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Dividing PERS Retirement Benefits - There is No "One Size Fits All" Approach Anymore!!

By Clark B. Williams[1]

Introduction

Until recently it was easy to divide PERS benefits in divorce. Before the 2003 Oregon Legislature overhauled the PERS system, it was most common, and also almost always most fair, to simply divide the marital portion of a PERS account in half, and for the "alternate payee" to have a separate account. This is the so-called "up front division method." This division method also serves to best disentangle the parties. This method has been allowed by Oregon law, ORS 238.465, since 1993.

But since 2003 and with the advent of the Individual Account Plan (IAP) and the Oregon Public Service Retirement Plan (OPSRP), dividing PERS benefits is much more complicated.

First, it is important to note that ***every*** PERS member (except a member who terminated employment prior to 2004) now has an IAP account. The IAP account is derived from a contribution by the government employer equal to 6% of the member's compensation each year, starting in 2004, plus earnings on those contributions each year. Many PERS members now have IAP balances exceeding $30,000. The IAP is in addition to the member's benefits in Tier One, Tier Two or OPSRP. So every PERS member has ***two*** benefits to divide, potentially, in a divorce. The IAP is a different system, and the division is handled separately.

Second, new PERS regulations effective January 1, 2011 must be followed. In particular, new template forms must now be attached to any divorce judgment or supplemental order dividing PERS benefits.[2] The template forms do not replace the need for a judgment or court order dividing benefits specifically in compliance with ORS 238.465. Rather, these template forms are ***in addition*** to the judgment or court order and must be completed and attached thereto as exhibits. Further, if only one of a member's two PERS benefits are being divided (e.g., a member's Tier One account is being divided but the member is keeping the IAP account), the judgment or order must still incorporate a PERS template form specifying that the benefit being retained is "free and clear" of any claim by the former spouse. So in every case at least two of these forms must be attached to the judgment or court order, one for the IAP and one for the Tier One, Tier Two or OPSRP benefit, as the

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case may be. PERS will now reject any judgment or order that does not include these forms.

Finally, no longer is it universally true that the "up front division method" is the best, or even fairest, way to divide PERS benefits. Depending on which party you represent, and whether the member is "Tier One" or "Tier Two ," your client may be better served to divide PERS benefits at retirement using the "time rule."[3] That dichotomy will be the focus of the remainder of this article.

This is the first of two articles addressing how best to divide PERS benefits in view of these changes. This first article will focus on dividing Tier One and Tier Two benefits. The second article, to be published in the June edition of the Family Law Newsletter, will focus on dividing IAP accounts and OPSRP benefits.

Understanding Tier One and Tier Two

To best represent your client in dividing PERS benefits, it is important first to understand how the benefits are earned and calculated, and when and how they are paid. I will discuss Tier One and Tier Two separately, because they are very different. In fact, depending on who you represent, the best division method for your client is often *opposite* for Tier One vs. Tier Two!

Tier One Benefits.

Any employee first employed in a PERS-covered position prior to January 1, 1996 is in Tier One. Tier One employees will receive a lifetime monthly pension benefit (or the lump sum equivalent) equal to the *largest amount* produced these three alternate methods:

1. *Full Formula.* 1.67%[4] x years of service x FAS ("final average salary"). So, for example, a school teacher who retires with 30 years of service and a final average salary of $5,000/month will receive a benefit of 1.67% x 30 years x $5,000 = $2,500/month under this method.

2. *Money Match.* The member's PERS account, doubled by the "money match" and then multiplied by an annuity factor that is based on the life expectancy of the member. For a member at age 58, the annuity factor is $7.96/$1,000. Therefore, for example, if the school teacher in the above example has an account balance of $175,000 at age 58 and then retires, the teacher's retirement under this option is $175,000 x 2 x $7.96/$1,000 = $2,786/month.

3. *Formula Plus Annuity*. For members participating in PERS since before August 21, 1981, a third formula applies which is a combination of the first two. The formula is: 1% x years of service x FAS ***plus*** the account balance (not doubled) times the annuity factor. In the school teacher example above, the formula would be 1% x 30 years x $5,000 ***plus*** $175,000 x $7.96/$1,000 = $2,893/month. In situations where the first two formulas yield a result that is close to each other (as in this example), then this third method (for those in the system before August 21, 1981) yields the best result.

