spouse to claim that post-divorce "extraordinary effort" led to the increases in the value of the pension, therefore requiring a diminution of the share allocated to the non-employee spouse. *See Gemma, supra; Fondi, supra.*

D. **How Important is the Math?**

While the decisions of recent years apparently require counsel to do some fairly sophisticated valuation in presenting retirement benefits to the divorce court, another line of opinion seems to indicate that the court is free to disregard those precise calculations when dividing the benefit. Most recently, the Nevada Legislature has indicated that the mathematical approach should be followed.

In *McNabney v. McNabney*, 105 Nev. 652, 782 P.2d 1291 (1989), the court (with two Justices dissenting) expressly held that the prescription in NRS 125.150(1) to divide assets in a "just and equitable" manner does *not* mean equally, and that there is not even a presumption of equal division of the community property portion of assets.

McNabney involved division of the future proceeds of a particular "big case" in a lawyer's divorce, in which the court approved an unequal determination based on the short duration of marriage (3 years, with separation after 2 years), and the facts of the case: the wife entered the marriage with "considerable separate estate," was self-supporting and neither expected not depended upon the husband for economic support; the wife would not require any financial assistance after divorce to maintain the same standard of living; and the asset in question was a substantial portion of the husband's law practice income.

The court stated that it was "perhaps" proper to use an even division of assets as a "starting point" to the court's analysis, and noted in *dicta* that a wife and mother may often deserve far more than 50% of property (although in this instance, the court was doing exactly the opposite by allocating the bulk of the asset to the party who obtained it).

McNabney was never applied to any pension cases at the appellate level. As of October 1, 1993, however, NRS 125.150 has been altered so that community property is to be equally divided

unless the court finds "a compelling reason" to make an unequal distribution and sets out that reason in writing. Thus, it appears that the math required under *Gemma* and *Fondi* is necessary, and *McNabney* appears to be largely a dead letter.

Some plans (e.g., the military), place limits on the percentages which can be allocated to the spouse under any circumstances, but no known plan limitation is more restrictive than the time rule, i.e., a mathematical percentage of one-half of the marriage during service.

E. **How to Actually Do It**[18]

The mechanics of dividing private pension plans are largely beyond the scope of this seminar.[19] Unless there are sufficient other resources to trade off a spousal pension share for some other asset, dividing a private pension requires a qualified domestic relations order, or QDRO. *See* I.R.C. § 401(a)(13).

Any amount of theoretical discussion is of limited use in actually sitting down to plan and draft the documents for division or retirement benefits in an actual case. This section references some of the forms attached as exhibits for reference. The practitioner building up a library of references for the purpose of drafting such documents should also look at the reference works set out in Section III.F, below, and/or other works on the subject available in the law library.

1. **Defined Benefit Plan QDROs**

Many practitioners do not understand why they cannot simply obtain a form order from the Plan Administrator of a pension plan, fill in the blanks, and submit it for signature by the Judge. The answer lies in the interest of the parties. The form orders distributed by Plan Administrators are largely sufficient to pass the test of qualification to *be* QDROs, but that is the Plan Administrator's only concern; he or she neither knows, nor cares, about what steps may be taken to protect your client from the vagaries of life (or the malice of the other party).

As counsel for either party, you must seek to have the QDRO address many items that are not strictly necessary to creating an enforceable QDRO. The absence of such provisions will not affect the *validity* of the order, but may well determine whether or not the order actually does your client any good in the real world.

Some illustrations might be helpful. You should expressly deal with potential changes in status, the ultimate example being death. While the former spouse's attorney probably cannot protect

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[18] A word of caution is in order here. While the directions and forms referenced in this section are believed to be accurate, they are by no means all-inclusive or complete, and are known to include matters that, if used without adequate thought and planning, would actually harm the party intended to be helped. Please do *not* simply adopt or use the formats below without separately analyzing your cases and adapting these materials to the particular facts and circumstances of those cases.

