Divorce and Retirement Plan Proceeds

Because divorce usually involves the division of assets, including some that may have tax implications, it is important to be aware of potential "tax traps," such as **vested account balances**, when you begin your retirement planning strategies.

In the past, with traditional **defined benefit plans**, such as company pension plans, participants generally received a retirement benefit, but they had no vested balance in an individual retirement account. In other words, employees had no rights to the employer's contributions to the retirement plan. However, with the popular shift toward workplace **defined contribution plans**, such as the 401(k), contributions made by employees to their retirement plan are always vested, and employer contributions vest over time, according to the schedule set forth in the plan document. Consequently, dividing vested retirement plan assets in divorce proceedings has become a complex financial issue.

Protect Yourself with a QDRO

A **qualified domestic relations order (QDRO)** is a judgment or order that involves child support, alimony, and property rights pertaining to a spouse, former spouse, child, or other dependent. A QDRO can be used to establish one spouse's right to part or all of the other spouse's retirement plan(s) and ensure that the recipient spouse pays the tax.

To be protected through a QDRO, it must specify the following:

- The name and address of the plan participant and the "alternate payee" (typically, the participant's spouse).
- The name and account number of each retirement account involved.
- The percentage (or dollar amount) of each plan that is to be paid to the alternate payee.
- The period of time or the number of payments covered by the QDRO.

The QDRO must be a part of a divorce decree or a court-approved property settlement document. The decree must also specify that a QDRO is being established under Section 414(p) of the Internal Revenue Code (IRC) and the particular state's domestic relations laws. Intent to establish a QDRO is insufficient; it must be documented in the divorce papers.

Getting divorced can be "taxing" enough, so be sure that you understand the process of dividing retirement plan assets. Through a QDRO, an individual can provide retirement funds for a former spouse, child, or other dependent, and ensure that those assets are taxed appropriately. Consult your qualified tax and legal advisors for guidance on your unique situation.

Who'll Be In Control When You Can't Be?

One thing is for certain: Life is unpredictable. But, it is still important to prepare for the future and whatever it may hold. Have you ever considered what would happen if you were to experience an accident or illness that left you incapacitated and no longer able to make important financial decisions? While this unpleasant prospect may be difficult to think about, you can prepare to establish a measure of control in your life should you become incapacitated. One strategy is to establish a **durable power of attorney**—a legal document that appoints someone you trust to handle your financial decisions.

An attorney is a licensed professional who has been granted legal authority to conduct business on your behalf. However, you have the right to provide anyone with this power. If the **power of attorney (POA)** is ***limited***, the individual you choose can conduct only that business specified in your agreement. If the POA is ***general***, the person's authority is more extensive but still assumes you are competent to review and approve decisions. If the agreement contains what is known as "durable" language (according to the passage of certain state laws), it allows the designated individual, also known as the **attorney in fact**, to make decisions on your behalf in the event of physical or mental incapacity.

The Time to Prepare Is Now

Generally speaking, a durable power of attorney allows you to specify, in advance, the person you

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