The Full Formula method is a traditional defined benefit formula. The Money Match method is a defined contribution formula. The Formula Plus Annuity method is a blend of both the first two. So whether PERS is behaving as a defined benefit plan or a defined contribution plan is entirely dependent on the prevailing method. This is important to recognize.

Other Factors. The following additional factors are important for understanding PERS Tier One benefits:

A. A member's PERS Tier One account balance is the cumulative total of an annual contribution equal to 6% of the member's compensation through 2003 (after which time these contributions have been made to the member's IAP account) plus earnings on that balance each year.[5]

B. The earnings added each year are determined by the PERS Board. Each member has a "regular account" and, if the member chooses, also a "variable account." The "regular account" is invested more conservatively, and ***very*** importantly it has a minimum earnings ***guarantee*** of 8% per year.[6] Again, the account balance at any time represents only half (or less) of the total value of the account because the account will be "matched" by an equivalent employer contribution at retirement.

C. The 1990's produced very strong earnings for PERS accounts. For the five years 1995 - 1999, inclusive, PERS regular accounts earned an average of 15.5% ***per annum*** and variable accounts earned 26% ***per annum***. The result was that the accounts of nearly all PERS members ballooned to the point that the Money Match method prevailed over the Full Formula method nearly every time. According to "PERS By The Numbers,"[7] nearly 90% of the retirees between 1999 and 2004 retired under the Money Match formula, and with an average retirement income of over 90% of final average salary, or FAS.

D. Years of Service after 2003 ***still*** count under the Full Service formula, even though no new contributions are being made to member Tier One accounts. The Money Match method continues to predominate. According to PERS by the Numbers,"[8] over 60% of retirees in 2007 (the latest year available) retired under the Money Match formula even though no new contributions have been made to Tier One accounts since 2003. However, that trend is reversing. Tier One members who are still many years from retirement may eventually retire under the Full Service formula, particularly those who have significant salary increases after 2003.

E. In an "up front division," PERS establishes a separate "alternate payee's" account for the portion of the Tier One account awarded to the former spouse. Because of this, the alternate payee's benefits are limited to the Money Match method. This is true even if the member eventually retires under the Full Formula method. This is very important to understand. Also, the former spouse's account is invested strictly in the "regular" account, even if derived partially from the member's "variable" account.

F. Tier One members can retire at age 58,[9] or at any age with 30 years of service. Tier One members can retire as early as age 55[10] with a reduction in benefits for early commencement. Benefits are measured in monthly

payments for the life of the member (Option 1). The member can elect survivorship options (Options 2, 2A, 3 or 3A) with another spouse or person with a lower actuarially determined monthly benefit, and/or a partial or total lump sum benefit.

G. All monthly benefits are increased annually by the increase each year in the Consumer Price Index ("CPI"), but limited to 2% per year.

Implications for Dividing Tier One Benefits.

Based on the foregoing, it is apparent that a Tier One Member's best retirement accumulation years are those already in the rear view mirror. In fact, in many cases the member's account balance is still so large, relative to years of service and salary, that the Full Formula method will never catch the Money Match method before retirement. In those cases, the additional years of service from now until retirement count for nothing in terms of Tier One benefits! The member will receive the same benefit if he or she quits now than if the member continues to work until retirement. This is a common phenomena for career Tier One members now in their 50's.

For example, here is a "live case" on my desk right now (I will round off the dates and numbers). Husband has been a Tier One PERS member since 1983, now age 51, with seven years to projected retirement at age 58 in 2018. He earns $75,000/year and has a Tier One account balance of $215,000 as of December 31, 2010. The PERS on-line estimator11 projects that Husband will retire at age 58 with an account balance of $368,000, to be doubled by the Money Match to $736,000, and which will annuitize at $5,845/month. Also according to the estimator, even if Husband's salary increases to $100,000/year by his retirement in 2018, the Full Formula method would yield only $4,772/month. So the Money Match will be the prevailing formula for him even seven years from now. Husband's salary would have to increase to at least $123,000/year by his retirement for the Full Formula method to overtake the Money Match method, which is unlikely in this economy. So unless that happens, Husband's continued service from now until retirement does not increase his final Tier One benefit by one dime. And remember, no contributions have been added to Husband's Tier One account since 2003. This means that for his 35-year career, from 1983 to 2018, ***the entirety of his Tier One benefit*** was earned in the first 20 years of his career, from 1983 thru 2003. His last 15 years from 2004 thru 2018 count for nothing in terms of Tier One benefits!