[19] Marjorie O'Connell, the principal in Divorce Taxation Education, Inc., takes one to two days to lecture on the intricacies of QDRO-drafting and private pension rules. No such effort is attempted here. The intent of these materials is more to flag the practitioner on what needs to be known to do this correctly, than to actually provide the instruction required to do so. Those wishing assistance with drafting should consider some of the references in the "Tools and Assistance" section on page 42.

his or her client from forfeiture by the *former spouse's* death prior to distribution, it is not difficult to nominate the former spouse as "surviving spouse" for purpose of receipt of the death benefits payable in the event of the *participant's* death, whether before or after the benefits are in pay status.

The absence of such a provision will not affect the validity of a QDRO, but if the facts are that the participant dies, has a new spouse, and the former spouse's attorney did *not* put such a clause in the QDRO, malpractice liability looms. On the flip side, failure to restrict the former spouse's "surviving spouse" benefit to the portion of the retirement benefits earned during marriage could leave the *participant's* attorney vulnerable to a claim by the intended beneficiary (later spouse) of the participant.

Similarly, the QDRO should provide for distribution from successor plans, for early retirement subsidies or other bonuses that might accrue, and should allocate the risk that, for whatever reason, the benefits are not paid.

Exhibit 11 is a form Qualified Domestic Relations Order for division of a defined benefit plan. It addresses, one way or another, the above concerns, but is of course not appropriate for every case. It may, however, provide a starting point.

2. **Defined Contribution Plan QDROs**

Most of what is written in the preceding subsection is equally applicable here. Because the form of benefit sought to be divided is different, the options provided and language used must be different. Exhibit 12 is a form Qualified Domestic Relations Order for division of a defined contribution plan. Again, it should be used as a starting point for drafting only.

3. **Military Retirement Benefits**

The form supplied as Exhibit 8 is in the format of a decree of divorce from a Clark County court. The material in boxes above the paragraphs is explanatory only. Note that the form is set up for the use of a computer's "search and replace" function to either Plaintiff and Defendant or the party's names.

Note also that the form is overinclusive in many respects; for the order to be valid under federal law, certain of the clauses in the form *cannot* stay in the form if others are used. It is up to the practitioner to understand the impact of these clauses so as to see what conflicts, and delete or amend as necessary. For example, the law normally allocates the premium cost on the survivor's benefit plan (SBP) to both parties; the form includes a clause that redirects the entire premium to be borne by the former spouse, which may or may not be what counsel (or the court) desire in a case. Be very cautious in using each paragraph.

The basic underlying statute, 10 U.S.C. § 1408, is included as Exhibit 14.

4. **Civil Service Retirement Benefits**

There have been very major recent changes to the regulations governing division of Civil Service retirement benefits. The changes are so sweeping that virtually every prior writing on the subject is out of date, and potentially dangerous to clients if relied upon. The text of the regulations were set out in the Federal Register. *See* Court Orders Affecting Retirement Benefits, 57 Fed. Reg. 33,570 (July 29, 1992) (to be codified at 5 C.F.R. Parts 831, 838, 841, 842, 843, 846, & 890. The

new regulations address the employee annuity (the pension), refunds of employee contributions, and survivor's benefits. The new regulations do *not* address the thrift plan.

The changes have been the subject of much writing by those in this field. The 1993 supplement to Mr. Snyder's introductory text on pensions is largely dedicated to Civil Service benefits, and the Office of Personnel Management has issued its own text (and disk) for those who want a guide to the new regulations and how to write orders complying with them. *See* U.S. Office of Personnel Management, *A Handbook for Attorneys on Court-ordered Retirement and Health Benefits Under the Civil Service Retirement System, Federal Employees Retirement System, and Federal Employees Health Benefits Program*, ISBN 0-16-038189-4, S/N/ 006-000-01377-5 (1992).

Semantics are very important to the new rule-makers at OPM. They have expressed concern that counsel use language they don't understand, so rather than make a mistake as to intent, they simply refuse to process any order titled "Qualified Domestic Relations Order," even if it is otherwise perfectly enforceable. The OPM reasoning is that use of the language indicates that the courts and attorneys do not know that ERISA is inapplicable to federal retirement plans, and so are conclusively presumed defective. For the same reason, do *not* use the ERISA term "Alternate Payee."

OPM has elected to coin new expressions: "Court Order Acceptable for Processing" replaces any reference to "qualified orders." Writers in the field have begun abbreviating it as "COAP." Any order submitted to OPM should be so entitled. Refer to the spouse of the wage-earner as "Former Spouse."

