

WHEN REMARRIAGE MUDDIES THE WATERS

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QDROs & Surviving Spouse Protection

You have completed your client's divorce and arranged for entry of a Qualified Domestic Relations Order (QDRO), which will award her a portion of her ex-spouse's retirement benefits. Sometime after the QDRO is entered, your client informs you that her former spouse is remarrying. She wonders whether the QDRO will continue to protect her interest in these retirement benefits after her ex-spouse remarries. In response, you quickly pull your office file to review once more the provisions of the QDRO. Whether your client's interest in her ex-spouse's retirement benefits is adequately protected may depend upon whether she has been designated as the "surviving spouse" in the QDRO.

Survivor benefit rules

Federal tax law governing qualified plans provides an automatic survivor benefit requirement, which applies to qualified plans that are required to distribute benefits in the form of a life annuity. Although this requirement does not apply to some qualified plans, all qualified plans are nonetheless affected by the rule. Under the survivor benefit rules, the participant's current spouse at the time the participant retires or, if the participant dies prior to retirement, as of the date of his death, is deemed to be the participant's "surviving spouse." This presumption is important in determining who is entitled to receive the balance of the participant's retirement benefits upon his death. If the participant is remarried at the time of retirement or, if earlier, his death, then his former spouse will not be entitled to receive these benefits, absent a clear designation of the former spouse as the "surviving spouse" in a QDRO. Therefore, a QDRO may

rebut the current spouse presumption if it expressly provides that a former spouse shall retain her rights as the surviving spouse.

Automatic survivor benefit requirements are found in the federal tax rules governing the distribution of qualified plan benefits in the form of a life annuity. Therefore, to have a complete understanding of the survivor benefit rules, a divorce attorney who is preparing a QDRO must also understand how the particular retirement benefits affected by the QDRO are to be distributed.

Pension plans, money purchase, and target benefit plans are required by law to distribute a married participant's accrued retirement benefits in the form of a qualified joint and survivor annuity (QJSA), which pays benefits over the joint lives of the participant and surviving spouse. If a married participant should die before retirement benefits become payable, i.e., the "annuity starting date," his surviving spouse would then receive periodic payments for life in the form of a qualified preretirement annuity (QPSA). An unmarried participant of these plans would receive accrued retirement benefits in the form of a single life annuity that provides periodic payments until the participant's death.

Although profit sharing and stock bonus plans are not required to offer a life annuity form of distribution, and therefore the survivor benefit rules generally would not apply in such cases, these plans must provide that, absent consent of the surviving spouse to the designation of another beneficiary, upon the participant's death, the participant's retirement benefit is payable in full to the participant's surviving spouse.

When designated in a QDRO, a former spouse is treated as the surviving spouse for all purposes relating to the participant's retirement plan. Thus, a former spouse who is so designated will be required to consent to a form of distribution other than the QJSA or to a participant's

waiver of the QPSA in cases where the plan requires those forms of distribution for married participants. As stated previously, in plans that are not subject to QJSA and QPSA requirements, a former spouse who is treated as the surviving spouse is entitled to consent to the payment of the participant's retirement benefits to another designated beneficiary.

Drafting QDROs

Some divorce lawyers mistakenly assume that a plan administrator's approval of a proposed QDRO will ensure that all issues important to the client have been adequately addressed. However, a valid QDRO may, and often does, fail to address the impact of the divorce upon the former spouse's right to receive benefits as the surviving spouse under the qualified retirement plan. Unfortunately, failure to include a survivorship provision in the QDRO often goes undetected until the participant dies or retires, that is, when the survivor benefits irrevocably vest in the current spouse and it is too late to do anything about it.

Courts have ruled that a former spouse who had not been designated as a surviving spouse in the QDRO was not entitled to any further benefits after the plan participant died and the QDRO could not be amended after the participant's death. Dorn v. International Brotherhood of Elec. Workers, 211 F.3d 938 (5th Cir. 2000). Courts also have ruled that a QDRO with respect to the survivor annuity portion of a retirement benefit could not be created in favor of the participant's first spouse when the participant had remarried and started receiving retirement benefits in the form of a qualified joint and survivor annuity. Rivers v. Central and South West Corp., 186 F.3d 681 (5th Cir. 1999).

Divorce attorneys should realize that the designation of a former spouse as the surviving spouse in a QDRO is simply a matter for negotiation by and agreement between the participant and the former spouse. A former spouse who is designated as surviving spouse under a QDRO

may receive as much or as little protection as the parties agree upon, extending surviving spouse treatment to a former spouse for all or some of the participant's benefits under the plan.

In fact, IRS Notice 97-11 provides that a former spouse may be treated as the surviving spouse with respect to benefits accrued through the date of divorce or with respect to all benefits accrued through the participant's retirement. See Appendix §(53). Where the former spouse is treated as the surviving spouse with respect to benefits accrued through the date of divorce, both the former spouse and the current spouse enjoy survivor annuity protection, including the right to consent to the designation of another beneficiary.

Unless one of the surviving spouses later waives the benefit, upon the participant's death the plan would pay two survivor annuities based on the life span of each spouse, the total amount of which would not exceed (on an actuarially equivalent basis) the amount payable to one surviving spouse. When the former spouse is treated as the surviving spouse with respect to benefits accrued through the participant's retirement date, a subsequent spouse of the participant would be denied spousal protection under the survivor benefit rules.

In our opening scenario, we left the divorce attorney as he was examining the QDRO. At this juncture, divorce counsel should first determine whether or not the former spouse has been clearly identified as a surviving spouse in the QDRO. If not, counsel must determine whether the parties have agreed to designate the former spouse as the surviving spouse. Once an agreement on this issue has been reached, the QDRO should be promptly amended to specifically designate the former spouse as the surviving spouse before the plan participant either dies (prior to his retirement) or retires (following his remarriage).

Agreement by parties

When preparing a QDRO, divorce counsel should always ascertain whether the parties have agreed to designate the former spouse as the surviving spouse for survivor benefit purposes with regard to some or all of the participant's retirement benefits. If the parties in their property settlement discussions have not addressed the matter, they should come to an agreement before the QDRO is entered with the court. Ideally, the proposed QDRO would include the appropriate language before it is submitted to the plan administrator for final approval prior to entry with the court.

In any event, due to the potential malpractice risk divorce attorneys face if this issue is not timely addressed, counsel for the former spouse should include this issue on a QDRO checklist, routinely raising it before completing the QDRO to adequately protect the client's interest in the participant's preretirement and postretirement benefits from the reach of the participant's current spouse.