# Estate Planning Insights

A Quarterly Publication of

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## COMMUNITY PROPERTY MURDERED BY FEDERAL AGENTS!

## *SPECIAL EDITION NO. 1*

**Introduction.** For nearly twenty years (both at this law firm and at her prior law firm), Karen Gerstner has been writing newsletters. All of the newsletters written to date can be characterized as examples of *expository* writing. The primary purpose of expository writing is to inform, explain and educate.

This Special Edition and the newsletters that will follow in this series are in a different category: *persuasive* writing. We are going to include facts and information in this newsletter (as we usually do), but we are also going to include a story and, ultimately, our opinion. We recognize that expressing an opinion can be very dangerous these days. Our intent is not to anger anyone, but to provide our thoughts regarding certain federal legislation, federal court decisions and IRS rulings over the past 34 years.

In this series of newsletters, we will focus on "retirement plans," a term that includes both "employee benefit plans" and "IRAs." In this particular newsletter, we will focus specifically on employee benefit plans that are "qualified plans" (defined later). In subsequent newsletters, we will focus on IRAs. Definition: An employee or retiree who participates in an employee benefit plan sponsored by his employer or former employer is referred to as the "participant."

Here is the essence of the problem addressed in this series of newsletters: (i) US Congresspersons and US Senators who enact federal legislation, (ii) federal judges who write opinions in federal court cases, and (iii) lawyers who write rulings for the Internal Revenue Service, who we are collectively calling "federal agents," have slowly but surely been "murdering" community property in the context of retirement plans. (It's not the best analogy, but it makes for a "more exciting" title of these newsletters.) Perhaps these federal agents have done this, and continue to do this, because *either* (i) they do not understand community property *or* (ii) they have a "common law outlook" when it comes to marital property law. It is possible, however, that some of these federal agents have taken action as a result of a bias against–and even a hostility toward–community property law. Regardless of the motive, the result is the same: a *huge* loss of valuable property rights for married people living in community property states.

**The First Murder.** Here's what happened.

Ward and June were married to each other for 30 years. They had 2 sons of their marriage: Walter and Theodore. Although the children and, especially, Theodore, got into "scrapes" from time to time, both were basically good kids.

During the 30 years of Ward and June's marriage, Ward worked outside the home and June worked inside the home. Ward and June lived in a community property state the entire time of their 30 year marriage.

Unfortunately, June died a few years before Ward retired. Ward was devastated by June's death. Ward and June had planned to travel and do other fun things together once Ward retired.

Ward and June owned typical assets at the time of June's death: their home, two cars, a joint checking account and Ward's employee benefits. Ward's employee benefits at the time of June's death consisted of a pension plan, a stock plan and a 401(k) plan. The total value of Ward's employee benefits at the time of June's death was $1,000,000. Under applicable state law, all of the assets on hand when June died, including Ward's employee benefits, were presumed to be community property. In fact, in the case of Ward and June, all assets on hand when June died were, in fact, community property under state law.

When June died, the June and Ward marriage terminated and the community property was deemed to be split. Ward kept his ½ of the community property and June's ½ of the community property became distributable to a new owner or owners because of June's death (a deceased person cannot own anything). June had a Will that gave 1/3 of her ½ of the community property directly (outright) to Ward and set aside the other 2/3 of her ½ of the community property to Ward for the rest of his life in a "life estate." June's Will also provided that, when Ward later died, if anything was left of the "life estate portion" (i.e., the 2/3 of June's ½ of the community property set aside to Ward in a life estate), that "remainder" should be distributed in equal shares to Walter and Theodore on Ward's death.

June's Will was admitted to probate. As a result, June's estate plan in her Will became effective. Note that the provisions in June's Will did not hinder Ward's continued enjoyment of the assets in any way during his life because all of June's ½ of the community property was available to Ward for the rest of his life. Of course (and as already noted), Ward still owned his own ½ of the community property after June died. Thus, after June died, 100% of the assets were available to Ward for his life for his heath, maintenance and support in his accustomed standard of living.

Here is what Ward could have done with the assets upon his death *under applicable state law* then in effect. Ward would have had the power to leave his ½ of the community property plus the 1/3 of June's ½ of the community property that June left directly to Ward to anyone Ward might choose. Only what remained of the life estate portion (i.e., the 2/3 portion of June's ½ of the community property set aside in a life estate for Ward) was not transferrable by Ward on Ward's death–the remainder of that portion was designated by June to go to Walter and Theodore on Ward's death.