They have also assigned new meanings to words long used elsewhere to mean something else. For example, in OPM-ese, the term "accrue" does *not* refer to the accumulation of benefits by virtue of employment. To OPM, "accrue" means the commencement of payments under the retirement plan. "Employee annuity" means recurring payments under CSRS or FERS to a retiree. "Former Spouse Survivor Annuity" means either the payments to the spouse, or the employee death benefit under FERS, when paid to a former spouse after the employee's death. Use of words to mean what you have always thought they meant (and what they mean to everyone else) could invalidate an order submitted to OPM; great care is warranted.

Every nook and cranny of the regulations must be examined to prevent error. There are too many to list, so only examples will be provided here. Practitioners are urged to get the reference works and regulations, and review them carefully.

The COAP must specifically state that OPM is to pay the money directly to the former spouse. Any reference to a "Self-only Annuity" contradicts any attempt to insert a survivor annuity. It is apparently possible to have an "interim COAP" provide for payments to a court while matters are being worked out, with an amended COAP submitted when the court issues its final order. The COAP may *not* specify that payments continue for the lifetime of the former spouse (since the benefits terminate at the death of the employee, and only *survivor's* benefits would be available after that date). Which retirement system is at issue *must* appear in the COAP.

A proper order under the new regulations will contain specific provisions dealing with each of the three types of benefits addressed in the regulations. If an order is submitted using the words "retirement accounts" or "retirement fund" as the thing to be divided, OPM will interpret the order as going to contributions only and will *not* divide the annuity. *See* 5 C.F.R. § 838.612. Attempts to stipulate to modifications without a formal order will be ignored.

One interesting conundrum is created by the OPM rule that an order purporting to provide for payments of a spousal share upon eligibility for retirement ("earliest retirement date" in the land of QDROs) pursuant to *Gemma* and *Fondi* will be rejected as "non-complying." Since such a provision is essentially mandated by state law, and forbidden by federal law, some clever draftsmanship is required; probably the best thing is to mandate direct payments from the employee *until* retirement (of course that is where the money would really have to come from anyway), and from OPM thereafter.

One bright spot in the new regulations is the (partial) abandonment of what had been the stubborn OPM position that mistakes could not be fixed, irrespective of equity or hardship. In *Newman v. Love*, 962 F.2d 1008 (Fed. Cir. 1992), the court held that OPM was not prohibited from honoring a court order for a survivor annuity, if the order was the *first* order addressing marital property issues, even if the order is issued after the retirement of the employee.

Under the new regulations, a court order will be honored even if issued after retirement or the death of the employee if it is the first such order. In the lingo of the OPM, if a court order awards, increases, reduces, eliminates, explains, or clarifies an award to a former spouse, the court order must be issued before retirement or death of the employee, *or* it must be the first order dividing the marital property of the retiree and the former spouse. *See* 5 C.F.R. § 838.806.

A COAP may be used as a resource for payment of accrued arrearages. The COAP must specify how much is to be paid, so as to obtain accrued arrears, interest on the arrears, and interest on the declining balance of arrears until paid. An amortization schedule must be done so that the order can reference how much will be due and when it will be due (OPM will not do the calculations for you). Note that if payment of a lump sum is ordered, and there is no specific order to direct the entire monthly retirement payment to the former spouse, OPM will only make payments against that lump sum up to half of the gross payment, and will not allow modification for interest. Again, if such is the situation, perform the amortization scheduling ahead of time, and make the lump sum in an amount that contemplates interest.[20]

Because the new format is too new for decrees to have been tested in court, the Exhibit attached as Exhibit 13 is not a form decree, but the "model paragraphs" provided by OPM for use by counsel. It is presumed that as time goes on, essentially standardized language will evolve for this form of order as well.

Note that Exhibit 13, and the new federal regulations governing OPM procedure, do *not* affect the Thrift Savings Plan (TSP). The TSP is a defined contribution type of plan for federal employees; FERS employees get matching federal contributions up to a certain level. While the program is open to CSRS employees, there are no matching contributions for them. There are a variety of funds in which the employee can choose to invest, including the "Government Securities Investment" or "G" fund, the "Common Stock Index Investment" or "C" fund, and the "Fixed Income Index Investment" or "F" fund.