The divorce will occur in 2011, and I represent Wife. So it is in her benefit, clearly, to use the "up front" 50-50 division. This will give her half of ***all*** Husband's benefits at his retirement. And I can argue, easily, that this is appropriate under these circumstances. Her half of the account balance at retirement will be $368,000, and she would then have her own payment options including lump sum. And this would be in addition to half of Husband's current IAP account (now about $28,000, so her half is an additional $14,000).

But if I represent the Husband, then I would explain to him that to use an "up front" division is to give away half of the best years. I would explain that it would be better to use the "time rule" to keep the account intact from now until retirement and ***then*** divide it on a prorated basis. Under the time rule, wife's share of the total benefit would be $736,000 x 28 years to date ÷ 35 years total service at retirement x 50% = $294,400. This represents a savings for Husband of $73,600 at retirement. Wife would get 40% of the total benefit, not 50%. The legal basis for this approach is the ***Kiser*** case12, which holds that the "time rule" applies to all defined benefit plans. And in the first instance, PERS is a defined benefit plan. The counter-argument, however, is that in this case where the Money Match is the prevailing method; PERS is performing as a defined contribution plan. And therefore it is appropriate to divide the account in half now, as with all defined contribution plans.

Therefore, when representing a Tier One member, particularly one who is late in his or her career, consider carefully whether it is better to argue for the use of the "time rule" to divide the account balance at retirement, rather than at the time of divorce, so that the member keeps a larger share of his or her eventual Tier One benefit. This is true even in most cases where the Full Formula will catch up to the Money Match in the years immediately before retirement, since the time rule will still normally yield better result for the member. But to be sure, it is best to run the actual numbers of each case thru the PERS on-line estimator.

And if you use the time rule to divide at retirement, then the judgment or supplemental order should address what happens on either death before retirement. And at retirement, if the opposing party is much older or has a shortened life expectancy, then you might consider also having the judgment or order mandate an Option 2 (100% survivor) benefit and to split the payments rather than to split the account. That way, on the first death then the survivor (hopefully your client) can then receive both halves of the benefit for the rest of his or her life.

Tier Two Benefits.

A PERS member is in Tier Two if he or she was first employed between January 1, 1996 and August 28, 2003. Employees first hired after August 29, 2003 are in OPSRP. The benefit structure for Tier Two employees is similar to Tier One. But there are enough differences to turn the typical approach for dividing Tier Two benefits 180 degrees from that for Tier One, as explained below.

These are the basic differences between Tier One and Tier Two

1. The normal retirement age is 60, not 58, for general service (not police or fire) employees.

2. There is no 8% interest guarantee as with Tier One regular accounts. Therefore, for example, in 2008 Tier Two accounts lost over 27% while Tier One regular accounts gained 8%.

3. The retirement formulas are just the Full Formula

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The purpose of this Newsletter is to provide information on current developments in the law. Attorneys using information in this publication for dealing with legal matters should also research original sources and other authorities. The opinions and recommendations expressed are the author's own and do not necessarily reflect the views of the Family Law Section or the Oregon State Bar.

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Publication Deadlines

The following deadlines apply if a member wants an announcement or letter included in the newsletter.

Deadline	Issue
May 15, 2011	June 2011
July 15, 2011	August 2011
September 15, 2011	October 2011
November 15, 2011	December 2011

method and the Money Match method. There is no Formula Plus Annuity method.

Contributions to Tier Two accounts were made, at most, for only eight years, from 1996 thru 2003. Contributions to Tier Two accounts were frozen after 2003, just as for Tier One accounts, with the 6% contributions after 2004 being redirected to new IAP accounts for each Tier Two member. And because of relatively poor earnings results for Tier Two accounts in the last decade, Tier Two accounts are still relatively small.