Ward was very lonely and depressed after June's death. Through a work colleague, Ward met and started dating "Feisty" (we will refer to her by her stage name as an exotic dancer). One year after June's death, Ward married Feisty. At the time of Ward's marriage to Feisty, his employee benefits were worth a total of $1,100,000 (an increase of $100,000 compared to the value as of June's death). Feisty basically had no assets. Feisty stopped working once she married Ward.

Feisty had 2 children from her 2 prior marriages: a son, Bobo, and a daughter, Cinnamon. Bobo had a "spotty" work history and had spent time in prison for burglary. Cinnamon, the never married mother of 2 children by different fathers, neither of whom ever paid any child support, was receiving government benefits for herself and her children. Feisty had been providing financial assistance to both of her children on a regular basis.

By the time Feisty married Ward, Walter and Theodore were grown up. Both sons had good marriages, good jobs and two children. Ward never "warmed up to" Feisty's children and Feisty didn't really like Ward's sons either, even though Walter and Theodore were unfailingly polite and respectful toward Feisty.

Ward continued to work for his company for 5 more years after he married Feisty. When Ward finally retired from his company, his employee benefit plans, consisting of his pension plan, stock plan and 401(k) plan, had a combined value of $1,660,000.

Upon his retirement, Ward rolled over his 401(k) plan to an IRA rollover and took possession of the stock (in kind) from his stock plan. Ward also began receiving his monthly pension benefits from his pension plan.

Ward died 4 years after his retirement. Ward's primary assets at the time of his death were his IRA rollover and company stock, together worth $1,850,000 at the time of his death. In addition, Ward owned the home, two cars and a checking account. On Ward's death, Ward's former employer started paying a surviving spouse annuity to Feisty from Ward's pension plan.

After Ward died, Walter and Theodore consulted a lawyer, remembering that their mother, June, had included some provisions in her Will that related to them. Their lawyer helped them file a petition with the state probate court, asking for an "accounting" to identify the portion of the assets remaining on Ward's death that had belonged to their mother and been held in the life estate for Ward–i.e., the amount to which they were entitled per the terms of June's Will and community property law.

Feisty then hired her own lawyer, Riley Rambo, who filed a petition in the federal court, alleging that the sons' state court action had to be dismissed because it involved employee benefit plans and, therefore, it was "preempted" by federal law applicable to employee benefit plans. The federal law Feisty's lawyer cited is the Employee Retirement Income Security Act of 1974 ("ERISA"). As a result of ERISA, argued Feisty's lawyer, Feisty was entitled to 100% of the assets on hand when Ward died.

Feisty's case was heard and decided by the federal district court and then by the federal court of appeals, both of which ruled in favor of Walter and Theodore. In other words, both of those federal courts ruled that federal law (ERISA) did not preempt (override) state community property law based on the facts in the case. Therefore, the sons could receive what was left on Ward's death of the

2/3 share of their mother's community ½ interest in the employee benefit plans accumulated during the Ward and June marriage.

Finally, the US Supreme Court considered Feisty's case. After acknowledging the merits of community property law as a marital property system and noting that millions of participants in employee benefit plans worth billions of dollars live in community property states, the US Supreme Court ruled in Feisty's favor. In other words, the US Supreme Court held that the provisions in ERISA preempted state community property laws in cases like this one–cases where the spouse of the participant (called the "nonparticipant spouse") dies first (i.e., prior to the participant). Thus, per the US Supreme Court, when June died, her community property ownership interest in Ward's employee benefit plans "evaporated" into thin air. Even though employee benefits accumulated during the marriage in the community property states are treated as community property per state law (i.e., owned ½ by each spouse), if the nonparticipant spouse dies before the participant, her ½ interest in the participant's employee benefits terminates upon her death. Thus, per the US Supreme Court, June had no right to leave any portion of her community property ½ interest in Ward's employee benefit plans–even just her interest in the portion of those plans accumulated during her 30 year marriage to Ward–to her sons, Walter and Theodore, even if distribution of that portion was delayed until after Ward's death.

As a result of the Supreme Court's ruling, Feisty obtained 100% of Ward's employee benefits, including the portion accumulated during the 30 years when Ward was married to June. In addition, Feisty was able to claim the protection of ERISA even for assets that were no longer subject to ERISA at the time of Ward's death (i.e., the IRA rollover and the stock distributed in kind from the stock plan).

Of course, when Feisty dies, she will leave what's left of the assets she received on Ward's death solely to her two children, Bobo and Cinnamon. Thus, Walter and Theodore, the children of Ward and June, being the children of the marriage during which the majority of Ward's employee benefit plans were accumulated, will end up with none of those benefits.

