

# **Separate Accounts for CalPERS and CalSTRS Members under Civil Code Section 4800.8 [Now Family Code § 2610]**

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## **Introduction**

This article will provide an explanation of Section 4800.8 [2610] [2610] of the Civil Code, amended by SB1190, and alert the reader to some of the potential problems associated with the application of the provisions of Section 4800.8 [2610] with respect to the division of service credit under the Public Employees' Retirement System (subsection (d)) and the State Teachers' Retirement System (subsection (c)). This article does not consider death benefits (subsection (a)) or survivor benefits (subsection (b)).

At first glance, allowing a member's service to be divided and separate accounts established seems to provide a logical solution to the disposition of the community interest in retirement benefits of CalPERS and CalSTRS members. However, closer examination reveals that only on rare occasions will such a division of community service produce separate accounts with total value similar to the value of the account if it were left undivided. Generally, the value of the nonmember's share will be significantly reduced if provisions of subsections (c) or (d) are used. But on the other occasions there is an opportunity to greatly increase the total value.

This article will demonstrate that application of the provisions of subsections (c) and (d) will generally distort the value of the benefits to be paid, usually to the detriment of the nonmember spouse. The purported advantages of subsections (c) and (d) are mostly illusory. Instead of solving the problems associated with *In re Marriage of Gillmore*, subsections (c) and (d) will usually generate more problems than they purport to solve. As this article will show, actuarial calculations can be made to illustrate the change in the value of benefits associated with particular applications of the provisions of subsections (c) or (d).

## **Provisions of Section 4800.8 [2610]**

SB1190 amended Section 4800.8 [2610] of the Civil Code and added sections to the Education Code (for CalSTRS members) and Government Code (for CalPERS) members. Section 4800.8 [2610], as amended, reads as follows:

The court shall make whatever orders are necessary or appropriate to assure that each party receives his or her full community property share in any retirement plan, whether public or private, including all survivor and death benefits, including, but not limited to, any of the following:

(a) Order the division of any retirement benefits payable upon or after the death of either party in a manner consistent with Section 4800.

(b) 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.

(c) Order the division of accumulated community property contributions and service credit as provided in Article 1.2 (commencing with Section 21215) of Chapter 9 of Part 3 of Division 5 of Title 2 of the Government Code. [For

CalPERS members]

(d) Order the division of community property rights in accounts with the State Teachers' Retirement System pursuant to Chapter 7.5 (commencing with Section 22650) of Part 13 of the Education Code. [For CalSTRS members]

Subsection (c) applies to the State Teachers' Retirement System (CalSTRS) as subsection (d) applies to the Public Employees Retirement System (CalPERS). Under these subsections, a court may order that the community service and contributions be divided into two separate and distinct accounts in the name of the member and nonmember. It is important to note that there is no requirement that the nonmember spouse receive exactly 50% of the community service and contributions.

The requirements for a nonmember to qualify for retirement benefits are:

(a) Member and nonmember must both attain the minimum age for service retirement under the benefit formula of the member.

(b) Nonmember must have been married to member who had sufficient service to retire at the time of the marriage separation.

Benefits for the nonmember are based on a "final compensation" during the community period and not during the entire career as is the case for benefits paid to the member. In other words, the "final compensation" of the nonmember is determined and frozen as of the date the parties separated under CalSTRS and date of marital termination under CalPERS. Additional provisions relate to purchase of service credit, redeposit of contributions and the like by the nonmember. The effect of these provisions is beyond the scope of this article.

At present, neither CalPERS nor CalSTRS is claiming that use of subsections (c) or (d) is mandatory. However, an argument could be made for this position based on the expressed intent of the Legislature that "this act apply to all public retirement benefits in which there is an undivided community property interest and in all dissolution of marriage or legal separation cases which are pending on the effective date of this act or in which the court has reserved jurisdiction over the benefit or not yet awarded the benefit."

The Enrolled Bill Report of CalSTRS stated the following:

Justification--This bill is needed to insure that the nonmember spouse receives his or her full community share of retirement benefits.