On the other hand, as with Tier One, continued serviced by Tier Two employees still count under the Full Formula method, which is the same method as for Tier One. As a result, with the passage of time since 2003, Tier Two retirements are increasingly under the Full Formula method, and that trend will only get stronger with time.

Implications for Dividing Tier Two Benefits.

Tier Two employees are often younger, with a longer horizon to retirement. In most cases, the account balance represents only a small fraction of the total retirement likely to be paid to the Tier Two member. An "up front" division limits the alternate payee to the less valuable Money Match method, as with Tier One. And so using an "up front" division method tends to short-change the alternate payee and to preserve the more valuable Full Formula benefits for the member.

I will illustrate with another "live" case on my desk today. Husband is the Tier Two member, having entered PERS on April 1, 2001. His Tier Two account balance was only $13,000 as of December 31, 2009. It is small because it represents contributions just for nine months in 2001 and for the years 2002 and 2003. Again, no new contributions have been made to this account since 2003. Yet as of 2011, Husband has ten years of service under the Full Formula method. Husband is already age 58 and may retire soon. His salary is approximately $55,000 per year. The parties are divorcing now. All Tier Two service is marital.

According to the PERS on-line estimator, were Husband to retire now, the Full Formula method would prevail and award husband a monthly pension of $714/month. But the Money Match method would produce only $224/month. In other words, the value of the account balance is only one-third of the value of the likely benefit based on salary and years of service.

I represent Wife in this case. If I were to divide the account in half, I would limit Wife to an account that would produce only $112/month to her. And Husband would retain the other $602/month. Therefore, I am proposing to use the "time rule" to divide the benefits. And appropriately so, since PERS in this instance is performing as a defined benefit plan. This way, I will insure that wife gets the equivalent of half of the total benefit, or $357/month. This is an additional $245/month to her for the rest of her life, with CPI increases. And she is just 58 herself, so this could mean a lot to her over the years.

Further, because of Husband's poor health habits and poor genetics, I am drafting the order to mandate that the

entire benefit be paid in the form of Option 2, a joint and 100% survivor annuity, which will yield a lower total payment of $632/month. Payments will be split equally for as long as both live. But if Husband dies first as expected, then Wife will receive both halves thereafter for as long as she lives. And in this case, the extra PERS benefits at that time will partially compensate her for loss of spousal support due to his death.

This approach is 180 degrees from the approach taken for Wife in the Tier One example, above.

Conclusion

No longer is it sufficient to blindly divide PERS Tier One and Tier Two benefits "up front" at divorce. Practitioners should take time to understand the particular PERS benefits in each case, whether Tier One or Tier Two and the account balances and service credits earned, and to estimate whether the Full Formula or the Money Match method will ultimately prevail at retirement. Practitioners may also need to consider the ages of each party, their likely retirement dates, their relative health and the likelihood that one will survive the other. A loose rule of thumb when representing the alternate payee is to recommend an "up front" division if member is Tier One and a "time rule" division if the member is Tier Two . And the rule of thumb is exactly the reverse when representing the member. But each case should be evaluated on its own merits.

Clark B. Williams

Clark grew up in northern California. He received his B.S. degree from the University of Washington in 1976, and his J.D. degree from Willamette University College of Law in 1979, graduating tenth in his class. He served one year in Portland as a law clerk for U.S. District Judge Robert C. Belloni. He returned to Salem to join the law firm now known as Heltzel, Williams, Yandell, Roth, Smith, Petersen & Lush, P.C., becoming a partner in 1984.

Clark practices exclusively in the areas of business, tax and estate planning, with a particular emphasis on retirement plans. Clark has drafted and processed over 2,000 qualified domestic relations orders (QDROs) of all types for lawyers throughout Oregon, and has testified as an expert witness on numerous occasions. He has also been a speaker on the subject of QDROs at the Oregon Family Law Conference and at the Oregon Judicial Conference. In 1993, Clark was the principal author of Senate Bill 210 sponsored by the Family Law Section, which became law and as is now codified as ORS 238.465, the principal statute governing the division of PERS benefits in divorce.

