

SILENT PARTNER

The Blended Retirement System and Divorce

*Introduction: **SILENT PARTNER** is a lawyer-to-lawyer resource for military legal assistance attorneys and civilian lawyers, published by the Military Committee of the American Bar Association’s Family Law Section. Please send any comments, corrections and suggestions to the address at the end of this Silent Partner. There are many **SILENT PARTNER** infoletters on military pension division, and other aspects of military divorce. Just go to www.abanet.org/family/military (the website of the above committee) or www.nclamp.gov (the website of the military committee, N.C. State Bar) > “For Lawyers.” Credit for writing the initial draft of this **SILENT PARTNER** goes to Major Amelia B. Kays, a Policy Analyst at Headquarters Marine Corps, Manpower and Reserve Affairs, Reserve Affairs Policy Branch, in Quantico, Virginia.*

Introduction

In the National Defense Authorization Act for 2016, Congress passed legislation to modernize the retirement systems for the uniformed services.¹ This involved implementing a “blended” retirement system which combines a “defined contribution” component with a “defined benefit” program. The new Blended Retirement System (BRS), effective January 1, 2018, applies to everyone who enters service on or after that date. Certain members who entered the uniformed forces before January 1, 2018 will have a choice: to opt-in to the new system or to remain “grandfathered” in the “legacy system” (i.e., the current military retirement system).

The Legacy Retirement System

The legacy retirement system for the uniformed services is a defined benefit system. Servicemembers (SMs) with 20 creditable years of service may apply for retired pay. When active-duty SMs retire, they receive a monthly pension calculated by multiplying the average of the SM’s highest three years of continuous pay (the retired pay base) by 2.5% times the years of service (the retired pay multiplier). For example, assume that John Doe is an E-7 who served for at least three years as an E-7 and has a total of 21 creditable years. He retires in 2016 and his “high-3” (retired pay base) is \$4,423.80. John’s retired pay multiplier is 21 years of service x 2.5 = 52.5%. This means that he would receive retired pay based on 52.5% of his high three basic pay, or \$2,322.50 per month.

The current Reserve Component (RC) retirement is based on a combination of satisfactory years and points achieved each year. An RC member (that is, a member of the National Guard or Reserves) earns 15 points each year for participation, one point each day for two weeks of annual training and any other active-duty time served, and points for weekend drills, performing funeral honors, and completing correspondence courses, depending on how many hours of work are

¹ “Uniformed services” means the Army, Navy, Air Force, Marine Corps and Coast Guard, plus the commissioned corps of the Public Health Service and the National Oceanic and Atmospheric Administration.

performed. RC members must earn 50 points annually to have a satisfactory year. Once the RC member has 20 satisfactory years, he or she can apply for retirement. Although it may commence earlier, RC retired pay generally begins at age 60.

The calculation of RC retired pay is a bit more complicated than that used for a “regular retirement,” that is, one from active duty. Assume that Roberta Roe is an E-7 who has served for at least three years as an E-7 and served a total of 21 satisfactory years. She applies for discharge in 2016 and she has a “high-3” pay rate of \$4,423.80 for her retired pay base.²

Her retired pay multiplier is the number of points she earned during her career divided by 360, multiplied by 2.5%. In this case, assume that Roberta earned 365 points during her first year of service – attending recruit training and her Military Occupational Specialty (MOS) school while on active duty – and then she earned the minimum 50 points each year thereafter for 20 years. Accordingly Roberta has 365 + 1,000 points or 1,365 retirement points. The number of points divided by 360 equals 3.79 – this is the equivalent of active-duty time. This number is then multiplied by 2.5% to get the retired pay multiplier, that is, the percentage of her base pay that will establish the amount of the pension. In this case it’s $3.79 \times 2.5 = 9.475\%$.

The last step is to determine the monthly pension payment. This is the product of the retired pay base (shown above) and the retired pay multiplier just established: $\$4,423.80 \times 9.475\% = \419.16 per month retired pay.

Enter the BRS!

There are two elements in the BRS – a defined benefit program and a defined contribution component. The first of these is the same as the current retirement system except that the percentage contained in the retired pay multiplier will change from 2.5% to 2.0%. The defined contribution portion will allow the member to participate in the Thrift Savings Plan (TSP), which is similar to a civilian 401(k) plan, and the SM will receive matching contributions from the government. Starting at 60 days of service,³ the government will create a TSP account for every SM who participates in the BRS, depositing 1% of the SM’s base pay into the account. Service members will be automatically enrolled in the TSP at the rate of 3% of their base pay, but they will have the option to change this amount. At two years of service, the government will match member contributions as follows:

SM Contributes	DoD Contributes	Auto DoD Matches	SM+DoD Total
0%	1%	0%	1%
1%	1%	1%	3%
2%	1%	2%	5%
3%	1%	3%	7%
4%	1%	3.5%	8.5%
5%	1%	4%	10%

² If Roberta had applied for transfer to the Retired Reserve, her actual retired pay would be based on the current pay of an E-7 at the time the pension payments started, rather than the payment shown in the text above. Unlike a discharged SM, however, she would have been subject to recall to the Reserves or to active duty after her transfer.

³ SMs who “opt-in” to the BRS will receive 1% contributions to TSP and government matching of the contribution amount that they select when they opt-in to the BRS on the first pay period following their opt-in election.