On the other hand, Civil Code Section 4800.8 [2610], as amended, expressly provides that (c) and (d) are orders the court *may* choose (i.e., "including, but not limited to...").

### **Separate But Not Equal**

A basic principle of community property law in California is that each party has an equal interest in community property. Common sense should indicate that it is wrong to destroy or reduce the value of an asset just so it can be divided. You don't saw the community Mercedes in half just to divide it. The value of the whole is more than the value of the parts. In most cases the value of the whole community retirement account is greater before division into separate accounts than after. How does this happen?

## **Final Compensation-- Mary's Retirement into the Freezer**

Let's look at the effect of final compensation on the retirement benefit. The basic formula for retirement benefits under CalPERS and CalSTRS is simple:

### **Final Compensation x Service x Age-factor**

If you double any factor, you double the value of the retirement benefit. If you cut any factor in half, you cut the value in half. For example:

John and Mary are both age 55. Ten years ago when they separated, John's "final average compensation" after 15 years of employment under CalSTRS during the marriage was \$3,000 per month. A separate account was established for Mary. Mary was credited with 7.5 years of the service and an attributed "final compensation" of \$3,000. John retained 7.5 years of the community service and went on to work another 10 years under CalSTRS. At this point John has 17.5 years of credited service and, due to salary increases, has a "final average compensation" of \$6,000. Both John and Mary are ready to start drawing benefits according to the familiar formula:

### **Final Compensation x Service x Benefit-factor**

John:  $\$6,000 \times 17.5 \times 0.014 = \$1,470$   
Mary:  $\$3,000 \times 7.5 \times 0.014 = \$315$   
Total: \$1,785

If jurisdiction had been retained and the community interest in the total benefit apportioned using the "time rule," the community would have received 60% of the total benefit (15 years community service over 25 years total service), and Mary's share would have been 30%.

### **Final Compensation x Service x Benefit-factor**

Total:  $\$6,000 \times 25.0 \times 0.014 = \$2,100$   
John: \$1,470  
Mary: 30%-community \$630

Mary's share under the separate account approach is \$315 payable over her lifetime. Under the retained jurisdiction approach, Mary's share is \$630 payable over John's lifetime. In the Enrolled Bill it was recited innocuously in one paragraph that "This provision would decrease program costs." Yes, indeed, by sacrificing Mary's benefit to do it.

### **Gillmore Made Worse**

Remember *Gillmore*? *In re Marriage of Gillmore* (1981) 29 Cal.3d 418, 174 Cal.Rptr. 493 held that the nonmember can choose to receive immediate payments when the member is eligible to receive benefits.

In the previous example, both John and Mary were age 55 and eligible to retire under CalSTRS. Under subsection (c) both Mary and John must have reached eligible retirement age. If Mary were five years younger, age 50, she would not be eligible to retire under CalSTRS. She

would have to wait five years before she could start receipt of her \$315 per month. Under *Gillmore* Mary has a right to begin receipt of \$630 per month starting now. "This provision would decrease program costs." Yes, indeed, by exposing the benefits payable to Mary to freezer burn.

### **Cost-of-Living Deferred**

If Mary has to wait until she has reached eligible retirement age, she also has to wait before she is eligible for post-retirement cost-of-living increases. "This provision would decrease program costs." Yes, indeed, by postponing the cost-of-living increases on Mary's benefits. Diet COLA for Mary.

### **John, Not Forgotten; Just His Benefits**

CalPERS members are covered by a continuance benefit payable after death of the member to the spouse of the member to whom the member was married at least one year prior to retirement and is married at death. If John marries Sue at least a year before he retires and is married to Sue at his death, a benefit equal to either 25% or 50% of John's retirement benefit is payable to Sue. If John has fewer years of service as a result of service being split off for Mary, the continuance benefit payable to Sue is reduced. Keep in mind that if Mary's service is a factor in the determination of Sue's benefit, Mary may have an interest in Sue's benefit. "This provision would decrease program costs." Yes, indeed, by reducing the benefits to be paid to Sue and eliminating Mary's interest in these benefits.