Withdrawal of TSP funds is limited to those separating from service, but practitioners should note that there are lump-sum distribution options from the plan (if $3,500.00 or less, the full fund balance is *automatically* distributed at the time of separation). However, practitioners should be

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[20] THE FOLLOWING IS A SHAMELESS COMMERCIAL MESSAGE: the author has created a computer program that computes interest at the legal rate in Nevada for all judgments, taking into effect any payments due or made. The program is called "Marshal Law." Contact the author for details.

aware that hardship loans up to $50,000.00 are available against the plan balance, and a specific category of hardship for loan purposes is "unpaid legal costs associated with a separation or divorce." The Federal Retirement Thrift Investment Board will, however, honor "most" court orders restricting distribution or safeguarding funds for other purposes (such as child support or alimony awards). Obviously, if the employee spouse has emptied out the TSP prior to the divorce, that fact should be brought up in the litigation.

5. **A (More or Less) Real World Example**

It has been suggested that it would be helpful to practitioners to have one actual case set out in these materials. Accordingly, Exhibits 16A-16J set out the documents necessary to do a valuation in one instance.

The presumed facts are that the husband is and will continue to be a PERS employee, that the parties married prior to the date the husband began service, that there are sufficient other assets to cash out the wife's interest in the plan, and that both parties desire to do so. At the present time, husband is 36 years old, and wife is 32. PERS reported in May, 1993, that as of the end of May, the husband had accumulated 6.860 service credits, had a "high-three" average compensation of $2,830.77 per month, and assuming immediate termination would have a retirement date of August 1, 2022 (his 65th birthday). The standard PERS information letter is attached as Exhibit 16A-16B. Counsel was doing the valuation in October, 1993.

Using the PERS assumption that the husband would terminate as of May 31, 1993, he would be eligible to receive $485.48 per month after turning 65, under Option 1 (the "unmodified" option, which has no reduction for any survivorship interests).[21]

As noted, by the time counsel did the valuation, it was October, 1993. Bringing the numbers forward is not difficult. Service credits accrue ratably over time -- each month is one-twelfth of a year, or .083333 credits. Thus, to bring the May figures forward to the end of October, it was only necessary to add .41667 (i.e., 5 X .083333). Added to the 6.860 credits shown, there were 7.28 (rounded) service credits at the end of October. Presuming no change in salary, the calculation as of October 31, 1993, would be $2,830.77 (average compensation) X 7.28 (service credits) X 2.5%, or $515.20. The spousal interest would therefore be half that figure, or $257.60, payable when the husband was eligible for retirement at age 65.

Using the most current figures available, the husband would have a life expectancy at age 65 of 15.2 years. *See* Exhibit 15. Because PERS grants COLAs, however,[22] it would greatly undervalue the pension interest to simply calculate the present value of the retirement for his estimated lifetime at the sum that would be payable at that time. Instead, it is necessary to do four calculations: from retirement to the first COLA, from the first until the second COLA, from the second until the third COLA, and from the third COLA for his estimated lifetime.[23]

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[21] The math is very straightforward: $2,830.77 (average compensation) X 6.860 (service credits) X 2.5% = $485.477705, which rounds to $485.48.

[22] *See* explanation of these rules set out above starting at page 16.

[23] Since the wife was younger than the husband, her life expectancy is not relevant for valuation purposes; even in an race and gender-blind chart, she should be expected to outlive the husband.

The estimated retirement date is the husband's birthday at age 65, or August 1, 2022. The sum to be paid is $515.20, and the term is three years (start through first COLA). An interest rate of 6.5% was chosen for these calculations. As shown in Exhibit 16C, the present value for the spousal ½-share of the future benefits is $1,282.61. After the 2% COLA three years after payments start, the sum raises to $525.50; the present value of the spousal share is $1,077.04. *See* Exhibit 16D. After the 3% COLA after another three years, the monthly sum is $541.27, and the present value $913.30. *See* Exhibit 16E. The final 3.5% COLA three years later brings the monthly sum to $560.22. By that time, the husband would be 74 years old, and a 74-year old white male has a life expectancy of 9.9 years, making the spousal share of the estimated remaining collection $2,085.59. *See* Exhibit 16F.

