

Women and Divorce: The Perils of Pension Division

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I. INTRODUCTION

A sizeable percentage of marriages end in divorce. Upon divorce, most states pursue fairness and even-handedness in the sharing of marital assets through either community property or equitable distribution statutes.¹ For most families, the two

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most valuable marital assets are equity in the family home and the marital component of a pension plan or plans.² Unlike homes, which can be sold, or for which comparable sales generally provide reasonable yardsticks for valuation, determination of the fair market value of a common class of pension plans can be a complex exercise in forecasting, and can result in widely varying appraised values. Case law contradictions among the states and, indeed, within individual states, reflect this difficulty.

While not necessarily required under all circumstances, there is a presumption in divorce law that, absent evidence to the contrary, an *equal* division of property is *equitable*.³ Hence, when a family-owned home is sold for division purposes, one half of the net proceeds may be allocated to each ex-spouse; for example, where there are 200 shares of IBM stock, each party to the marriage would normally receive 100 shares. Furthermore, were one spouse to retain sole possession of the home or the stock, the appraisal of the fair market value of either asset may be obtained to determine the required compensatory payout of other assets to the second spouse.⁴

With pension assets, division is also "simple" if the pension plan is a *defined contribution* plan, in which case the accumulated dollar value may be *accurately* divided into equal "shares," even if one spouse keeps the plan and pays the court-decreed equal share of the plan's dollar value to the other (that payment made at

antitrust cases.

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¹ Table 1 shows state by state how marital property is divided upon divorce. Forty-two states have either an equitable distribution or community property provision in their divorce laws.

² The largest tangible asset form of savings is "Owner Occupied Homes" and the largest intangible asset is "Insurance and Pension Reserves." The Economic Report of the President to Congress, Table B-26, at 328 (U.S. Government Printing Office, Washington, D.C. (1992).

³ See, e.g., *White v. White*, 324 S.E.2d 829, 832 (N.C. 1985) (quoting N.C. GEN. STAT. § 50-20(c) and stating that "equal division is made *mandatory* 'unless the court determines that an equal division is not equitable.'"); see also *Coleman v. Coleman*, 365 S.E.2d 178 (N.C. Ct. App. 1988). Virtually every state that has an equitable distribution statute has a case that states equitable means equal, unless special circumstances are present.

⁴ In divorce settlements, if one spouse is given sole possession of an asset that cannot easily be divided, such as the family home, the other spouse receives other property or money as an offset. Alternatively, the courts could require a sale of an indivisible asset and split the proceeds.

the designated valuation date).⁵ Such a pension plan, with an accrued value of, say, \$20,000 at the designated valuation date, would call for a payment of an equal share of money or property worth \$10,000 (assuming equal is decreed equitable) to a nonemployee spouse.

In contrast, if the pension plan is a *defined benefit* plan, the quest for equity in a division of pension assets calls for an *accurate* appraisal of the (present) value of the future pension benefits, earned during the marriage, that *actually* will be enjoyed by the pension recipient.⁶ Placing an accurate and "fair" present value on such defined benefit plans is far more complex than generally recognized. In the case of defined benefit plans, the logic applied to the division of other assets is not enough to ensure equity. In fact, what is perceived by courts across the nation to be an *equal* distribution is apt to be neither equal nor equitable.⁷

Part II of this paper shows why valuations of defined pension benefits present unique problems to the courts in divorce cases.⁸ In Part III, the consequences of inaccurate pension valuations are discussed. The basic lesson drawn from the sensitivity analysis described in Part III is that many courts are systematically undervaluing defined benefit pension plans. This prejudices the nonemployee

⁵ For a discussion of defined contribution pension plans and the differences relative to defined benefit plans see Steven R. Brown, *An Interdisciplinary Analysis of the Division of Pension Benefits in Divorce and Post-Judgment Partition Actions: Cures for the Inequities in Berry v. Berry*, 39 BAYLOR L. REV. 1131 (1987); see also BARTH H. GOLDBERG, VALUATION OF DIVORCE ASSETS, § 9.2 (1984).

⁶ *Present value* defines the current, or present, value of money to be received in the future. *Future value* defines the rate of growth of money currently available. Present value and future value have a reciprocal relationship. Most people are aware that money held in a bank grows at a specified interest rate. If the interest rate is 5 percent per year then \$100 in hand today will be worth \$105 in one year. The present value of \$105 received one year from now is \$100.

Mathematically if PV is present value, FV is future value, and *i* is the rate of interest, then:

$$PV(1 + i) = FV \text{ and } PV = FV/(1 + i)$$

Of course, the mathematics can become more complicated when the present value of annuities, which are a stream of payments to be received in the future, are computed. See generally CHARLES P. JONES, FINANCIAL MANAGEMENT 101-14 (1992).

⁷ The contention that courts misvalue defined benefit pension plans and, thus, prejudice nonemployee spouses (disproportionately females) in equitable distribution litigation, is the major proposition advanced in this paper. This proposition is developed in the following parts of this paper.

⁸ There are other legal events, such as wrongful death cases or dissolution of partnerships, that require valuation of defined benefit pension plans, but divorce is by far the most significant.

spouse, usually the woman, in divorce cases, and, as Part III illustrates, the amount of the prejudice may be substantial.

Part IV of this paper examines court decisions from geographically diverse jurisdictions that have dealt with defined benefit pension valuations. Across jurisdictions and, indeed, across time within jurisdictions, there appear to be wide disparities in the awareness of critical valuation assumptions that affect appraised pension values and in the recognition of the biases built into alternative pension valuation approaches. Implications of the critical issues reviewed in this paper are discussed in the conclusions in Part V.

II. EQUITABLE DISTRIBUTION OF MARITAL ASSETS

A. *Generic Marital Property Distribution Law*

Table 1 classifies states according to the legal theory used for distribution of marital assets.⁹ If the state is classified solely as "alimony," then the issue of valuation of marital assets does not arise; this is because the legal theory of property distribution is not based on division of marital assets between the former spouses, but rather on adequate financial assistance to the dependent spouse.¹⁰ It is notable that 42 states call for either equitable division of marital assets or have community property statutes. Under either of these legal theories, absent exigent

⁹ Marital assets constitute property acquired during marriage regardless of which spouse "paid" for the property. There are exceptions for property acquired in exchange for property acquired prior to the marriage and for property acquired by gift, bequest, devise, or descent, and other exceptions having to do with prenuptial agreements. Definitions of "marital property" vary somewhat across states but those exceptions are not relevant to this paper. *See, e.g.*, ARK. CODE ANN. § 9-12-315 (Michie 1993).

¹⁰ Black's Law Dictionary defines alimony as "the sustenance or support of the wife by her divorced husband [which] stems from the common law right of the wife to support by her husband." BLACK'S LAW DICTIONARY 73 (6th ed. 1990). Under Alabama law, alimony is appropriate "if either spouse has no separate estate or if it be insufficient for the maintenance of such spouse, [and] the judge, upon granting a divorce, at his discretion, may order to such spouse an allowance out of the estate of the other spouse, taking into consideration the value thereof and the condition of the spouse's family." ALA. CODE § 30-2-51 (1989). According to the courts, "the purpose of alimony is to preserve, insofar as possible, the economic status quo of the parties as it existed during the marriage." *Dees v. Dees*, 390 So. 2d 1060, 1064 (Ala. Civ. App. 1980).

According to the Supreme Court of Delaware, different considerations underlie property division and alimony: "While the income which marital assets (and other assets) will produce is a factor to be considered in the division of such assets . . . the division of marital property is not a substitute for alimony and different factors are considered or emphasized." *Donovan v. Donovan*, 494 A.2d 1260, 1264 (Del. 1985) (citations omitted).

circumstances, marital property must be valued and divided.¹¹ Equal division of *marital* property, including pension assets, is generally required even when the state also has an alimony requirement.¹²

¹¹ The equitable distribution statute in North Carolina is typical: "Upon application of a party, the court shall determine what is the marital property and shall provide for an *equitable distribution* of the marital property between the parties in accordance with the provisions of this section." N.C. GEN. STAT. § 50-20(a) (1995) (emphasis added).

¹² In North Carolina, for example, a divorce decree extinguishes (with some exceptions) the right to equitable division of property, but does not affect the right of a spouse to alimony. N.C. GEN. STAT. § 50-11 (1995).