### **Cash-Out Pressure**

The nonmember who is awarded a separate account has the right to a refund of the accumulated contributions in the separate account of the nonmember. In most cases, the value of the accumulated contributions is less than the value of the retirement benefits. Generally, the nonmember knows even less about retirement than the member and will be more likely to cash-out. "This provision would decrease program costs." Yes, indeed, by leading the non-member to elect the less valuable alternative and cash out.

### **A Little More for CalPERS and Less for John, Too**

CalPERS has the right to levy a fee on both the member and nonmember to cover the expense in establishing and maintaining nonmember accounts, not to exceed \$4 per month. "This provision would decrease program costs." Yes, indeed, by having John and Mary help pay those costs.

### **Taking Advantage of the Situation**

Fortunately, in the effort to design provisions that would decrease program costs, a few situations were overlooked in which subsections (c) and (d) can be used to increase the total value of benefits. The increased "pie" can then be used to the benefit of both parties.

### **Sexual Arbitrage**

Females, on the average, live longer than males. If the nonmember spouse is female and the

same monthly benefit can be made payable over her lifetime rather than his, more payments are expected, and the actuarial present value of the expected payments is increased. See *In re Marriage of Verlinde* (1987) 189 Cal.App.3d 918, 234 Cal.Rptr. 694. For example, the actuarial present value of \$1.00 per month is substantially greater when it is to be paid over the life of a female, versus a male:

### Improvement

Age	Male	Female	over Male
50	133.583	146.328	9.54%
55	122.438	137.161	12.03%
60	109.186	125.877	15.29%

### Maximum Service and Then Some

The benefit formula for many safety members (fire and police members) under CalPERS is 2.7% per year for retirement at or after age 55, with a maximum benefit of 75% of final compensation. This results in the maximum benefit being earned after 27.78 years of service.

As an example, consider the case of a male member age 60 with 35 years of service and final compensation of \$5,000 per month. His monthly retirement benefit would be 75% of \$5,000 or \$3,750. The actuarial present value of this benefit stream payable over his lifetime is \$448,473. Assume this member has just separated from a 55 year old spouse to whom he has been married throughout his career. If 27.78 years of service credit are assigned to her, a monthly retirement benefit of \$3,750 is payable over her lifetime. The actuarial present value of this benefit stream is \$555,212. The member still has 7.22 years of service credit, resulting in a monthly benefit of 2.7% times 7.22 years times \$5,000 or \$974.70. The actuarial present value of this benefit stream is \$116,567. Thus, the total actuarial present value of benefits is increased from \$448,473 to \$671,779--a windfall of \$223,306.

### Disability

Members of CalPERS who have industrial disability coverage will generally obtain at least 50% of their compensation upon disability retirement regardless of their service. If circumstances are such that the member can reasonably expect to receive an industrial disability retirement, the nonmember can be assigned part of the service, retaining an amount of service in the member account so the member still meets the service requirement for service retirement and so the community service is divided into two distinct accounts, and the member will still receive the same disability retirement benefit. If the member in the previous example retires for industrial disability, a benefit of 50% of compensation will be paid in addition to the 75% of final compensation being received by the nonmember. If the credited service is split as a result of a legal separation rather than a marriage dissolution, the parties remain married, and the nonmember remains eligible for the continuing benefit. Non industrial disability is more complicated and thus beyond the scope of this article. However, it also presents opportunities to increase the total value of benefits expected to be paid.

### Health

If either the member or nonmember has health problems, these conditions need to be considered by the forensic actuary in the analysis of the value of benefits involved. As the benefits involved are expected to be paid over a different time horizon, the actuarial present

value of benefits expected to be paid is changed. If the member spouse is in poor health, a general rule would be to assign as much service as possible to the nonmember. See *In re Marriage of Bergman* (1985) 25 Cal.App. 3d 889, 102 Cal.Rptr. 225.