The total present value of the spousal share of the future collection would therefore be $5,358.54 at the time of divorce.

All of the above, however, may be incomplete and, under the circumstances, a misleading analysis. The husband gave assurances that he would continue employment until he had at least ten years in the system, and appeared able to do so. If it was presumed that he would complete ten years of service, his category would change from "five or more years" to "ten or more years," and thus would change his retirement date from age 65 to age 60. Additionally, his salary would almost certainly increase during the next three years; suppose for purpose of illustration that the historical wage chart gave rise to an expected four percent per year increase in wages.

The husband's continuing service after divorce would also change the spousal percentage. Presuming immediate divorce, but the husband's continued employment to ten years, the parties would only be married for 7.28 service credits out of the 10 that would be earned after ten years of service. Thus, the *Gemma*/*Fondi* time rule percentage would be half of that for the former spouse, or 36.4% (i.e., 7.28/10 X ½).

For the purpose of this second set of calculations, no attention should be paid to the "½ present value" line, since the spousal interest *only* is what is being calculated as the "Monthly Retirement Benefit to be Received." This is the classic "smaller slice of a larger pie" situation, and the calculations are very similar to what was done above.

The estimated retirement date is the husband's birthday at age 60, or August 1, 2017. The sum to be paid is $289.77[24] and the term is three years (start through first COLA). An interest rate of 6.5% was chosen for these calculations. As shown in Exhibit 16G, the present value for the spousal share (here, the entire sum calculated) of the future benefits is $1,995.11. After the 2% COLA three years after payments start, the sum raises to $295.56; the present value of the spousal share is $1,675.33. *See* Exhibit 16H. After the 3% COLA after another three years, the monthly sum is $304.43, and the present value $1,420.63. *See* Exhibit 16I. The final 3.5% COLA three years later brings the monthly sum to $315.08. By that time, the husband would be 69 years old, and a 69-year old white male has a life expectancy of 12.7 years, making the spousal share of the estimated remaining collection $3,842.46. *See* Exhibit 16J.

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[24] Calculated as follows. First, average wage is raised by multiplying the known $2,830.77 by 1.04 three times, to represent three 4% pay raises. The resulting figure of $3,184.23 is multiplied by 10 (service credits at 10 years) and then by 2.5%. The resulting retirement figure is $796.06, but the spousal share is only 36.4%, not half. Multiplying $796.06 by the spousal 36.4% share yields $289.77.

The total present value of the spousal share of the future collection would therefore be $8,933.53 at the time of divorce if the above assumptions as to continued employment are made.

The above two examples should demonstrate that there are a range of numbers that could be reasonably arrived at by a pension evaluator, depending upon the assumptions that are made in the case. Counsel must be prepared to look into the specific assumptions engaged in by actuaries or others in doing valuations, in order to argue that any particular valuation is more or less reasonable.

F. **Tax Considerations in Dividing Retirement Benefits**

Books could be written on the subject of proper tax treatment of pension and retirement interests. In fact, several books exist that spend considerable time and attention on this subject, and no effort will be made here to recapitulate all that information. *See*, *e.g.*, *Retirement Equity Act: Divorce and Pensions* (Divorce Taxation Education, Inc. 1985 & Supp. 1988); H. Wren, L. Gabinet, & D. Carrad, *Tax Aspects of Marital Dissolution* (1991). Some general observations and recent trends are properly glossed here, however. As noted in *Ford v. Ford, supra*, 105 Nev. 672, 782 P.2d 1304 (1989), "immediate and specific" tax liability *is* to be taken into account by the court in the disposition of community property.

Transfers of a portion of a retirement plan to a former spouse by means of a QDRO is not a taxable event to the wage-earner. Benefit payments to a former spouse under a QDRO are taxable income, except as to the former spouse's prorated share of any non-deductible employee contributions, which are not taxable. *See* 29 U.S.C. §§ 402(a)(9), 72(m)(10).

