



Protecting Spousal Rights in Divorce

ERISA Covered Qualified Retirement Plans



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Topics included.

- How differences among plan types affect spousal rights and requirements to divide pension assets in divorce
- Methods of allocating -- Shared payment v Separate Interest
- Impact of qualified plan requirements and plan provisions
- How these issues interact with QDRO rules.


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Plan Classification and Structure

- ▶ Plans may be classified in various ways
 - ▶ ERISA Covered or not ERISA Covered
 - ▶ Qualified or non-qualified
 - ▶ Defined contribution (DC) or defined benefit (DB)
 - ▶ Type of DC Plan--Different types of DC Plans have specific requirements that may affect DRO and spousal rights
 - ▶ Nature of plan sponsor--Single/multiemployer; government/private

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QDRO/spousal rights are affected by classification of plan.

- ▶ Is the plan subject to ERISA QDRO and preemption rules?
- ▶ Does the order divide an account or a stream of benefit payments?
- ▶ When can distributions be made under law?
- ▶ Does the plan provide a QJSA/QPSA?

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QDRO/spousal rights are also affected by plan terms.

- What payment options are available under the plan? Are any DB options subsidized?
- Does the DC plan provide for loans, hardship distributions, investment control by account holder?
- Does the plan provide for forfeiture of employer provided benefits upon death?
- Does the plan have any “defaults” – rules that apply unless DRO provides otherwise?
- What is the “earliest retirement age” for the plan?

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ERISA Coverage/Qualified Plans

- Plans subject to ERISA QDRO and Preemption rules
 - Qualified plans – subject to detailed IRS requirements
 - 403(b) annuities for educational and charitable organizations
- Plans not subject to ERISA QDRO and Preemption rules
 - 457 plans
 - 403(b) annuities for government and church organizations

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Defined Contribution (Qualified/ERISA Covered)

- Profit-sharing plan (including 401(k) and stock bonus)
 - May provide for loans, hardship distributions, control of investments by account holder
 - In-service distributions permitted
- Money purchase plans--Some rules similar to DB plans
 - QJSA is default option for married participant
 - Limited in-service distributions
 - May provide for loans, control of investments by account holder
- Employee Stock Ownership Plan (ESOP)
- Plan documents must state the type of plan.

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Defined Contribution(Nonqualified)

- 403(b) annuities
 - May permit plan loans, hardship distributions
 - ERISA Covered – sponsored by educational and charitable organizations
 - Not ERISA Covered – sponsored by government and church organizations
- 457 plans
 - Not ERISA Covered

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Defined Benefit (Qualified/ ERISA Covered)

- Accrued benefit is annual benefit commencing at Normal Retirement Age
 - Benefits paid in lifetime income stream; QJSA is default option for married participant
 - Typically offer benefit payment options
 - May include ancillary benefits such as life insurance
 - Limited in-service distributions
- Traditional - Definitely determinable benefit formula
- Hybrid
 - Cash Balance-notional (not real account); additions by formula
 - Variable Annuity Plan – benefits fluctuate with markets
 - Pension Equity Plan

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Why do Payment Options matter?

- DB Plans and many DC plans offer multiple payment options.
 - DB Plans and some DC plans—QJSA/QPSA is the default option for married participant unless waived with spousal consent.
- Options take effect on Ps "annuity starting date" (ASD)
- Options typically cannot be changed after ASD unless provided by plan.
- DB Plans may subsidize some payment options (more valuable).
- DB and some DC Plans, beneficiary cannot be designated before choice of payment option on ASD.
- If DRO specifies payment option, it must be consistent with plans terms.

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Qualified Plan Rules affect QDROs and Spousal Rights

- QJSA/QPSA
- Spousal consent
- Annuity Starting Date
- Assignment/alienation of benefits

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Qualified Joint & Survivor Annuity (QJSA); Qualified Pre-retirement Survivor Annuity (QPSA)

- DB Plans and some DC Plans –default option for married participant unless waived with spousal consent.
 - DC plans provide lifetime benefit by purchasing annuity with all or part of account balance.
- Spouse on ASD retains QJSA or consent rights to alternate form/beneficiary unless QDRO provides otherwise.
- Plans may have multiple J&S options
 - Plan must designate “qualified” J&S Option if more than one.
- Plan may require 1 year of marriage before J&S option is available.
- ERISA prohibits only J&S option with APs subsequent spouse but some plan options may permit J&S with children, etc.