### **Pitfalls A Plenty**

As can be seen from the above, many pitfalls await practitioners who blindly advise clients to accept a 4800.8 [2610] (c) or (d) division of benefits. A few examples will further illustrate this point:

#### **Example 1**

Assume a male member age 60 with a community benefit of \$1,000 per month. Absent a division into separate accounts, the actuarial present value of the nonmember's one-half interest is \$54,593. If the nonmember is 63 the actuarial present value of one-half the service credit is \$71,353, an increase in value of \$16,760 or 30.70%. If all the community service (less one day, say, so the community service is divided in to two parts) is assigned to the non-member, the actuarial present value of total benefits is increased from \$109,186 to \$142,706. The "pie" has been increased in value by \$33,520.

#### **Example 2**

Assume the nonmember in Example 1 is age 50 rather than 62. In this case if one-half the service credit is assigned to the nonmember, the actuarial present value of the benefits expected to be received by the nonmember is reduced from \$54,593 to \$39,822, a decrease of \$14,771.

#### **Example 3**

Assume the nonmember in Example 1 is age 55 rather than 62. In this case if one-half the service credit is assigned to the nonmember, the actuarial present value of the benefits expected to be received by the nonmember is reduced from \$54,593 to \$50,064, a decrease of \$4,529.

#### **Example 4**

Assume a female member age 60 with a community benefit of \$1,000 per month. The actuarial present value of the nonmember's one-half interest is \$62,938. However, if the nonmember is 60 and takes one-half the service credit, the actuarial present value of his benefits over his lifetime is reduced to \$54,593.

#### **Example 5**

Assume that the nonmember in Example 4 is age 55. In this event, the actuarial present value of his one-half interest in the service benefits is reduced from \$62,938 to \$44,690.

#### **Example 6**

Assume that the nonmember in Example 4 is age 50. In this event, the actuarial present value of his one-half interest in the service benefits is reduced from \$62,938 to \$36,468.

#### **Example 7**

Assume a male member age 45 and a nonmember age 40 with an accrued community benefit of \$1,000 per month starting at his age 50. Assume he will continue in employment until age 50 and receive salary increases that average 5% per year. The actuarial present value of her one-half interest is \$57,207. If she takes one-half the service credit, the actuarial present value of benefits expected to be paid over her lifetime is \$13,142.

### Summary

The only time the provisions of Section 4800.8 [2610 - subparagraphings has changed too] subsections (c) and (d) should be used is if their use benefits the member and nonmember. That is, the use of the provisions of Section 4800.8 [2610] to establish separate member accounts is warranted only if the value of the total "pie" can be increased. Actuarial analysis is required to make this determination. Remember, division of service and contributions by themselves do not result in an equal division of community property.

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### Update

This article was published in 1990 in the Family Law News. Unfortunately, Only a small amount of "progress" has been made since then, including

- \* Separate accounts for the Judges Retirement System uses compensation of sitting judge.
- \* CalPERS has a policy of allowing a separate account order to be obtained in place of a previous "tag-along" order after death of the employee spouse before retirement.
- \* CalSTRS now has an Option 8 which is much like the CalPERS Option 4.
- \* CalPERS and CalSTRS websites are full of information and convenient to access.
- \* Some 1937 Act County plans have authorized separate accounts using final compensation of the Member at the time that the nonemployee spouse commences.

and some would argue that these constitute a regression:

- \* CalPERS has instituted a provision whereby the member spouse can later re-purchase the service credit given over to the nonmember by paying the value of the accumulated contributions if the nonmember took them out or by paying the value of the separate account. And if the nonmember took the separate account, the member can receive an actuarial adjustment in his benefits equal to the "bath" that the nonmember took. Government Code § 21251.15.
- \* CalPERS has instituted a policy not to allow Safety Members to receive more than half of the community years under a separate account. They have done this to deter the practice of giving the nonmember a full longevity retirement and a member a full disability retirement. However, it is questionable whether the law allows it.

Barbara A. DiFranza, August 8, 2004