	Classification	Valuation Date	Post Divorce Appreciation	Statutory Provision
1 Alabama	Alimony		No	§30-2-51
2 Alaska	ED	Variable	No	§25.24.160
3 Arizona	CP	DOR	No	§25-318
4 Arkansas	ED	DOD	Yes	§9-12-315
5 California	CP	Variable	Yes	§2610
6 Colorado	ED	DOD	No	§14-10-113
7 Connecticut	Alimony	DOD	No	§46B-81
8 Delaware	ED+Alimony		No	Title 13 §1513
9 Florida	ED+Alimony	Variable	No	§ 61.075
10 Georgia	Alimony		No	§19-5-13
11 Hawaii	Alimony	DOD	No	§580-47
12 Idaho	CP	DOD	Yes	§32-712
13 Illinois	ED+Alimony	DOT	No	Ch. 750 §5/510
14 Indiana	ED	DOD	Yes	§31-1-11.5-11
15 Iowa	ED+ Alimony	DOD	No	§ 598.21
16 Kansas	Alimony		No	§ 60-1610
17 Kentucky	Alimony	DOD	No	§ 403.190
18 Louisiana	CP	DOR	Yes	Civil Code Art. 2356
19 Maine	ED +Alimony		No	Ch. 19 § 722A
20 Maryland	ED	DOD	No	Family Law § 8-201
21 Massachusetts	Alimony		No	Ch. 208 §34
22 Michigan	Alimony	Variable	No	§552.23
23 Minnesota	ED+Alimony	DOT	No	§518.54
24 Mississippi	Alimony		No	§93-5-23
25 Missouri	ED+Alimony	DOT	No	§452.330
26 Montana	ED	DOD	No	Title 404.202
27 N. Dakota	ED		Yes	§14-05-24
28 Nebraska	Alimony		No	§42.366
29 Nevada	CP+Alimony	Variable	No	§125.150
30 New Hampshire	ED+ Alimony		No	§458:16-a
31 New Jersey	ED	DOD	No	Ch 2A:34-23
32 New Mexico	CP	DOR	Yes	§ 40-3-9
33 New York	ED	Variable	Yes	14 § 236 (Dom. Rel.)
34 North Carolin	ED+Alimony	DOS	No	§50-20
35 Ohio	ED+Alimony	DOD	No	§3105.18
36 Oklahoma	ED	DOD	No	Title 43 §121
37 Oregon	CP+Alimony		Yes	§107.105
38 Pennsylvania	ED	DOS	Yes	Title 23 §3501
39 Rhode Island	ED+Alimony	DOT	No	§15-5-16.1
40 South Carolina	ED+Alimony	DOR	No	§20-7-472
41 South Dakota	ED	DOT	No	§25-4-44
42 Tennessee	ED+Alimony	DOD	No	§36-4-121
43 Texas	CP	DOD	Yes	§3.63 (Family Code)
44 Utah	ED+Alimony	DOD	No	§30-3-5
45 Vermont	ED	DOT	No	Title 15 §751
46 Virginia	ED+Alimony	DOT	Yes	§20-107.3
47 Washington	CP	DOR	Yes	§26.16.030
48 W. Virginia	ED+Alimony	DOT	No	§48-2-32
49 Wisconsin	ED	DOD	Yes	§767.255
50 Wyoming	ED+Alimony	DOD	No	§20-2-114

ED and CP stand for equitable distribution and community property, respectively.

DOT, DOS, DOR, DOD stand for date of trial, separation, retirement, and divorce or dissolution, respectively.

All equitable distribution and community property states include vested

pensions among marital property. Some include nonvested expectancies in pensions among marital property, but others do not.¹³ The focus below is on the disposition of vested interests in pension benefits. As indicated earlier, pensions can be classified as either *defined contribution* pension plans or *defined benefit* plans. A *defined contribution* pension plan is basically a pooled group Individual Retirement Account (IRA) combined with professional portfolio stock and money management. In such plans, valuation is quite easy because retirement assets are individually identified, and the assets are largely held as securities that have readily identifiable market values. Generally, valuation of a defined contribution pension plan is not challenging.

With a *defined benefit* plan, however, part of the employee's employment contract is a guarantee by the employer of an additional payout after the employee retires. The additional compensation is generally paid out according to a formula, with pension benefits related to the employee's salary level, years of service, and retirement age.¹⁴ At any point in time, the value of a defined benefit pension is the sum of the future monthly payments that *actually* will be provided to the retiree, adjusted or reduced to present value.¹⁵ The number of monthly payments may be

¹³ A nonvested profit-sharing plan is marital property subject to equitable distribution although "it may be necessary to discount the plan to some extent to reflect the possibility that it will not vest." *Fisher v. Fisher*, 33 Pa. D. & C.3d 69, 71 (1984). *But see* *Durham v. Durham*, 708 S.W.2d 618, 619 (Ark. 1986) (nonvested right in military retirement does not constitute property). In North Carolina the issue is decided statutorily: "The expectation of nonvested pension, retirement, or other deferred compensation rights shall be considered separate property." N.C. GEN. STAT. § 50-20(b)(2) (1995).

¹⁴ In a typical plan, the annual defined benefit is directly related to the employee's salary (often a prescribed formula such as an average of the highest four or five years), years of services (say, 2 percent of the four or five highest salaried years), and a multiplier to adjust for the age of the employee.

The defined pension benefit, B, might be stated as:

$$B = W \times Y \times F$$

where W is wages (an average of the four or five highest salaried years), Y is years of service, and F is a multiplier often supplied by the Pension Benefit Guaranty Corporation, a corporation within the United States Department of Labor. *See* *Bishop v. Bishop*, 440 S.E.2d 591, 596 (N.C. Ct. App. 1994). In the formula above, if W is \$50,000, Y is 30 and F is 2.4%, then B, annual pension benefit, is defined at \$36,000.

¹⁵ Referring to the example in note 14, *supra*, if the defined pension benefit is \$36,000 annually, then its present value is reduced by the period of time between the present age of the employee and the actual receipt of the pension annuity. If the employee is completing age 55 at date of separation and his or her earliest possible retirement is at age 60, then the present value, PV, of the defined pension benefit, *in the first year alone* is simply represented as:

projected, based on life expectancy for the employee spouse (sole survivor plan), and present value calculations may be viewed as adjusting for likely interest earning rates.¹⁶

It frequently is assumed that the present value of a defined benefit pension plan can be computed with reasonable accuracy once the employee's salary, years of service, age, and retirement date are known, by application of the pension benefit formula in force at the prescribed valuation date.¹⁷ *However, the level of benefits earned during marriage may be adjusted subsequent to valuation (most often to provide for partial cost-of-living adjustments).* In fact, the majority of defined benefit pensions have been periodically escalated to provide some adjustment for inflationary changes.¹⁸ Failure to take into account possible — indeed, in many cases likely — adjustments in defined benefit pension plans can result in a serious underestimation of the total value of the pension.¹⁹

$$PV = \$36,000/(1 + i)^5$$

For each subsequent year, the PV value of the defined benefit would decline according to the rate of interest.

¹⁶ Referring to note 15, *supra*, if the one-year present value of a one year plan payment is equal to $\$36,000/(1 + i)^5$, where \$36,000 is the annual amount paid out under the defined pension formula and there are five years before the employee's earliest possible retirement, the overall value of the pension must be adjusted for the expected life span or mortality of the employee. If we assume that benefits will not change, then the overall value of the defined pension is:

$$PV = \sum_{k=5}^n \$36,000_k / (1 + i)^k$$

where k is the number of years between the date of separation or divorce and the earliest possible retirement and n is expected years remaining until death.

¹⁷ In footnotes 14 and 16, *supra*, the critical assumption made in computing present value, PV, is that the defined benefits formula is unchanged. In other words, F is assumed a constant. If instead, F increases to adjust for cost of living, then present value estimates would be too low. For discussions on defined benefit plan increases, see generally J.C. Poindexter, et al., *Policy and Practice in the Equitable Distribution of Defined Benefit Pension Plans*, Table 1 (unpublished manuscript on file with the *Ohio State Law Journal*) and Steven G. Allen et al., *Post-Retirement Benefits Increases In the 1980s: Did Plan Finances Matter?* in *TRENDS IN PENSIONS* 1992 326 and Table 13.9 (1992).

¹⁸ Clearly, raising pension benefits is a regular event in many plans. See Allen et al., *supra* note 17, at 321-22 and Tables 13.1 and 13.2. Note further that Social Security is a completely COLA-adjusted defined benefit pension.