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Which DC Plans are subject to the Survivor Annuity Requirements


- DC Plans subject to minimum funding rules of Code – Money Purchase Plans.
- All other DC Plans **unless** –
 - Plan provides that P nonforfeitable accrued benefit is payable in full upon Ps death to surviving spouse unless waived with spousal consent;
 - P does not elect a life annuity;
 - Plan is not a transferee or offset plan.
 - The benefit must be available to surviving spouse within a reasonable period of time (generally 90 days);
 - Account payable to surviving spouse is adjusted for gains and losses occurring after death of P in accordance with rules applicable to other distributions.

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What is the Annuity Starting Date (ASD) and Why is it Important?

- ASD is first day of first period **FOR** which benefits are payable.
 - QDRO before Ps ASD can provide AP separate interest; after P's ASD, limited to shared payment unless plan permits change of option.
 - Options are elected at ASD; most plans do not permit change of payment options after ASD.
- Determines whether benefit to surviving spouse is paid as QJSA or QPSA.
- Other plan rules may be affected by ASD
 - Additional accruals following return to work may require separate option election and consent.
 - DB plans may provide for "retroactive annuity starting date" (RASD) which may affect which spouse must consent
- ASD but not disclosure and consent rules apply to AP benefits.


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IRS rules on assignment/alienation of benefits

- Coordinates Code requirements for qualified plans with QDRO rules.
- States QDRO cannot provide the alternate payee with a greater right to designate a beneficiary for the alternate payee's benefit amount than the participant's right.


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ERISA Pre-emption: state/local requirements cannot conflict with plan

- Plan rules control benefits to AP except as permitted in ERISA §206(d)(3).
- Familiarity with rules of plan is critical. Examples of problems—
 - Designation of beneficiary
 - When benefits to AP may be distributed; earliest retirement age.
 - What options are available to AP
 - Whether option elected at ASD may later be changed.
- QDRO may not modify plan rule unless provided by law.

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Qualified Domestic Relations Orders: Important Definition

- Domestic Relations Order
 - Functional definition—need not be separate order
 - Some plan obligations are triggered by receipt of a DRO—provide procedures, escrow
 - DRO provides some protections for spouse even if it is defective
 - In contrast, unsigned order even if pre-approved by plan provides NO legal protection to spouse.

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Qualified Domestic Relations Orders: Requirements

- QDRO must clearly specify—
 - Name/address of P and AP.
 - Amount/percentage of Ps benefit to be paid to AP or manner in which determined.
 - Number of payments or period to which order applies.
 - Each plan to which order applies.
- DOL, relying on Legislative History, suggests strict compliance is not required but plan could require specificity.

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Amount or Percentage: Shared Payment Allocation Method

- Allocates to AP a portion of each benefit payment to P; "if, as and when".
- AP does not receive payment unless P receives payment
- Must specify when AP's right to receive share begins and ends.
- APs rights end upon earlier of death of P or death of AP.
- APs rights also end if Ps benefits are suspended or terminated
- Must be used if Ps benefits have commenced
- May be used before P's benefits have commenced.
- May be used for payment of child support arrears from DB plan which is limited time/amount.

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Amount or Percentage: Separate Interest Allocation Method

- Awards AP a separate right to a portion of Ps benefit or account to be paid at a time and/or in an option different from Ps benefits.
- Must specify amount/percentage of Ps benefit awarded to AP or manner in which amount/percentage is determined.
- For DC Plans establishes separate account for AP over which AP may exercise rights of P (e.g., time of payment, form of payment, loan, investment control).
- For DB Plans should address APs right to share in early retirement subsidies or future benefit increases.
- Should address what happens to APs separate interest if P or AP dies before Ps/APs benefit commences.
 - Code permits forfeiture of benefit derived from employer contributions

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Number of Payments; Name of Plan

- Number of payments/time period – typically defined by commencement date and benefit option or APs right to elect commencement/benefit option
- Name of Plan– plan sponsor may have more than one plan with a similar name.

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QDRO Cannot

- Require plan to provide any type/form/option not otherwise provided by plan.
 - But providing for payment before Ps retirement at “earliest retirement age” is OK
 - Any payment option under plan (or APs right to elect) is OK but NOT J&S benefit with APs subsequent spouse
 - Plan may have J&S options with children as beneficiary so do not broadly exclude all J&S be
- Require plan to pay increased benefit on basis of actuarial value.
- Require plan to pay benefits to AP that were awarded to another AP under prior QDRO.