Similarly, an employee realizes no gain for tax purposes by withdrawing Keogh or IRA funds pursuant to court order and dividing them with a former spouse. *See* Private Letter Ruling 9016077 (April 20, 1990). The REA does not govern the division of IRAs, but the Internal Revenue Code provides that they may be divided tax free between divorcing spouses by agreement or court order. *See* 29 U.S.C. § 408(d)(6). A QDRO is *not* required to divide IRA accounts, as long as the decree (or an order incident to the decree) specifies the division. *See* 29 U.S.C. § 408(d)(6).

Recent changes to the IRS regulations have set a trap that many unwary parties are certain to fall into, and which could give rise to much avoidable malpractice litigation. It was created in a most sneaky manner. The supposed tax bill of 1992, H.R. 11, was vetoed, but tax provisions were quietly inserted in the "Comprehensive National Energy Policy Bill of 1992," H.R. 776, and the "Unemployment Compensation Amendments of 1992," Pub. L. No. 102-381 (July 3, 1992).

It was the last of these that created the trap. The idea was to simplify roll-overs from a retirement plan to an IRA. The rules do *not* apparently affect transfers from one IRA to another. The traditional means of transferring funds from an employee's retirement plan to a former spouse's new IRA should be altered, however. Traditionally, a QDRO would be submitted to the employee's plan,[25] a check would issue to the former spouse, and the former spouse would have 60 days within which to "roll over" the funds to a tax-deferred account (*e.g.*, IRA) without suffering any tax consequences. Do ***not*** follow this procedure any more.

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[25] This mainly refers to defined *contribution* plans, since one generally cannot withdraw substantial sums from a defined *benefit* plan.

While the new rules have eliminated various of the arcane fine points of roll-overs,[26] they have added this trap: Any distribution eligible for rollover that is not directly transferred to a trustee for another qualified plan or for an IRA is subject to 20 percent withholding. Some explanation is in order to see why this is as bad as it is.

The rule is *not* just a withholding mechanism; actual taxes are triggered. The entire amount withheld is itself considered a taxable distribution, on which regular income taxes, plus early withdrawal penalties, are assessed. If a 31% bracket taxpayer tried to roll over $100,000.00 by having a check issued, even to be paid to his spouse's IRA the next day, he would actually receive only $80,000.00. Taxes of $6,200.00 would be owed that year on the $20,000.00 withheld, plus a $2,000.00 penalty for early withdrawal. The net cost for holding the funds for a day is therefore $8,200.00, and the $20,000.00 withheld earns nothing during the entire tax year. If the remaining $80,000.00 was indeed rolled over within 60 days, the employee would be entitled to a refund of the remaining $11,800.00 at the end of the tax year.

In other words, to have a transfer *really* be tax-free, the employee *must* arrange for a direct transfer from the tax deferred account to another tax-deferred account without touching the money directly. Any other course of action will have the above consequences. Hardship withdrawals are subject to these regulations (and so must be significantly larger than planned to compensate). Loans do not require such withholding, but any default on repayment converts the loan to a taxable distribution.

If the participant takes the money outside of a QDRO, even to give it to the former spouse under a court order, full tax consequences and the 10% penalty are triggered as to the participant. If a QDRO is used to send the money to the Alternate Payee (or to the Alternate Payee's qualified tax-deferred plan), the "taxable event" is attributed to the Alternate Payee, and there is no 10% penalty.

There has been a common misperception and resulting tax problem with military cases, which was partially resolved by changes going into effect February 4, 1991. For each divorce case prior to that date, the military pay center withheld taxes from the gross retired pay, divided the post-tax amount between the member and the spouse pursuant to court order, and sent a check to each. At the end of each year, the member was eligible to claim a tax credit for amounts withheld on sums ultimately paid to the former spouse, and the former spouse owed a tax liability for any amounts she received.

The "bottom line" of this procedure was to always pay more actual money to the member, and less to the former spouse, than was shown on the face of a simple percentage division of the retirement benefits. The tax problem arose because many former spouses, not receiving a Form 1099 or W-2P, thought the money they received was "tax free," not realizing that it was *their* responsibility to account for, and pay taxes on, all sums they received. *See Eatinger v. Comm.*, TC Memo 1990-310. Many members did not realize that they had a tax credit coming each year (which usually took an accountant to figure out). Most courts were unaware that the effect of their orders was being skewed by application of the tax code which altered the distribution of payments ordered.