Clark, and his wife, Julie, live in Keizer and have four children and two grandchildren.

[1] Special "thanks" go to Paul Saucy, Esq. and to Peter Ungern, Manager of the PERS Specialty Services Section, for their contributions in the writing of this article.

[2] The forms can be found at http://www.oregon.gov/PERS/MEM/docs/forms/046fs.pdf?ga=t

[3] The "time rule" is also referred to as the "coverture fraction." It is an arithmetic way of determining each spouse's interest in the plan benefit by separating out the premarital or postmarital portion of the benefit by multiplying the marital share (usually 50%) by a fraction. The numerator of the fraction is usually the number of years during the marriage that the employed spouse earned credit for service under the retirement plan. The denominator is usually the total years of service under the retirement plan to the point of retirement or termination of employment. For example, 10 years of marriage divided by 20 years of service up to the point of retirement (the last 10 years being postdivorce) multiplied by the marital share (usually 50%) equals the former spouse's share of the benefit. *See Richardson*, 307 Or 370, 378–379, 769 P2d 179 (1989) This formula has the effect of treating each year of service during the member's career as having equal credit in determining the former spouse's share, even though the benefits may not have accrued uniformly during the employee's career. That is why the Court of Appeals in *Kiser*, ___ Or.App. ___ (2001) referred to the "time rule" as the "straight line method."

[4] 2.0% for "police or fire" employees

[5] Originally the contribution came from the member's after-tax salary (hence, called the "employee contribution") but since the early 1980's and as a result of collective bargaining most employee contributions are "picked up" by the government-employers.

[6] The 2003 Oregon Legislature tried to repeal this 8% guarantee, prospectively, but the Oregon Supreme Court ruled that it was constitutionally protected.

[7] http://www.oregon.gov/PERS/docs/general_information/bythenumbers.pdf?ga=t

[8] *Id.*, at p. 7

[9] Age 55 for "police or fire" employees

[10] Age 50 for "police or fire" employees

[11] http://apps.pers.state.or.us/benefitestimator/bencalc_step1_start.asp

[12] Cited in footnote 3.

Child Support Guidelines Review

By Jean Fogarty

By the time this issue goes to press, the 2011 Child Support Guidelines Advisory Committee will have begun reviewing the formula used to determine all Oregon child support awards. Since amending the guideline rules in 2010, the Oregon Child Support Program has compiled and analyzed comments and observations from practitioners, parents, and program staff. The Program has identified three major issue areas for review:

- Medical support (health insurance, cash medical, and cost sharing)
- The parenting time credit
- Calculating support for children attending school (ORS 107.108)

The Guidelines Advisory Committee is composed of members of the bench, the private bar, advocacy organizations, and the Child Support Program, and represents a broad spectrum of expertise and stakeholder interests. The Committee will meet throughout 2011 to do the hard work of evaluating these issues (and a number of others) and offering recommendations to the Child Support Program Director to refine and improve the guidelines. The Program will implement the new guideline rules in 2012.

The Child Support Program welcomes your questions and suggestions throughout the guidelines review process. You can reach the Program by email at guidelinesquestions@doj.state.or.us, or by mail at Oregon Child Support Program, 494 State St, Suite 300, Salem, OR 97301.

Submitted by:

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Editor's Note: these are brief summaries only. Counsel should read the full opinion. A hyperlink is provided to the on line opinion for each case.

OREGON COURT OF APPEALS

Parent-Child Relationship; Visitation

Dylan M. Digby and David Meshishnek, 241 Or.App. 10 (2011) A139448

http://www.publications.ojd.state.or.us/A139448.htm

Trial Court: Hon. Carol E. Jones, Yamhill County Circuit Court

Brewer, C. J.

Appellants appeal from a judgment awarding petitioners, the Digbys, visitation with two minor children on the grounds that petitioners had established a qualifying "ongoing personal relationship" with the children under ORS 109.119(10)(e). Appellants argue that the trial court erred in awarding visitation on that basis because petitioners had not alleged an ongoing personal relationship in their petition, and instead had alleged only a "child-parent" relationship under ORS 109.119(10)(a). The trial court found that, by alleging a child-parent relationship petitioners had adequately alleged an ongoing personal relationship because an ongoing personal relationship is essentially "lesser included" of a child-parent relationship.

