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401k PLANS - CALCULATION OF PRE-MARITAL ACCUMULATIONS

NEGOTIATING AND DRAFTING DOMESTIC RELATIONS ORDERS

Attorneys are urged to be alert to inadvertent insertions of flawed language into the:

allocation of benefits section of the Marital Settlement Agreement

Problems arise when the subject plan is a Defined Contribution Plan (e.g., 401k Plan, Savings Plan, Thrift Plan, Individual Retirement Account) and a **Premarital Account Balance exists.**

The genesis of this problem is a practitioner's insertion into the Marital Settlement Agreement of language akin to the following:

The parties shall equally share the **marital portion** of the ABC 401(k) Plan. Any ***premarital portion*** of the Plan shall be excluded and is the sole property of the Participant Spouse. From the date of this Agreement until distribution to the Alternate Payee, the Alternate Payee's portion shall be adjusted for earnings (positive or negative).

The origin of the problem.

Counsel failed to confirm at the time of settlement that data regarding the Participant's Account Balance at or close to the date of marriage existed. Absent this data the term:

The term "Pre-Marital" has legal validity, but, as a mathematical calculation it is meaningless.

Counsel has expressed an equitable concept for the apportionment of this asset. But the data to perform the required calculations to give meaning to the words are most likely not available (especially

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if the Date of Marriage was more than 10 years ago).¹ Result: Counsel has crafted an unimplementable settlement.

To Avoid this Problem:

Attorney Tasks Prior to Drafting an Agreement Containing Pre-Marital Assets:

Confirm that the following data is ascertainable.

- ✓ The participant's account balance as of or close to the date of marriage
- ✓ Each consecutive account balance statement for from the Date of Marriage up to the Date Action for Divorce Filed ²

The Default Position (Subject to rebuttal by furnishing of ALL essential data.

When a Pre-Marital plan component exists, but the data required for the calculation does not. There is no possibility of calculating the participant's Account Balance as of the Date of Marriage.

Alternatives When Essential Account Balance Data is not available (or is no longer retrievable).

Alternative Calculation Strategies

Alternative # 1.

Coverture Fraction (Time Rule)

Alternative # 2.

Impute earnings from the Date of Marriage Value by the application of an *assumed Average* Interest Rate (based on given a given Economic Index, e.g., Moody's Aaa Corporate Debenture) for the measuring period.

¹ Plans change administrators frequently and the data does not necessarily follow to the new Administrator.

² If the End of Marriage Date (for marital property acquisition) is not current, then additional Account Balance statements are required.

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Alternative # 3.

Imputed earnings calculated from the Date of Marriage's presumed or given Value using "year by year" actual annual interest rates for the full measuring period.

Clarification.

Based on the accrual period and the initial value (which it is emphasized is generally unknown) outcomes will vary.³

However, the Imputed Annual calculation (Method #3), is most likely to replicate actual economic conditions for the measuring period, thus producing the more accurate outcome.

Clarification.

The difference between the two imputed interest methods can be substantial. The **averaging method** produces a positive linear slope, emphasizing the impact of compounding (there are no negative earning years). The **actual annual performance method**, includes possible negative earning years, producing a non-linear graph, reducing the impact of compounding, and more closely reflecting actual market conditions for the measurement period.

When a Plan with an Account Balance is the subject of negotiations, first ascertain the existence of any Pre-Marital Account Balances. If found to exist, it is suggested that you contact Troyan prior to the onset of negotiations for elaboration on the content of this article.

³ For a plan participant to retain account balance statements for more that a few years is unlikely. When the date of marriage was more than ten years ago, this probability of not having premarital account balance data is greatly enhanced.