¹⁹ If we use the North Carolina State Retirement Plan coupled with a requirement to

B. *Methods of Distribution*

Although states have developed their own lexicon when dealing with distribution of marital property, there are two basic methods of pension benefit distribution in the event the parties cannot agree on a plan for the division of assets.²⁰ When agreement cannot be reached, state statutes allow for distributive awards either as: (1) a *fixed percentage* of the pension annuities when they are actually received, or (2) an *immediate offset*, in which the nonemployee spouse receives other property to compensate for giving up his or her share in pension benefits.²¹ So, with some exceptions, it may be said that most state statutes contemplate, either with or without the nonemployee spouse's agreement, distribution of marital *pension property* either in the form of an *immediate offset* or a *fixed percentage* of the retirement benefits when those benefits are actually paid to the employee spouse. In the eyes of most courts, the alternate distributions are applied as if they are equivalent when, as shown below, they are not, even after adjustment to present value.

It is vitally important to note that with an immediate offset, an appraised value of future pension benefits must be determined, whereas with the fixed percentage

assume earliest possible retirement, *see* notes 36-37 and accompanying discussion *infra*, then the underestimation associated with assuming no growth in pension benefits could exceed 50 percent of the value of the pension. Poindexter et al., *supra* note 17, Table 2. *See also Allen et al.*, *supra* note 17, at 326 and Table 13.9.

²⁰ As an example, in North Carolina,

The distributive award of vested pension, retirement, and other deferred compensation benefits may be made payable:

...

- c. As a prorated portion of the benefits made to the designated recipient at the time the party against whom the award is made actually begins to receive the benefits; or
- d. By awarding a larger portion of other assets to the party not receiving the benefits, and a smaller share of other assets to the party entitled to receive the benefits.

N.C. GEN. STAT. § 50-20(b)(3)c and d (1995).

²¹ *Id.* Throughout the states, there are variations in the statutory language but the basic options are the same: *immediate offsets*, with the renunciation by the nonemployee spouse of any interest in the pension of the employee spouse, and deferred *fixed percentages*. The statutes allow for immediate offsets that occur in a series of payments rather than a single lump sum. When immediate offsets are paid out in installments, there should be an interest charge on the payments that occur in the future. *See Seifert v. Seifert*, 346 S.E.2d 504, 506-08 (N.C. Ct. App. 1986), *aff'd*, 354 S.E.2d 506 (N.C. 1987).

method there is no need to place a value on those future benefits.²² This dichotomy occurs because, with the immediate offset method, the nonemployee spouse never actually receives any of the pension payout. The spouse receiving the immediate offset gives up any right to pension funds in return for the immediate receipt of property.²³ Of course, with an immediate offset distributive award, *if the pension is not properly valued, the award will fail to match the court's intentions for equitable distribution of property. If the future pension benefits are undervalued, the nonemployee (often female) spouse will receive an inadequate offset.*

With a fixed percentage distributive award, the division of this form of marital property only occurs at retirement, so valuation of the nonemployee spouse's interest at the date of divorce or separation is unnecessary. The value of the marital portion of the pension, together with any appreciation or depreciation of pension benefits, will be shared by both parties.²⁴ In like fashion, if the pension fund defaults on its payments, both parties bear the loss, whereas with the immediate offset method, the nonemployee spouse escapes the risk of pension default. In addition to the risk of default by the employer, an immediate offset enables the nonemployee spouse to escape other risks, including post-divorce actions by the employee spouse that affect the size and existence of pension benefits.²⁵ These risks are borne by a nonemployee spouse who is awarded a fixed percentage of the pension benefits of the employee spouse. An accurate appraisal of the present value of the nonemployee's (fixed percentage) interest in the pension benefits of the former spouse would *raise* the plan's value to the extent that future appreciation of benefits could be expected, but *lower* that value to reflect risks that are endured.²⁶

²² According to Judge Eagles in *Seifert*, "[u]nder this method [fixed percentage], the trial court need not determine present value of the pension. All the court must do is to determine the percentage to which the nonemployee spouse is entitled." *Seifert*, 346 S.E.2d at 508.

²³ The spouse receiving the immediate offset is the *nonemployee* spouse.

²⁴ According to Judge Eagles in *Seifert*, the fixed percentage method "also provides for any 'growth' on the amount of the vested pension or retirement benefits because the nonemployee spouse will receive a fixed percentage of the benefits actually received by the employee spouse at retirement." *Seifert*, 346 S.E.2d at 508.

²⁵ The election or nonelection of survivor benefits or the revocation thereof affects the existence or size of the pension benefits. Elections and other actions by the employee spouse can affect payments to the nonemployee spouse. Many of these issues are discussed in Brown, *supra* note 5. There are numerous instances in which post-divorce actions by employee spouses reduce retirement payments to the former spouse. *See, e.g.*, Brown v. Brown, 828 S.W.2d 601 (Ark. Ct. App. 1992).

²⁶ Indeed, the mortality of the ex-spouse is a factor in the existence or amount of some pensions. *Freiberg v. Freiberg*, 127 Cal. Rptr. 792, 798 (Cal. Ct. App. 1976), *overruled on other grounds by In re Marriage of Gillmore*, 174 Cal. Rptr. 493, 497 at n.5 (Cal. Ct. App. 1981).

C. *Separate and Marital Property*

Often the duration of pension-producing employment and marriage are not the same. Statutes often provide formulas for determining the marital portion of a pension. The most common statutory formula, sometimes called a coverture fraction, calls for dividing the number of years of simultaneous marriage and employment (at the job from which the pension benefits are derived) by total employment time.²⁷ If an employee worked for 20 years at an occupation earning pension benefits, but was married for just 12 of those 20 years until the date of separation, the statutory marital property share would be 60 percent (12/20) of the value of the pension at the date of separation. The implicit assumption in this identification of "marital" asset value is that all years of employment are fungible when in fact they are not in many cases.²⁸

D. *Passive Versus Active Appreciation*

In computing the value of the pension subject to distribution, state statutes generally exempt from marital property any "contributions, years of service or compensation which may accrue after the date of separation."²⁹ The statutes, however, typically allow for the capture of appreciation in marital assets after

²⁷ In North Carolina the equitable distribution statute reads as follows: "The award shall be determined using the proportion of time the marriage existed, (up to the date of separation of the parties), simultaneously with the employment which earned the vested pension, retirement, or deferred compensation benefit, to the total amount of time of employment." N.C. GEN. STAT. § 50-20(b)(3) (1995).

²⁸ Additional pension benefits associated with an additional year of employment (1) increases with duration of employment, and (2) often have thresholds that give significant boosts for one additional year of employment. R. Frasca, *The Valuation of Defined Pension Benefits as a Marital Asset: An Abundance of Approaches*, 4:1 J. FORENSIC ECON. 47 (1990); Richard A. Ippolito, *The Labor Contract and True Economic Pension Liabilities*, 75 AM. ECON. REV. 1031 (Dec. 1985)

Developing the mathematics to demonstrate these propositions is outside the scope of this Article but serves to reinforce the main point of this paper that a simplistic approach to pension evaluation in divorce proceedings can have unexpected consequences.

²⁹ See, e.g., N.C. GEN. STAT. § 50-20(b)(3) (1995). The California Court of Appeals has stated that "[w]hen the non-employee spouse makes an election before the employee-spouse actually retires, it constitutes "' . . . an irrevocable election to give up increased payments in the future which might accrue due to increased age, longer service and a higher salary.'" [Citations]" *Crook v. Crook*, 3 Cal. Rptr. 2d 905, 908 (Cal. Ct. App. 1992).

separation or divorce.³⁰ The authors of various state statutes clearly contemplated possible appreciation or depreciation of pension benefits after the date of separation. *Further, there is no indication that they intended that these gains or losses should be received by recipients of fixed percentages of retirement benefits but withheld from recipients of immediate offsets.* This anomalous result, unfortunately, is the current norm in court-mandated distributions of marital assets upon divorce.

III. CRITICAL ISSUES IN PENSION EVALUATION

A. *The Reality of Pension Disbursements and Inequitable Distributions*

Fixed percentage *shares* of pension benefits at time of the actual disbursement could have the same *value* to the recipients as present-valued immediate offset payments only if the actual future payouts match the values projected at the date of separation. If future payouts are underestimated then immediate offsets have less value than fixed percentage shares. So, the issue of whether pensions are or are not subject to escalator adjustments over time is an inescapable one for courts.