The 1990 amendments to the USFSPA, effective for divorces February 4, 1991, and later, addressed all of those problems. The change, embodied at 10 U.S.C. § 1408(a)(4), altered the definition of "disposable pay" so that taxes were no longer taken "off the top" before the retirement

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[26] The "received entirely within one year" requirement, the prohibition on periodic payments, so that any sum received had to be half or more of the account, etc.

benefits were divided between spouses. Both spouses are now sent a W-2P reflecting what they received during the year and allowing for reasonable tax planning, and courts are permitted to divide what is essentially the gross sums of benefits, as they intend.[27]

Pending is Representative Schroeder's efforts to have the redefined "disposable" pay apply to all cases irrespective of the date of divorce. *See* H.R. 2258.

There was a major tax case relating to military retirement benefits decided in 1992 by the United States Supreme Court, but its impact on Nevada residents should be small. In *Barker v. Kansas*, ___ U.S. ___, ___ S. Ct. ___ (No. 91-611, Apr. 21, 1992), the court ruled that states are prohibited from imposing income taxes on military retirees if they do not similarly assess taxes on retirees of their state retirement systems. A similar, earlier decision had prohibited similar discriminatory taxes upon Civil Service retirees. *See Davis v. Michigan Dept. of Treasury*, 489 U.S. 803, ___ S. Ct. ___ (1989). Since Nevada does not have an income tax, the case is probably of interest only if the parties have a multi-state connection and an income tax problem.

One new angle to consider is the granting of a *security interest* in favor of one spouse who is owed sums upon divorce, using the benefits in a retirement plan as the security. The IRS approved of such an arrangement in Private Letter Ruling 9234014 (August 21, 1992), where each of the parties was granted a security interest in the benefits allocated to the other to secure contingent tax obligations. It is unclear what other obligations could be thus secured, but presumably anything normally included under the rubric of "Domestic Relations Order" (i.e., alimony, child support, or community property division) would qualify.[28]

G. **Tools and Assistance**

There are many resources available to assist the practitioner in building QDROs. Mr. Snyder's book, referred to above, has a sample QDRO and some drafting tips. More comprehensive step-by-step guides to drafting QDROs are contained in other texts; four such are: Gary Shulman, *Qualified Domestic Relations Order Handbook* (Wiley 1993); Michael Snyder, *Qualified Domestic Relations Orders* (Clark Boardman Callaghan 1987 & Supp. 1993); *Qualified Domestic Relations Orders* (justPensions, 3600 Cashill Blvd., Reno, NV 89509; (800) 831-3825); and *Retirement Equity Act: Divorce and Pensions* (Divorce Taxation Education, Inc. 1985 & Supp. 1988; DTE, Inc., 1710 Rhode Island Ave. N.W., Washington, D.C. 20036; (202) 466-8204). The Reno firm also provides actuarial expert witness assistance at trial, if needed.

Practitioners are cautioned that QDRO drafting can be a complex venture, replete with traps by omission and commission. **Slavish copying of any form is an invitation to disaster.** Unless the case warrants personal attention in taking care of all contingencies, it might be most economical to enlist expert assistance.

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[27] All problems have not been solved. For technical reasons beyond the scope of this seminar, the amount actually paid to the former spouse may still be less than the amount ordered by the court, but this direct payment limitation under the Social Security law is not a substantive limitation on the jurisdiction of the state courts, which may enforce their orders by other means in appropriate cases.

[28] Special thanks to William H. Cook, Jr., Esq., of New Orleans, LA, for pointing out this information and strategy.

Those who are interested in obtaining further materials as to military-related divorces may want to watch for the upcoming publication by the American Bar Association of: Marshal Willick, *A Lawyer's Guide to Military Retirement and Benefits*, due out (with luck) within the next year (ABA Publications: (312) 988-5555).

IV. **CONCLUSION**

Pension plans have become ubiquitous. It has become increasingly important for domestic relations practitioners to seek out the existence of such assets in each case, to learn all aspects of the relevant plans, and to develop appropriate valuations for those assets. Only then can counsel intelligently negotiate -- or litigate -- their clients' interests in such retirement benefits.

TABLE OF EXHIBITS