Held: The trial court erred in awarding visitation on the basis of an ongoing personal relationship. The statutes defining "child-parent" relationship and "ongoing personal relationship" have separate requirements that must be shown by different burdens of proof, thus, an ongoing personal relationship is not "lesser included" within an allegation of a child-parent relationship. Reversed. CA 02.23.11

Property Division

Donald Alan Gagliardi and Lawanda Johnette Gagliardi, 241 Or.App. 293 (2011) A145284

http://www.publications.ojd.state.or.us/A145284.htm

Trial Court: Hon. Susie L. Norby, Clackamas County Circuit Court

Schuman, P. J.

Husband appeals from a judgment dissolving the parties' 15-year marriage, assigning error to the trial court's division of property and to the award of child support.

Held: Husband has not preserved his assigned errors. Affirmed. CA 03.02.11

Stalking Order

Stephen Mathew Gunther v. Mary Rose Robinson, 240 Or.App. 525 (2011) A142981

http://www.publications.ojd.state.or.us/A142981.htm

Trial Court: Hon. Michael J. McShane, Multnomah County Circuit Court

Ortega, P. J.

Respondent appeals after the trial court entered a permanent stalking protective order against her.

Held: Petitioner failed to establish that respondent engaged in two qualifying contacts during the two years before the filing of the petition for an SPO. Reversed. CA 02.02.11

Spousal Support

Brian James Morrison and Donna C. Morrison, 240 Or.App. 656 (2011) A139817

http://www.publications.ojd.state.or.us/A139817.htm

Trial Court: Hon. Ronald D. Grensky, Jackson County Circuit Court

Haselton, P. J.

Wife appeals a general judgment of dissolution, contending that the trial court erred in setting the amount and duration of various components of its award of spousal support to wife, and husband cross-appeals the supplemental judgment, contending that the trial court erred in awarding wife her attorney fees.

Held: (1) The Court of Appeals rejected husband's contentions on cross-appeal without discussion. (2) On de novo review, ORS 19.415(3) (2007), the court concluded that wife is entitled to compensatory support, ORS 107.105(1)(d)(B), and indefinite maintenance support, ORS 107.105(1)(d) (C). Accordingly, the court modified the judgment on appeal and affirmed on cross-appeal. On appeal, reversed and remanded for entry of judgment (1) awarding wife compensatory spousal support of $2,000 per month for eight years and (2) maintenance spousal support of $5,000 per month for three years, $4,000 per month for the next three years, and $3,000 per month thereafter; otherwise affirmed. Affirmed on cross-appeal. CA 02.16.11

Paul Jeffrey Finear and Laurie Lynnette Finear, 240 Or.App. 755 (2011) A138783

http://www.publications.ojd.state.or.us/A138783.htm

Trial Court: Hon. Daniel Leon Harris, Jackson County Circuit Court

Ortega, P. J.

Wife appeals from a dissolution judgment in this 23-year marriage, contending that the trial court erred in determining that husband should retain an entire inheritance acquired during the marriage and also erred in stepping down support and not awarding indefinite spousal support. Husband cross-appeals, contending that the trial court awarded excessive spousal and child support.

Held: Considering the length of the marriage, wife's absence from the labor market while raising and home-schooling the parties' children, her age and lack of meaningful work experience and skills, and the disparity in the parties' incomes and earning capacities, it is just and equitable that wife be awarded indefinite spousal support. Although the initial support level awarded by the trial court is just and equitable, in the absence of evidence that wife's earning capacity will increase over time, it is not appropriate to step down spousal support. In all other respects, the judgment of the trial court is affirmed. On appeal, dissolution judgment modified to award wife indefinite spousal support of $1,100 and otherwise affirmed; affirmed on cross-appeal. CA 02.16.11

Note on Opinions Reviewed:

The Editor tries to include all the Family Law related decisions of the Oregon Appellate Courts in these Notes. Some cases do not have holdings that have legal significance however they are included to insure none are missed.