Readily available empirical evidence indicates that a "one shoe fits all" assumption of a zero future growth rate of benefit payments (earned in a previous time interval) is untenable as indicated in Table 2 and Figure 1. In a series of papers, Clark, Allen, McDermid, and Sumner describe a history of pension plan payout adjustments in the 1970s and 1980s.³¹ In the 1970s, these authors found that "most retirees in the sample of plans used received at least one increase in benefits and many received substantial nominal benefit increases."³² Overall, they found, "[p]ost-retirement increases amounted to approximately two-fifths of the rise in the Consumer Price Index."³³ In the slower inflation of the 1980s, the authors found that the proportion of defined benefit pension recipients receiving benefit increases was less, but that the increases provided came closer to matching

³⁰ According to the North Carolina Equitable Distribution Statute, "[t]he award shall include gains or losses on the prorated portion of the benefit vested at the date of separation." N.C. GEN. STAT. § 50-20(b)(3)(d) (1995). In *Brown*, an Arkansas court wrote: "We find no valid reason for holding that the award of one-half of 90 percent of the gross retirement benefits does not carry with it the same portion of any COLA increases or decreases subsequent to divorce." *Brown v. Brown*, 828 S.W.2d 601, 602 (Ark. Ct. App. 1992).

³¹ *Allen et al.*, *supra* note 17; *Steven G. Allen et al.*, *A Comparison of Pension Benefit Increases and Inflation, 1973-79*, 107 MONTHLY LAB. REV. 42 (May 1984) (hereinafter *Benefit Increases and Inflation*).

³² *Allen et al.*, *Benefit Increases and Inflation*, *supra* note 31, at 42.

³³ *Id.*

inflation than those granted in the 1970s.³⁴

With regard to major individual employers, it is possible to obtain historical measures of the escalations applied to benefits paid to their employees, as illustrated in Table 2 and Figure 1. Retired State of North Carolina employees enjoyed benefit increases that averaged 4.69% annually in the 1970 to 1990 time interval, while the rate of increase for IBM employees was 3.13%.³⁵ Over this same interval, inflation as measured by the Consumer Price Index, averaged approximately 6% yearly.

³⁴ *Allen et al.*, *supra* note 17, at 322-23.

³⁵ *Poindexter et al.*, *supra* note 17, at Table 1.

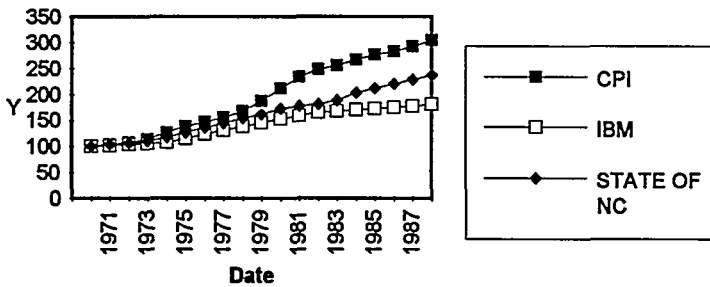
Table 2

**INDEX VALUES, CPI, AND SELECTED
RETIREEE BENEFITS**

Year	CPI Index Value	IBM Index Value	STATE of NC Index Value
1970	100	100	100
1971	104.4	101.9	104
1972	107.7	103.9	107.1
1973	114.4	105.9	110.8
1974	127	107.9	117.4
1975	138.6	115.7	126.8
1976	146.6	124.1	135.7
1977	156.1	131.3	144.4
1978	168	139	153.9
1979	187	145.8	161.9
1980	212.2	152.9	172.9
1981	234.1	158.9	178.1
1982	248.6	165.1	181.6
1983	256.5	167.6	188.9
1984	267.6	170	204
1985	277.2	172.5	212.2
1986	282.5	175	220.2
1987	292.7	178	229.1
1988	304.6	181.1	237.3
1989	319.3	194.2	245.6
1990	336.5	197.3	260.6

Sources: International Business Machines, Inc., (1994)
 North Carolina State Government Teachers' and State
 Employees' Retirement System, (1993).
 Allen, Clark & McDermed (1992)

Figure 1



The sensitivity of the present values of pension benefits to “cost of living” adjustments can be illustrated by simple examples. If the escalation rate of pension benefits is 5% annually (just above the actual 1970-90 rate for North Carolina State retirees), the level of pension benefits would rise by 25% in 4 years, 50% in 8 years, 75% in 11 years, and would double in 14 years.³⁶ Quite apparently, an effort to avoid uncertainty or conjecture in valuing pension benefits by assuming a zero rate of post-date of separation increases is on shaky empirical ground. In the absence of empirical evidence, a zero assumed rate of increases is a co-equal in arbitrariness with -10%, +10%, or any other rate. Confronted with actual empirical evidence of historic behavior patterns, the assumption of zero percent growth appears more speculative, conjectural, and invalid than an assumption of positive adjustments in pension benefits. With the elapse of years between the age at separation/divorce and age at which pension benefits are available, escalations of 50% or more in present values for pensions are not unreasonable.³⁷

B. Property Distribution of Defined Benefit Pensions in Divorce

Table 3 provides an illustration of property distribution in divorce, comparing an immediate offset and a fixed percentage deferred distribution. The pension is a defined benefit pension and the court is assumed to be making the customary assumption that pension benefits do not appreciate. Let us also assume, consistent with empirical data, that in fact pension benefits do appreciate.

³⁶ All percentages were rounded to the nearest whole year.

³⁷ In an effort to increase certainty in pension valuation, some courts require employee spouses to calculate the present value of their pensions at the date of separation or earliest possible retirement, whichever date is later. See *Bishop v. Bishop*, 440 S.E.2d 591, 595 (N.C. Ct. App. 1994); *Surette v. Surette*, 442 S.E.2d 123, 125 (N.C. Ct. App. 1994). In both of those cases, the earliest possible retirement was 50 and life expectancies were into the 70s. *Bishop*, 440 S.E.2d at 594; *Surette*, 442 S.E.2d at 124.

Table 3

Equitable Distribution Simulation: Escalated and Nonescalated Pensions

(1)	(2)	(3)	(4)	(5)	(6)
Marital Property Minus Pension	Statutory Fraction	Zero Growth PV of Pension	Non-Empl. Spouse Share Of Pension	50% Growth PV of Pension	Non-empl. Spouse Share of Pension
\$100,000	.6	100,000	30,000	150,000	45,000

(7)	(8)	(9)	(10)
Immediate Offset		Fixed Percentage	
Non-Empl. Share Of Total Property	Empl. Share Of Total Property	Non-empl. Share of Total Property	Empl. Share of Total Property
\$80,000	110,000	95,000	95,000

For our hypothetical measures, consider Emily and Ed whose total marital assets, minus pension assets are valued at \$100,000 (Column 1, Row 1). Assume that Ed is the employee spouse and Emily is the nonemployee spouse, though the analysis is the same regardless of the gender of the employee spouse. Assume further that Ed and Emily were married for 12 years and that Ed was working at his job for 20 years. The coverture fraction thus equals .6 (12/20) (Column 2). Assume that the projected pension benefits to be enjoyed by Ed, based on the formula in place at the date of separation, has a present value of \$100,000. This value must accurately reflect Ed's life expectancy and a suitable discount or interest rate. With the assumption that *defined benefits* will not change, future benefit payments are set (Column 3). The valuation date for these computations is

the date of separation, and, further, for valuation purposes, it is assumed that Ed will quit his job at the date of separation and will retire as early as possible. As is apparent, Column 3 is packed with explicit and implicit assumptions.

With projected benefits *frozen* at the level prescribed by the date of separation formula, the nonemployee spouse, Emily, would be entitled to \$30,000 of the total value of the pension (Column 4).³⁸ If, in fact, the pension provider subsequently escalates benefit payments, the "value" of the pension package is altered dramatically, with only the employee spouse enjoying the gain, even though the gains do not reflect post-marital effort on the part of the employee spouse.

To illustrate this, consider an overall increase in the level of pension benefits of 50% (with a present value that rises commensurately to \$150,000) during the interval while pension payouts are actually distributed.³⁹ If the *actual* present value of the pension "with adjustments" is \$150,000, then \$90,000 (or 60% of the true value of the pension) is a "correct" marital property measure, with a one-half value of \$45,000 (Column 6). If the accurate value of the pension were known (or correctly estimated) at the date of separation, \$45,000 is the immediate offset amount to which Emily would be entitled.