The above story is basically the situation that was presented to the US Supreme Court in the case of *Boggs v Boggs*, with the names and amounts changed and "invented personal facts" included for human interest. The legal issues in *Boggs*, however, were exactly as described in our Ward and June story.

**Community Property Marital Property System.** (In this and the next five sections, we are ignoring federal law.) Community property is a marital property system that dates back to the Visigoths in Spain in the 5th Century. Community property has been embraced (more or less) by many countries, including Spain and France.

In the United States, there are eight (8) "traditional" community property states: Texas, Louisiana, New Mexico, Arizona, California, Idaho, Nevada, and Washington. Clearly the marital property laws in these states were influenced by the Spanish and the French. Wisconsin adopted a form of community property by statute in 1968. Thus, the nine (9) states named above can be viewed as the "true" community property states. Two states, South Dakota and Tennessee, authorize the creation of "community property trusts." Alaska allows both residents and nonresidents to create Alaska community property trusts. In addition, Alaska allows resident married couples to create, by agreement, community property not held in trust. Because community property is not the default marital property regime in Alaska, South Dakota and Tennessee (and because retirement plans cannot be placed in a trust while the participant is still living), only the nine states first named above will be considered the "true" community property states.

**Common Law Marital Property System.** The primary "other" system of marital property applies in the forty-one (41) US states that are *not* community property states (and Washington, D.C.) This other marital property system comes from English law. These 41 states can be labeled "common law" or "title" states. In a common law state, the title of an asset generally tells you the owner of the asset. In a common law or title state, if one spouse receives a paycheck, that spouse owns 100% of that paycheck. In addition, if that spouse places his paycheck into an account titled solely in his name, that spouse is the 100% owner of that account.

**Title Does Not Equate to Ownership in a Community Property State.** As we have discussed many times, in the case of a married couple domiciled in Texas (or another community property state), the title of an asset does not tell us the owner of the asset. At most, the title of an asset *may* tell us the *manager* of the asset. And in some community property states, the title of the asset does not even indicate the manager of the asset because, in those states, both spouses have management rights over the asset even if it is titled solely in one spouse's name.

In Texas, we have various types of community property based on who has the right to manage (or, *control*) the asset. Of course, many assets owned by married couples in Texas are joint management community property assets–community property subject to the management and control of both spouses. However, we also have "sole management community property"–community property that is managed solely by one spouse. *Management and ownership are two different things.* One can own something and not have the right to manage it and one can manage something and not own any ownership interest in it. In the case of community property that is subject to the sole management of one spouse (for example: one spouse's paycheck), the spouse who is managing that asset must remember that the other spouse has an ownership interest in it. In fact, the managing spouse has a *fiduciary duty* to take into account the ownership interest of the other spouse when managing the asset. The managing spouse cannot fraudulently dispose of the other spouse's community property interest in the community property asset he is managing.

Because marital property ownership in Texas is not based on the title of the asset, one must find out *how* and *when* a particular asset was acquired to determine the ownership of the asset. It's more complicated than in the common law or title states.

**Merits Of Community Property System.** Although community property is very old, it appears to be a more *enlightened* and *egalitarian* system of marital property ownership than the English system followed in the common law states. Community property is based on the idea that marriage is a type of partnership. Both spouses are considered equal partners in that marital partnership. While there are differences between the community property states, in general, all assets acquired during the marriage by either spouse (excluding gifts and inheritances and assets acquired using assets owned prior to marriage) are owned by the spouses as community property. That is true whether a spouse is working outside the home or inside the home and is true regardless of the amount of compensation paid to the spouses if both are working outside the home. Per community property law, both spouses are deemed to be contributing to the well being and success of the marital partnership. Therefore, both spouses share equally in the fruits of their labors as marital partners. Again, it does not matter if the asset acquired during the marriage is titled solely in the husband's name or solely in the wife's name or in both spouses' names. Texas is not a title state! Ownership of assets is based on how and when the assets were acquired. If an asset was acquired during the marriage other than by gift or inheritance and other than with assets owned prior to the marriage, it is community property. In fact, we have a presumption in Texas that all assets on hand when the marriage terminates–whether by death or divorce–are community property.

**Compensation = Classic Community Property.** Compensation paid to either spouse during the marriage is "classic" community property. Compensation comes in many forms, including, but not limited to salary, bonuses, commissions, fees, net profits from a business, etc. (Continuing to ignore federal law), compensation is what goes into employee benefit plans. For example, in the case of a 401(k) plan, contributions made by both the employee and the employer are compensation because they relate to services performed by the employee. Amounts placed in IRAs are deemed to come from compensation. An employer who provides a pension plan to employees is doing that based on the employment relationship (so the amounts going into the plan represent a form of compensation). As noted, compensation received by a married person living in a community property state is community property even though paid to (or, "titled") solely in the name of the employee spouse. In addition, in all of the community property states, income earned by community property assets during the marriage is also community property.