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Type or form of benefit; earliest retirement age"

- Plan terms important for both issues if DRO will specify benefit and timing.
 - Provision for election by AP at/after "earliest retirement age" and in any type/form/option provided by plan avoids a potential error
- If APs DB benefits commence at "earliest retirement age" before Ps retirement, APs benefits may NOT include any early retirement subsidy
 - DRO should provide for recalculation to include subsidy for AP if P subsequently retires with subsidy.
 - State how subsidy is to be allocated.

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Increased Benefits Determined on Basis of Actuarial Value

- Plan rules describing actuarial adjustments and subsidies are important.
- DRO provisions modifying plan actuarial adjustments, subsidies could violate this rule.
- If DRO will shift cost of actuarial adjustment, be sure it is done correctly.

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Timing Issues: Subsequent DROs

- Subsequent DRO between same parties that modifies prior QDRO is OK IF the two orders taken together would still satisfy ERISA requirements.
 - AP must still be awarded portion of benefit or DRO does not satisfy ERISA definition and second DRO is preempted.
- Subsequent DRO between different parties
 - DRO may assign benefits to subsequent AP from benefits remaining to P under prior QDRO.

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Post Death DROs

- DRO is not disqualified SOLELY because it is issued after Ps death.
 - BUT Ps employer provided benefit may be forfeited upon death so no benefit can be allocated
- If P remarried before death and before DRO is issued, subsequent spouse or a beneficiary may be receiving survivor benefits.
 - Plan cannot be required to change benefit option in effect unless plan rules provide for this.

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Orders after Ps Annuity Starting Date

- DRO cannot require a change in benefit option unless plan terms provide for this.
- DRO after annuity starting date is typically shared payment

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DRO Preparation Issues and How to Address Them

- Plan not willing to provide documents or information or concern that P might seek benefit distribution after divorce but before DRO can be prepared.
 - Submit divorce decree/property settlement agreement to plan. If it has any provisions re allocating benefits plan must process the order and provide its procedures. Ps benefits would be escrowed.
 - Obtain order prohibiting distribution Ps benefits pending DRO
- Limited information re benefit payment options offered by plan
 - Use general language that gives AP right to choose from among options. Do not exclude all J&S options—only with subsequent spouse.

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DRO Preparation Issues and How to Address Them

- Inconsistent terms; lack of clarity
 - Draft precisely. Do not cut and paste from models without reviewing the whole. If plan documents are available make certain DRO is consistent with plan.
- Provisions not required by ERISA for QDRO but important to include
 - What happens when P/AP die.
 - Provide right to manage APs account in DC Plan
 - Address increases/decreases in DB benefits
 - Address subsidies in DB plans

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Common Problems that Disqualify a DRO

- Language inconsistent with type of plan, e.g., awarding portion of an account in a DB plan.
- Identity of plan unclear.
- DRO provides that AP may designate beneficiary to succeed to APs interest if AP dies before benefits commence.
 - Not typically permitted by DB plan but may be provided by DC plan.
- DRO combines elements of shared payment and separate interest in a way that cannot be administered by plan.
- DRO includes provisions that cannot be administered together e.g., providing AP may choose when benefits commence but also providing APs benefits commence when Ps benefits commence

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Common Problems that Disqualify a DRO


- Order awards AP a separate interest plus survivor benefits based on some or all of separate interest.
 - DRO that awards separate interest plus survivor benefits as alternative if separate interest benefits are forfeited is OK.
- Order provides APs benefits will commence when provided by plan but plan does not state
- Order awards AP portion of benefits being paid to beneficiary after Ps death.
- Order requires APs benefits to commence when Ps benefits commence but plan has no obligation to monitor Ps benefits and automatically commence APs benefits or notify AP of Ps retirement.

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Common Problems that May Prejudice APs Rights

- Failure to promptly obtain entry of preapproved unsigned order. If P retires before signed order is submitted, separate interest in unsigned order will be unavailable.
- Revised order not submitted in time to obtain escrowed benefit for AP.
- Divorce decree is silent re pension assets, subsequent DRO. No subsequent DRO is prepared. P submits divorce decree when P retires. Plan does not hold benefits because it is unaware of APs interest.

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Summary

- ▀ Identify plan classification; rules that apply.
- ▀ Review plan documents
- ▀ Draft DRO consistent with classification, plan terms, ERISA §206(d)(3).
- ▀ For ERISA covered plans, only ERISA rules matter for QDRO status.