Measures in columns 7 through 10 permit comparison of the values of distributable assets with benefits *frozen* at the date of separation (formula-predicted levels) versus values with benefits that are escalated. With an immediate offset distribution, Emily would receive 50 percent of nonpension marital property (\$50,000), plus \$30,000 more of nonpension marital property to offset giving up her share of the marital component of Ed's pension (Column 7). Ed receives \$20,000 of the nonpension marital property plus all of the pension funds, \$90,000 of which is marital property (Column 8). The result of an immediate offset distribution, combined with the assumption that benefits do not appreciate, is that Emily receives 42 percent of the marital property while Ed gets 58 percent.

If, instead of an immediate offset distribution, Emily is provided a fixed percentage of Ed's retirement pension, she will receive a full 50% of the marital property regardless of whether pension benefits appreciate or not. If defined pension benefits appreciate 50% between the date of separation and actual payment of retirement benefits (to a present value of \$150,000), Emily would receive pension benefits of \$45,000 (equal to one-half of the 60% coverture fraction share times the present value of the pension benefits). Combined with \$50,000 of nonpension marital assets, her equitable share has a value of \$95,000 (Column 9). This, of course, is one-half of a total marital property value of

³⁸ Emily is entitled to one-half of 60% of an asset valued at \$100,000, or \$30,000 (.5 x .6 x \$100,000).

³⁹ Data is available (on file with the *Ohio State Law Journal*) showing increases in *present value* of pension plan benefits exceeding 50% due to COLA adjustments for employees of the State of North Carolina.

\$190,000, with Ed receiving the remaining \$95,000 (Column 10). With current practice in applying equitable distribution/community property statutes, the nonemployee spouse is apt to receive a full 50% (or other "equitable" share) of marital property only if she takes a fixed percentage of pension benefits when they are actually paid out, but this means she has to endure the risks of pension plan defaults plus continuation of financial entanglement with the ex-spouse to receive a full share of pension benefits.

Of course, if there is no appreciation in pension benefits, the fixed percentage method yields the same distribution as the immediate offset. In this case, Emily would receive 30% (one-half of the 60% coverage fraction share) of the pension annuities plus 50% of the nonpension marital property for a total of \$80,000. Ed would receive the same, the other 40% of his pension considered separate property, but would bear all risks associated with the plan. With appreciation of pension benefits, the reason the nonemployee spouse receives less than 50% of the marital property is that the nonemployee spouse is compelled to give up the appreciation on an asset that is more likely than not to appreciate.

It is interesting to consider this outcome contrasted with the handling of what is generally the most valuable family asset, the family home. Homes often appreciate significantly in value between the date of separation and a subsequent date of equity value distribution in divorce cases. The time lapse may be to the date of the equitable distribution hearing, date of actual sale of the residence, date of majority of children in the home, or some other prescribed date. If the value of the home appreciates over this time interval, courts characteristically award the equitable share of the *appreciated* value of the home at the later date to the divorcees.⁴⁰ Not accounting for pension benefit appreciation may be viewed as analogous to freezing the value of the family home at its date of separation value, limiting the one ex-spouse to the equitable share of that date of separation value while awarding the remaining (and escalated) share value to the other.⁴¹ The financial consequences of the "freeze" assumption of pension benefits to the nonemployee spouse are likely to be proportionally more severe because the "freeze" period is much longer than the period between separation and property distribution. Recognizing escalations of pension benefits (and the accompanying increase of value of a pension plan) is conceptually just as necessary as recognizing rising real estate values, albeit fraught with more complexity stemming from the need for current appraisal based on projected future benefit escalations.

⁴⁰ See *Atkins v. Atkins*, 401 S.E.2d 784, 790 (N.C. Ct. App. 1991) (holding that it was not reversible error for the trial court to consider as a distributional factor appreciation of marital property between the date of separation and date of trial).

⁴¹ In this example, it is assumed that marital property is valued at the date of separation, and that the divorce trial and property distribution occurs sometime later.

IV. PENSION CASES ACROSS THE NATION

There are a number of states in which court battles over post-separation appreciation in pension benefits are especially keen. In none of these states can it be claimed that the final evolution of the law in the area has occurred. Some states seem farther along than others in their judicial analyses of this issue, but exceptions and reversals abound. The cases below illustrate the legal contortions various state courts have engaged in to avoid recognizing post-separation increases in pension benefits when awarding immediate offsets. In each case the basic anomaly is clear: recipients of a fixed percentage of pension benefits enjoy post-separation, or post-divorce in most states, increases in pension benefits, but immediate offset recipients do not. Note that many of these cases are very recent, another indication of the continuing absence of judicial resolution of this issue.

It is clear from the sample of cases reviewed below that benefit appreciation is most fully recognized with fixed percentage payouts. It may be claimed that some inroads are being made with respect to recognition of benefit escalations in immediate offsets, but the value gap remains quite wide between immediate offsets versus a sharing of benefit escalations with fixed percentage distributions.

A. North Carolina

Seifert v. Seifert,⁴² a state court of appeals decision, distinguished between immediate offsets and fixed percentage methods of property distribution of pensions.⁴³ In applying the equitable distribution statute to a defined benefit pension, the court examined the two methods commonly used, the present value (or immediate offset) method and fixed percentage method, and correctly held that the two methods do not mix well.⁴⁴ Under the fixed percentage method, the court concluded that "the trial court need not determine present value of the pension. All the court must do is to determine the percentage to which the nonemployee spouse is entitled."⁴⁵ The percentage to which the nonemployee spouse is entitled was set at one half of the coverture fraction.

With application of the present value method of valuation, the court of appeals noted that an immediate payout is required. The court held that mixing the present value method with a deferral of actual payments to the nonemployee spouse until the employee spouse began drawing such benefits was a double reduction for present value.⁴⁶ Any deferral of payments, the court added, would call for interest

⁴² 346 S.E.2d 504 (N.C. Ct. App. 1986), *aff'd*, 354 S.E.2d 506 (N.C. 1987).

⁴³ *Seifert*, 346 S.E.2d at 507.

⁴⁴ *Id.* at 509.

⁴⁵ *Id.* at 508.

⁴⁶ *Id.* at 509.

on the future "installments."⁴⁷ The case was remanded because the trial court mandated a pension distribution based on the present value of projected benefits, but provided neither an immediate payout of the calculated present value of the spouse's share of retirement benefits nor interest add-ons for installment payments.

The court of appeals also noted that, with the deferred fixed percentage method, the nonemployee spouse would share in any growth in pension benefits.⁴⁸ The court, however, did not address the next logical issue which is that nonemployee spouses who receive an immediate offset under the present value method *do not share* in such growth. The court did note, though, that with the present value method, all of the risk of default or nonpayment of the pension is transferred to the employee spouse, whereas such risks are borne equally under the fixed percentage method.⁴⁹ The court also noted that the present value method offered the advantage of cleanly separating the financial affairs of the former spouses, whereas with the fixed percentage method, certain elections and employment-related decisions can affect the size of the monthly payments.⁵⁰ In addition, in some plans the mortality of the employee can be a factor in determining whether the nonemployee spouse gets paid benefits.⁵¹

Although the present value method with immediate distribution of property, as supported by the court in *Seifert*, has intuitive appeal, caution is appropriate. The wisdom of electing to receive an immediate offset depends in part on the magnitude of the risks of default that are eliminated, the perceived value of acrimony that is avoided, and the counter-balancing value of likely appreciation of future pension benefits that is foregone. There is not necessarily a balance or equality between these variables, and indeed, the probability of a near match is low. The court's discussion suggested no recognition of likely appreciation of benefits in defined benefit pensions, even though risk factors and avoidance of acrimony are recognized.

⁴⁷ *Id.*

⁴⁸ *Id.* at 508.

⁴⁹ *Id.*

⁵⁰ *Id.* at 508. In California, post-divorce opportunistic behavior is such a problem that the courts have the power to:

order a party to elect a survivor benefit annuity or other similar election for the benefit of the other party, as specified by the court, in any case in which a retirement plan provides for such an election, provided that no court shall order a retirement plan to provide increased benefits determined on the basis of actuarial value.

CAL. FAM. CODE § 2610(a)(2) (Deering 1995).

⁵¹ *Freiberg v. Freiberg*, 127 Cal. Rptr. 792, 797 (Cal. Ct. App. 1976); *Shill v. Shill*, 599 P.2d 1004, 1008 (Idaho 1979).