For simplicity, community property assets can be thought of as assets that are owned 50% by each spouse, in undivided interests, regardless of title and regardless of control or management rights.

As already stated, community property is an egalitarian marital property system because it takes into account and values the contributions made by both spouses to the marriage. Marriage is viewed as a partnership. In contrast, the *flavor* of the marital property laws in the common law states is one of "individualism." Each individual, including a married individual, is the sole owner of the assets that individual obtains through performing work during the marriage, which leads to compensation paid to that individual. All assets derived from that spouse's compensation are also owned 100% by him.

**Criticism Of Common Law System.** In the common law states, the contributions toward the marriage made by a stay at home spouse are basically ignored in determining ownership of the assets accumulated during the marriage. Consider the case of a typical 20th Century couple living in a common law state. The husband worked outside the home and the wife worked inside the home. As a result, all compensation paid to the husband, including his salary, bonuses and employee benefits, and all assets acquired with that compensation and titled in the husband's name were owned 100% by the husband. In that example, even though the wife may have worked just as hard at home, taking care of the children and managing the home for the benefit of the family, she ended up owning no assets at all under applicable state law. Of course, some husbands made gifts to their wives of an interest in assets they acquired, such as the family home, by titling the assets in both spouses' name. But that was a voluntary act (a gift) by the husband.

Because wives in common law states ending up owning so few assets of their own, making them more or less dependent on their husbands for support, the common law states had to pass laws mandating that a husband provide a certain minimal amount to his wife upon his death. These laws in the common law states are usually called "elective share statutes." In most common law states, married men have to leave at least 1/3 of their assets to their wives upon their death. Of course, these statutes apply to both spouses, not just husbands, but, historically, these laws were passed because many wives in common law states acquired insufficient assets during the marriage for their support after the husband's death.

**Retirement Plans.** In order to understand federal law applicable to certain retirement plans, we have to understand, at least in general terms, the different types of retirement plans.

Retirement plans can first be divided into separate categories based on whether they are sponsored by an employer or not. We may generally refer to retirement plans sponsored by an employer for its employees and retirees as "employee benefit plans." There are basically two types of employee benefit plans: qualified plans and non-qualified plans. Within the category of qualified plans, there are two sub-categories: defined benefit plans and defined contribution plans. An example of a defined benefit plan is a "true" pension plan. An example of a defined contribution plan is a 401(k) plan. Many employers sponsor multiple types of employee benefit plans, including multiple qualified plans and multiple non-qualified plans.

In contrast to employee benefit plans, the other big category of retirement plans is individual retirement accounts–IRAs. As indicated by the name, an IRA is a retirement plan that is for the benefit of an individual. An individual who has sufficient earnings can create his own retirement plan by opening and contributing to an IRA. In addition, an employee who retires or otherwise "separates from service" and no longer works for his employer may take a lump sum distribution from his employee benefit plan and roll it over into an IRA rollover.

For purposes of this newsletter, ERISA–the federal law implicated in the case reported earlier–applies to qualified plans, but does not apply to IRAs. (We are not going to discuss the few exceptions to this general rule.)

**History And Purposes Of ERISA.** As noted, ERISA is a federal law. It was passed by Congress in 1974 due to pension plan abuses (such as mismanagement and theft) and other problems (bankruptcy of the employer). ERISA was passed *primarily* as a labor law. It is co-administered by the Department of Labor (DOL) and the Treasury Department (IRS). Thus, its provisions appear in both the labor code and the tax code. The focus of ERISA was to protect participants in employee benefit plans so that they could be assured of receiving income during retirement. ERISA also included stringent rules because Congress wanted to protect "rank and file" employees.

The stated primary goals of ERISA are the following:

1. To Achieve National Uniformity in the Administration of Qualified Plans.
2. To Reduce the Administrative Burden on Plan Administrators.
3. To Insure the Payment of Retirement Benefits for Retirees and their "Beneficiaries."

With the passage of ERISA, the duties imposed on plan administrators were greatly increased. Thus, the first two stated goals of ERISA were designed (i) to make it easier for plan administrators to follow the rules and (ii) to eliminate situations in which plan administrators were at risk of paying out benefits twice, thereby depleting the plan and jeopardizing the retirement benefits promised to participants. The first two goals of ERISA are primarily "administrative" goals. A significant portion of ERISA is devoted to administrative matters.