From two years of service forward, members are vested in the BRS and can keep their DoD automatic contributions and matching amounts if they choose to separate from their uniformed service.

Continuation Pay

The BRS will also provide SMs with mid-career Continuation Pay between the beginning of the eighth and the start of the twelfth year of service. The amount of Continuation Pay will range from 2.5 to 13 times the amount of monthly base pay for active duty SMs and .5 to 6 times the amount of monthly base pay for RC SMs. Members who accept Continuation Pay will be required to serve for at least an additional three years.

Lump Sum Option

The final new component of the BRS is a provision which allows SMs to take a lump-sum payment upon becoming eligible to receive retired pay. SMs will have the option to take either 25% or 50% of their monthly pension payments between the date of retired pay eligibility (upon retirement from active duty and, for RC members, usually at age 60) and the age of Social Security payment eligibility when they retire from military service; as of this writing (2017), this is at age 67. The lump sum will be adjusted by a “Discount Rate,” which will be determined by combining the 10-year average of the Department of the Treasury High-Quality Market Corporate Bond Spot Rate Yield Curve at a 23-year maturity plus an adjustment factor intended to account for unique aspects of the military retirement program. The rate will be published annually on June 1 and go into effect on the following January 1. When the SM reaches the age for collection of Social Security, the pension payments will return to the full amount.

Opt-In Decision

Those who enter the uniformed services on or after January 1, 2018 will be enrolled in the BRS. Active-duty members entering service after January 1, 2006 but before January 1, 2018 and RC members with fewer than 4,320 points on December 31, 2017 can choose between opting in to the new system and remaining in the legacy retirement system. Members with 12 years of service (for RC members this is calculated as 4,320 points or more on December 31, 2017) will remain in the legacy system. Those SMs who are eligible to opt-in to the BRS have all of calendar year 2018 to decide whether to enroll in the new system. Anyone may access the on-line training about the BRS through *Military OneSource*, <http://www.militaryonesource.mil/>. Additional BRS information may be found at <http://militarypay.defense.gov/BlendedRetirement/>.

Impact of the BRS on Family Law

Enrollment in the new retirement system is a significant change in retirement planning. It will not only affect a member’s family; it also could affect, when applicable, the SM’s former spouse. One reason is because, under the new system, the percentage in the retired pay multiplier is reduced from 2.5% to 2.0%; thus for those who serve 20 years the pension is reduced from 50% of the “high-3” base pay to 40%. For members who have already signed a separation agreement or received a divorce decree, dissolution of marriage, property division judgment or court-ordered property settlement providing a percentage of retired pay to a former spouse, the choice to opt-in to the new retirement system will directly impact the amount of retired pay which the former spouse receives. Additionally, members or military spouses who file for divorce in cases where the SM is eligible to opt-in to the BRS will need to include provisions in their separation agreements and settlements to address how this choice affects the distribution of the marital or

community-property share of the SM's military retired pay. The same issues will be present when the case is tried, not settled; the judge will need to be educated on the options and their impact.

Another impact of the BRS on family law is the option to receive Continuation Pay at 8-12 years of service. If the member receives, say, \$10,000 in Continuation Pay, is that marital or community property? Part of the answer will depend on when it was received – before or after the date of classification according to state law (e.g., the date of divorce, date of filing or date of separation). But the bonus (for that's what it really is) must also be analyzed through a different lens as well, namely, the nature of the payment. Assume that the classification date is the date of divorce. If the payment arrives at approximately the time of divorce, will it be considered marital or community property because of its marital foundation (i.e., the years of marital military service which were a necessary foundation for the bonus), or will it be seen as non-marital property, since it is granted in exchange for a promise of future service?

Finally one has to analyze the lump-sum option for a cash amount of retired pay, taken upon becoming eligible to receive retired pay. This option will lower the funds payable to the former spouse. Can a court order bar the retiree from taking a lump sum? Probably not. Will the lump sum be considered “disposable retired pay” under USFSPA, thus making it divisible through a court order? No one knows – the rules have not been written yet. If the retiree takes this lump-sum option, the use of an indemnification clause will be essential to try to recoup for the spouse those funds which are lost (through reduced retired pay) when the member, upon retirement, decides on some “cash in hand” at the rate of 25% or 50% of the present value of the retirement.

Keep in mind that the spouse or former spouse will not receive notice from the government of election into the BRS by the military member. He or she won't be notified about the choice of a 25% or 50% lump sum payment upon retirement. How will the former spouse know about the critical – but unilateral – choices which the member makes?

The impact of the two choices (i.e., opting into the BRS and electing to receive a lump sum) will only become discoverable in most cases when the member retires. How will the former spouse know when that occurs? If a pension division order has been submitted to the retired pay center, then it is likely that the former spouse will know because of receipt of a share of retired pay. That is not true, however, if there is a VA waiver equal to or greater than the amount of retired pay. In that situation, the former spouse receives nothing, and there is no pension-share payment sent to him or her. Nothing is received, as well, by the former spouse who has not yet submitted an order to the retired pay center, perhaps thinking that the property settlement, in and of itself, accomplished the division of retired pay.

This will also need to be specifically addressed in divorce decrees and property settlements for SMs participating in the BRS. For advice on drafting divorce settlements for members and their spouses who participate in the BRS, consult the upcoming Silent Partner, “Distribution of Property Under the Blended Retirement System.”

(Rev. 08-21-2017)

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