In *Bishop v. Bishop*,⁵² plaintiff Nancy Bishop appealed the trial court determination of her share of the defendant's pension. The defendant was a long-time DuPont employee with a defined benefit pension providing an earliest possible retirement date at age 50 and normal retirement at age 65.⁵³ Defendant was 48 at the date of separation, with an expected life span of 30 years according to the trial court. Using an interest (or discount) rate of 7.5%, the trial court in *Bishop* calculated a present value of the prospective pension benefit stream of \$47,445, based on an August, 2007 retirement start date, when the defendant turned 65. The present value of the pension brought back to the date of separation was found to be \$13,724.⁵⁴

The court of appeals noted that valuation of defined benefit pension plans is "fraught with uncertainties."⁵⁵ The court quoted an article by Lawrence Golden which lists several risks of default in pensions including the risks that the employee spouse will decide not to continue to work with the same employer.⁵⁶ The court of appeals then provided a very specific procedure for valuing defined benefit pensions. The court decreed that, first, the pension must be valued assuming the employee spouse retires on the date of separation or at the earliest possible retirement after the date of separation, whichever comes later.⁵⁷ Valuing pensions at the earliest possible retirement date is a timing decision that is not required by the North Carolina Equitable Distribution statute, but one which appears motivated by a desire of the courts to generate a more certain procedure in valuing defined benefit pensions. The court indicated that the pension valuation procedure applied (1) must "not include contributions, years of service or compensation which may accrue after the date of separation," but that (2) it should include "gains and losses on the prorated portion of the benefit vested at the date of separation."⁵⁸ *The court's discussion of present value measures provides no clarification of the manner in which "gains and losses on the prorated portion of the benefit vested at the date of separation" are, in any sense, to be captured by the recipient of an immediate offset.*

Second, according to the court, the employee spouse's life expectancy at the date of separation and, hence, the number of months that the employee spouse can expect to receive the pension annuity must be determined. Third, the court stated the present value of the pension at the earliest possible retirement date must be

⁵² *Bishop v. Bishop*, 440 S.E.2d 591 (N.C. Ct. App. 1994).

⁵³ *Id.* at 594.

⁵⁴ *Id.* at 593.

⁵⁵ *Id.* at 595 (citing LAWRENCE J. GOLDEN, *EQUITABLE DISTRIBUTION OF PROPERTY*, § 7.13 (1983)).

⁵⁶ *Id.*

⁵⁷ *Id.*

⁵⁸ *Id.*

calculated using an acceptable discount or interest rate. Fourth, if the earliest possible retirement date does not match the date of separation, then the date of separation present value of the pension must be determined.⁵⁹ Note that the third step in this computation implicitly calls for an assumption of zero appreciation in benefits.

In *Bishop*, the court of appeals indicated that the order of the trial court “does not reflect that the trial court considered, as it must, any projected ‘gains and losses’ on the portion of the pension which was vested as of the date of the separation.”⁶⁰ The court noted, however, that no evidence was presented on this issue, and therefore it is not reversible error. It is submitted that no evidence could be presented on this issue because, under the present value method as elucidated by the court of appeals, there is no room for such evidence.⁶¹ Only if the courts allow for evidence of *likely* future adjustments in pension benefits in the third step, either by the individual employer or employers generally, is it possible to consider “gains or losses” on the prorated marital portion of the pension.⁶²

B. California

In *Crook v. Crook*,⁶³ the court of appeals held that post-divorce appreciation in the amount of pension benefits can be captured by the nonemployee spouse.⁶⁴ According to the court of appeals in *Crook*,

When the non-employee spouse makes an election before the employee spouse actually retires, it constitutes “. . . an irrevocable election to give up increased payments in the future which might accrue due to increased age, longer service and a higher salary.’ [Citations]” However, the non-employee spouse is entitled, “. . . to share in any increase in benefits which would have been received had [the employee spouse] actually retired on the date she [or he] elected to receive her [or his] interest, such as automatic cost-of-living adjustments.”⁶⁵

Note that the ruling in California took place with a fixed percentage

⁵⁹ *Id.* at 595-96.

⁶⁰ *Id.* at 596.

⁶¹ In other words, the court assumes that the level of benefits will not change in a defined benefit pension such as DuPont’s. This flies in the face of a good deal of empirical evidence. *Allen et al.*, *supra* note 17, at 321-25.

⁶² To date, there are no North Carolina cases that allow recipients of immediate offsets to obtain a share of likely future appreciation in defined pension benefits.

⁶³ 3 Cal. Rptr. 2d 905 (Cal. Ct. App. 1992).

⁶⁴ *Crook*, 3 Cal. Rptr. 2d at 908.

⁶⁵ *Id.* (alteration in original) (citations omitted).

distributive award and parallels the North Carolina ruling in *Seifert* in which the North Carolina Supreme Court indicated that if the nonemployee spouse is awarded a fixed share she would share in any gains or losses incurred on the marital portion of the pension.⁶⁶

In *Crook*, the court of appeals in California provided a listing of the types of gains and losses in which the nonemployee spouse can share.⁶⁷ If the pension benefit gain is due to increased service, or a higher salary after the date of separation, it cannot be captured by the nonemployee spouse, but if the gain is due to inflation adjustments in pension benefits then the gain can be captured.⁶⁸ Again the basic asymmetry problem surfaces, for if a nonemployee spouse elects to take an immediate offset, it is not clear that cost-of-living adjustments in the pension can be captured in California. It is odd logic that allows a court to endorse alternate division procedures that result in quite disparate values for the same asset.

C. Texas

In *Berry v. Berry*,⁶⁹ the Supreme Court of Texas appeared to preclude any adjustments for post-divorce appreciation in benefits.⁷⁰ According to Brown, who broadly criticized this decision, *Berry* essentially requires divorce courts to value pension assets at the date of divorce, *assuming benefits are frozen at that date*.⁷¹ Subsequently, in *Anderson v. Anderson*, a former wife sought to share in the cost-of-living (COLA) increases in her ex-husband's military pension benefits, a claim that her husband argued was barred by the *Berry* decision.⁷² According to the court of appeals, however, the trial court was not required by law to value the former wife's interest in the former husband's military benefits as of the date of the 1971 divorce, nor was the court required to apply the *Berry* formula to limit the former wife's portion of benefits to those earned during marriage, where husband began receiving benefits in 1981.⁷³

When Marie Anderson was divorced from her husband in 1971, the divorce decree entitled her to one-half of her husband's pension benefits.⁷⁴ In 1983, William Anderson, two years after he began receiving benefits, was seeking to

⁶⁶ *Seifert v. Seifert*, 345 S.E.2d 504, 508 (N.C. 1986).

⁶⁷ *Crook*, 3 Cal.Rptr.2d at 908 (1992).

⁶⁸ *Id.*

⁶⁹ 647 S.W.2d 945 (Texas 1983); *see also* discussion in Brown, *supra* note 5.

⁷⁰ *Berry*, 647 S.W.2d at 947.

⁷¹ Brown, *supra* note 5, at 1184.

⁷² 707 S.W.2d 166 (Tex. Ct. App. 1986).

⁷³ *Id.* at 169.

⁷⁴ *Id.* at 167.

limit his former wife, Marie, to one-half of the benefits *valued at the time of divorce in 1971*. William, citing the *Berry* decision, claimed that the court was required to assume that future benefits were frozen at the date of divorce.⁷⁵ At the time of divorce, William would have been eligible to receive \$273.79 per month, but when William actually reached retirement age, he was entitled to \$530.42 per month.⁷⁶ The court distinguished *Anderson* from *Berry* by noting that in *Berry*, the wife/nonemployee spouse sued to partition pension benefits twelve years after divorce, and that the husband had continued to work at the same job. In *Anderson*, the husband did not serve in the military at any time after the divorce, but “was merely waiting to live ten more years to collect on what had already accrued in his behalf.”⁷⁷ Although the court is correct regarding the factual difference in the two cases, it does not automatically follow that there was no passive escalation in pension benefits enjoyed by the employee-spouse in *Berry* (and *earned* during marriage). Surely at least some of the appreciation in benefits that occurred in *Berry* was due to the same forces that raised the benefits in *Anderson*. It is strained logic that justifies giving all COLA-related pension benefit increases to a former spouse who continues working at the same job, but requires a sharing in pension escalation if the employee spouse quits work at the time of divorce.

D. Indiana

In *Tirmenstein v. Tirmenstein*,⁷⁸ an Indiana appeals court affirmed the award of a post-date of separation increase in pension benefits to the nonemployee spouse due to both continued service and increased base salary.⁷⁹ The defendant’s pension was directly related to both years of service and base salary. After separation, the defendant continued to work at the same place (a police department), becoming eligible for a pension that was a higher percentage of his base salary, while his base salary also increased with the passage of time. Since the right to enjoy an increasing percentage of base salary and a higher base salary was earned while the employee spouse was married, the nonemployee spouse was entitled, according to the court of appeals, to share in the post-dissolution increases in pension benefits attributable to increased years of service and wages.⁸⁰ The defendant/employee spouse claimed that the pension award was “more than fifty percent . . . of the present value of his pension benefit” at the time the award was made because of

⁷⁵ *Id.*

⁷⁶ *Id.* at 168.

⁷⁷ *Id.*

⁷⁸ 539 N.E.2d 990 (Ind. Ct. App. 1989).

⁷⁹ *Tirmenstein*, 539 N.E.2d at 992.

⁸⁰ *Id.* at 991.

post-divorce increases being taken into account.⁸¹ The court simply stated that,

Here, the present value is irrelevant. The trial court chose not to give Bette an immediate right to receive some portion of the present value of Robert's pension benefit, either in a lump sum or over a period of years. In other words, the trial court did not divide the present value of Robert's pension. Instead, Bette was given the right to receive a percentage of what Robert receives when he receives it⁸²

In this case the trial court and appellate court anticipated future increases in pension benefits, some of which would be tied to post-marital employment, and emphatically held that the spouse who receives a fixed percentage of the defendant's pension is entitled to share in the totality of this appreciation. The issue of whether the recipient of an *immediate offset* could receive some of this future appreciation was not discussed.

E. Virginia

In *Banagan v. Banagan*,⁸³ a Virginia trial court ordered that Brenda Banagan receive ten percent of her husband's retirement payments for as long as such payments continued.⁸⁴ Brenda appealed the pension award while her husband, Jerald, claimed that pension rights did not include rights to share in the value of any future escalation in benefits. The trial court held that benefit determination was to occur when the husband actually turned 55.⁸⁵ At the time of the divorce he was less than 40.

The defendant husband was concerned because of the greater benefits the pension could be expected to provide with the passage of time. The wife claimed that she was entitled to share in the "natural appreciation" of the husband's pension, and that not only should she share in the appreciation of the pension until her husband reached 55, but, rather, throughout his and her expected life span.⁸⁶

Citing earlier cases, the court of appeals indicated that when a pension award is payable in the future it cannot be limited to a present value calculation because such a calculation denies the benefit of future earnings and adjustments that are attributable to the deferred share of future appreciation.⁸⁷ Moreover, according to

⁸¹ *Id.* at 993.

⁸² *Id.*

⁸³ 437 S.E.2d 229 (Va. Ct. App. 1993).

⁸⁴ *Banagan*, 437 S.E.2d at 230. Both Banagans had pensions and a net value of 10 percent of the husband's pension was awarded to the wife.

⁸⁵ *Id.*

⁸⁶ *Id.* at 231.

⁸⁷ *Id.* (citing *Primm v. Primm*, 407 S.E.2d 45 (Va. Ct. App. 1991); *Zipf v. Zipf*, 382

the court of appeals, such future appreciation cannot be limited to that which occurs before age 55, the first age when pension benefits could be computed under the husband's pension plan.⁸⁸ Quite apparently, the value of pension escalation is recognized as part of the marital estate in fixed share pension distribution in Virginia.

F. *Wisconsin*

In *Arneson v. Arneson*,⁸⁹ the Wisconsin Court of Appeals rejected the claim of Ara Lee that her husband's pension was under-valued. Defendant John Arneson's actuary expert testified that the present value of his pension was \$30,242 as of the date of the trial, while Mrs. Arneson claimed a pension value, appraised at the date of retirement, of \$57,351. Paralleling the North Carolina *Bishop* case, the court of appeals held that present value must be calculated in the *current* time period and not in the future.⁹⁰ Although at retirement age 65, John's pension could have a present value of \$57,351, the court concluded that the "trial period" \$30,242 award could be expected to grow to \$57,351 by age 65, so that the same stream of post-65 expected payments could be generated.

Ara Lee asked for a fixed percentage of John's pension, but the trial court concluded that an immediate offset was more appropriate.⁹¹ The court of appeals cited a Wisconsin Supreme Court ruling as the case that established the proper methodology for valuing pensions.⁹² In that case, *Bloomer v. Bloomer*, the nonemployee spouse was able to capture post-separation appreciation through deferred distribution.⁹³ In *Arneson*, Ara Lee correctly determined that she was likely to receive significantly more value if she took a fixed percentage rather than an immediate offset, because of the capture of future appreciation with a fixed percentage distribution. Her request for a fixed percentage was denied, on the rationalization by the court of appeals that immediate offset offered important advantages.⁹⁴ No empirical basis for balancing the potentially substantial loss of value of pension benefits against "values" of such advantages was provided.

S.E.2d 263 (Va. Ct. App. 1989)). Apparently, the court was of the opinion that present value computations could not include future appreciation in benefits.

⁸⁸ *Banagan*, 437 S.E.2d at 232.

⁸⁹ 355 N.W.2d 16 (Wis. Ct. App. 1984).

⁹⁰ *Arneson*, 355 N.W.2d at 23.

⁹¹ *Id.* at 21.

⁹² *Id.* (citing *Bloomer v. Bloomer*, 267 N.W.2d 235 (Wis. 1978)).

⁹³ *See Bloomer*, 267 N.W.2d at 240.

⁹⁴ *Arneson*, 355 N.W.2d at 21.

G. Arkansas

In *Brown v. Brown*,⁹⁵ the nonemployee female spouse appealed a trial court decision that denied her a share of the cost of living increases in her former husband's pension. The defendant's military pension had an automatic annual cost of living escalator clause, but the defendant refused to give the plaintiff, Phyllis, a share in this appreciation. The court of appeals stated that no Arkansas court had confronted this issue, but that there were some decisions from other states on point.⁹⁶ In reversing the trial court, the court of appeals held that the appellant was entitled to her coverture fraction of the COLA appreciation in the pension benefit. This case dealt with a fixed percentage distribution of pension benefits, with nothing in the appeals court discussion indicating the logic of sharing benefit appreciation only in cases resulting in this form of distribution.

H. Pennsylvania

The full array of issues discussed in this paper is present in recent Pennsylvania cases. Rulings in these cases consider the risks borne by each spouse with either immediate offsets or deferred distributions, explore post-separation escalations of pension benefits, and deal with the consequences of mixing present values with deferred distributions of pension benefits. Interestingly, the clarity of vision of the Pennsylvania courts seems to have varied in a puzzling pattern over time. As a consequence, the lack of equivalence between awards with immediate distributions and those employing fixed percentage divisions has remained as an unresolved enigma for Pennsylvania courts.

In *Zollars v. Zollars*,⁹⁷ the Superior Court of Pennsylvania in 1990 dealt unequivocally with the issue of appreciation of pension benefits in connection with an immediate offset distribution. In this case, defendant husband's expert, using Pension Benefit Guaranty Corporation measures, estimated the present value of the husband's pension at \$54,825.60.⁹⁸ Both trial and superior courts agreed, instead, with plaintiff's expert who computed the value of the husband's pension at \$176,000 based on the evidence of semi-annual cost of living adjustments in the level of pension plan benefits.⁹⁹ The trial court used the coverture fraction to

⁹⁵ 828 S.W.2d 601 (Ark. Ct. App. 1992).

⁹⁶ *Brown*, 828 S.W.2d at 602 (citing *Neese v. Neese*, 669 S.W.2d 388 (Tex. Ct. App. Ct. 1984); *In re Marriage of Bocanegra*, 792 P.2d 1263 (Wash. Ct. App. 1990); *In re Marriage of Haugh*, 790 P.2d 1266 (Wash. Ct. App. 1990); *Thorpe v. Thorpe*, 367 N.W.2d 233 (Wis. Ct. App. 1985).

⁹⁷ 579 A.2d 1328 (Pa. Super. Ct. 1990).

⁹⁸ *Zollars*, 579 A.2d at 1331.

⁹⁹ *Id.* According to the court,

allocate marital versus non-marital portions of the pension and awarded plaintiff wife an immediate offset payment of \$106,013, equal to some 60% of the estimated pension present value.

Using the *frozen benefits* assumption valuation of the husband's expert, which ignores appreciation in pension benefits due to cost of living adjustments, the wife would have been entitled to a lump sum distribution of \$32,895, which the trial court had dismissed as insufficient for a 50 year old woman in relatively good health. The decision of the trial court was reversed on other grounds because it combined a present value measure with deferred distribution of actual assets.¹⁰⁰

It is notable that the clear vision apparently enjoyed by the Pennsylvania court in handling the appreciation of pension benefits in *Zollars* is somewhat clouded in subsequent rulings. In the later case of *Berrington v. Berrington*,¹⁰¹ the focus also was on appreciation of pension benefits after the date of separation. In this case, the trial court again held that *passive* increases in values of pension benefits are marital property. Citing an earlier case, the court indicated that marital claims on a pension begin at marriage and end at the date of separation with respect to all contributions to pension benefits.¹⁰² However, it noted, when the plan is vested and the value of pension benefits increases after the date of separation *due to other factors*, the increased pension value is marital property.¹⁰³ The trial court in *Berrington* explained that deferred distributions of pension funds benefit nonemployee spouses, because such a pension fund is larger "than that which

Robert claimed that the present value of his pension as of separation was \$54,825.60. Robert bases this on figures computed using the tables of the Pension Benefit Guarantee [sic] Corporation. These tables were designed for use when the employer or other pension guarantor has gone out of business, and no further growth is anticipated. This is not the case with Robert's pension which continues to grow and which will be supplemented by regular cost of living increases. Growth of the marital contribution is marital property.

Id.

¹⁰⁰ *Id.* (noting in part that "[t]he problem with the formula [used by the trial court] is that it combined a deferred distribution with an offset based on present value figures of the gross amount of all marital assets"). Of course the error complained about here, mixing deferred distribution of pension assets with a present value method, is reminiscent of the error made by the trial court in the *Seifert* case.

¹⁰¹ 598 A.2d 31 (Pa. Super. 1991).

¹⁰² *Berrington*, 598 A.2d at 37 (citing *Morschhauser v. Morschhauser*, 516 A.2d 10, 12-13 (Pa. Super. Ct. 1986)).

¹⁰³ *Id.* at 38.

would have been distributable under the immediate offset method.”¹⁰⁴ This is so, of course, if: (1) there are post-date of separation escalations of pension benefits and (2) the value of those escalations is not incorporated in immediate offset present value appraisals and distributions.¹⁰⁵ Recognizing this, the trial court based its decision on “moral” grounds.¹⁰⁶

The *Berrington* court also reviewed and compared some of the advantages of immediate offsets relative to deferred distributions indicating that, if there is risk that forfeiture may occur, deferred distribution is preferable so that both parties share the risk. Also, according to this court, deferred distribution is preferable where non-pension marital assets are insufficient to allow for an immediate offset.¹⁰⁷

The superior court found the trial court’s reasoning unacceptable. The higher court, while acknowledging the existence of reasons for preferring the deferred distribution method, such as risks of forfeiture, decreed that it would not allow an award that is higher because the plaintiff chose the deferred distribution method.¹⁰⁸ The court suggested that allowing a deferred distribution method to capture such future benefits would encourage employee spouses to quit their jobs shortly after the date of divorce to prevent ex-spouses from capturing post-divorce appreciation in pension benefits.¹⁰⁹ At the same time, the court held that post-separation escalations in pension benefits may be captured under some circumstances, as long as the appreciation is not due to contributions by employer or employee. The court clearly recognized that the immediate offset method and deferred distribution method would yield different amounts. With all of this background reasoning, in order to “compromise,” the court “suggested” that benefit determination be set at the date of separation, with projected benefits based on the defendant’s salary at that time.

According to the superior court, “the marital property calculation must yield the same pension under either method of distribution.”¹¹⁰ Of course, the only way to make the values of these alternative distributions equal is to recognize post-date of separation appreciation of benefits in an immediate offset.¹¹¹ The trial court in

¹⁰⁴ *Id.*

¹⁰⁵ *Id.* at 37.

¹⁰⁶ *Id.* at 39.

¹⁰⁷ *Id.* at 40.

¹⁰⁸ *Id.* at 38.

¹⁰⁹ *Id.* at 39.

¹¹⁰ *Id.* at 40.

¹¹¹ Alternatively, the courts could refuse to recognize post-separation appreciation in pension benefits under fixed percentage deferred distribution, but this refusal would require numerous modifications of QDROs (Qualified Domestic Relations Orders) every time benefits are raised for changes in cost of living.

Berrington recognized what was at stake and held that the nonemployee spouse was entitled to a deferred distribution to permit capture of a share of this appreciation. The superior court's response in *Berrington* was to mandate an impossibility—that is, the equalization of values that can be equal only with an adjustment (for escalations in pension benefits in the immediate offset case) while prohibiting incorporation of an allowance for escalations of pension benefits. These recent decisions suggest that the “escalation” issue will continue to be litigated in Pennsylvania unless the courts endorse a procedure for more accurately measuring the “true” value of pensions when immediate offsets are ordered.¹¹²

V. CONCLUSION

It is interesting to note that many of the cases from various states discussed above originated in 1990 or later. This, of course, reflects the rapid spread of equitable distribution standards, the accompanying increased reliance on expert valuation testimony, and an explosive growth in the volume of appeals of pension valuations. The volume of appeals of pension valuations appears to stem, in no small part, from inadequacies in the measures mandated by courts. As pension valuations are highly complex and have only recently come before courts in large numbers, it is not surprising that valuation issues have not been adequately dealt with by many courts.

Precedents established in earlier decades and even in the 1990s appear to invite litigation and to be vulnerable to attack. Most notably, the frequently (though not universally) applied assumption of *frozen* retirement benefits results in such anomalous contrasts between present values of awards with immediate offsets as opposed to deferred distributions as to demand appeal. With pensions a very significant asset among marital properties, the pressure for accurate valuation is enormous and the incentives for appealing inequitable judgments are compelling.

Correct valuation of pensions requires recognition that pension benefits can

¹¹² The continued litigation on this issue is an example of the movement of the common law towards efficiency as predicted by Richard Posner and others from the Law and Economics program at the University of Chicago. See generally RICHARD POSNER, *ECONOMIC ANALYSIS OF LAW* (3d ed. 1986); George L. Priest, *The Common Law Process and the Selection of Efficient Rules*, 6 J. LEGAL STUD. 65, 65-75 (1977) (observing that common law decisionmaking facilitates over time the efficient allocation of resources); Paul H. Rubin, *Why is the Common Law Efficient?*, 6 J. LEGAL STUD. 51 (1977) (noting in part that “resorting to court settlement is more likely in cases where the legal rules relevant to the dispute are inefficient”).

For nonemployee spouses, particularly women, many have a tremendous desire to extradite their financial affairs from that of their former spouses, but a fixed percentage of the pension will allow them to capture future appreciation. Increasingly, nonemployee spouses are appealing immediate offsets as being inadequate.

grow following separation not only because of *active* efforts of the employee spouse, but also because of *passive* adjustments for inflation or other factors. The latter adjustments, more likely to occur than not, should be considered marital property. Courts need also to recognize explicitly that, with share-of-benefits deferred distributions, nonemployee spouses share in, or capture, their marital share of the value of escalations in benefits. They also, of course, share in any plan risks.

Immediate offset distributions have a number of claimed advantages, the most frequently cited being the separation of financial affairs of the divorcing parties and the shifts in risk from the offset award recipient to the employee spouse accomplished by such a distribution. If courts are to balance these advantages against the payoff of a share of escalated pension benefits, either a *value* basis for the balancing or rights *to choose* the type of distribution preferred appear warranted. A casual assumption that the value of disentanglement and risk avoidance matches the present value of future escalations in benefits is not consistent with observed litigant behavior, i.e., with the rejection of court-mandated immediate offset pension values and subsequent appeals. That the current state of affairs invites a large volume of appeals is apparent.

In many states there appears to be ample statutory authority for the escalation of pension values to be addressed in immediate offset distributions. There does not appear to be a statutory guide for balancing subjective advantages of immediate offset payments (disentanglement and risk-shifting) against the dollar value of escalated future benefits. The current posture of most, if not all, courts does not fit well with economic evidence on the likelihood of pension escalations. This makes the anomalous treatment of immediate versus deferred, fixed proportion, distributions of pension values doubly troubling. The volume of appeals of pension valuations, largely by nonemployee female spouses, will doubtless remain elevated until there is a significant change in the valuation methodology applied by courts.