The third goal of ERISA is concerned with two different things: (i) making sure employees who retire receive the benefits they were promised and/or earned, so that they will have income during retirement, and (ii) making sure that the beneficiaries of deceased participants receive the benefits to which they are entitled promptly after the participant's death. The first of those two goals was a direct response to pre-ERISA abuses in the management of pension plans. For that reason, the first of those two goals correlates highly with the legislative history of (and reasons for passing) ERISA. While it's true that part of ERISA's stated goals is to insure prompt payment to beneficiaries of participants who die, that is more incidental to the *original* purposes of ERISA.

To prevent "getting around" ERISA requirements, the drafters of ERISA included (i) a preemption clause and (ii) an anti-alienation clause. ERISA's preemption clause is *very* broadly worded. It states that ERISA supersedes (overrides) any and all state laws that *may relate to* any employee benefit plan. ERISA's anti-alienation clause precludes anyone from "assigning" (or, transferring) an employee benefit plan in a way not clearly permitted by ERISA. That provision is very broadly worded as well.

Over the years, a number of cases have arisen in which a particular state law has been held to "relate to" an employee benefit plan and, therefore, has been preempted by ERISA. Consider the many state laws that *could* relate to an employee benefit plan. Was ERISA really intended to override *all* of those state laws?

As noted, ERISA was passed primarily as a labor law, not a "wealth transfer law." The drafters of ERISA focused on the administration of retirement plans. They created rules to protect and preserve retirement plans for participants. They especially wanted to make sure that rank and file employees were treated fairly. And, of course, they had to include tax rules relating to retirement plan distributions. The drafters of ERISA were not thinking about retirement plans as *assets*. They were primarily thinking about retirement plans as a source of income during retirement for retired participants. As a result, the ERISA drafters did not even initially consider some very obvious matters that should have been addressed–such as what happens to a participant's employee benefits if the participant and his spouse get divorced. It took 10 years after ERISA was passed for Congress to add the Qualified Domestic Relations Order (QDRO) provisions to ERISA, allowing qualified employee benefit plans to be divided between the spouses in a divorce.

**Wealth Transfer Law**. We have stated that ERISA was not primarily concerned with "wealth transfer" matters. What is *wealth transfer*? The transfer of wealth is one of the primary goals of estate planning. Wealth can be transferred during life and/or at death. Various laws relate to the transfer of wealth. Those laws have developed <u>over centuries</u> and continue to develop all the time. For example, who qualifies as a "child" of the person who has died for purposes of distributing his assets to his "children"? It's not always a simple question, especially today when children are adopted in various ways and when some couples have frozen embryos. ERISA does not contain those types of wealth transfer provisions. And while it's true that the drafters of ERISA considered *some* aspects of "wealth transfer law" (mostly trust law, treating the retirement plan like a trust and imposing fiduciary duties on plan administrators similar to those applicable to trustees), in drafting ERISA provisions, Congress did not take into account the many potential wealth transfer matters that could arise. And now that retirement plans are the single largest asset owned by many people, the wealth transfer issues, which are state law issues, are conflicting more and more often with ERISA due to ERISA's very broad preemption clause.

Wealth transfer law is a very broad term and encompasses many things. For example, to design an effective transfer of wealth at death, the starting point is ownership of the assets. In the case of a married person, ownership of the assets depends on the marital property laws of the state in which the couple is domiciled (or, in some cases, the state in which the assets were acquired). Wealth transfer must also consider the various methods by which assets are transferred at death (by Will, pursuant to a trust instrument, via a beneficiary designation form, pursuant to the effect of a particular form of title used on the asset). A fundamental and paramount goal of wealth transfer law is *to carry out the intent of the transferor*. Compare that goal to the stated goals of ERISA (see page 5). ERISA does not have as one of its goals to carry out the intent of the participant with respect to the distribution of his retirement plans on his death. ERISA's primary focus is to provide administrative rules to be followed by all plan administrators, nationwide, thereby making it easier for plan administrators to administer retirement plans. As an example, ERISA has been held to preempt state laws that provide that if a qualified plan participant gets divorced and forgets to update his beneficiary designation after his divorce, his retirement plan must still be paid to his ex-spouse. These state laws–called "revocation on divorce statutes"–were passed based on the wealth transfer goal of carrying out the transferor's intent. ERISA doesn't care about that. Its concerns are administrative convenience for the plan administrator and national uniformity.

**REACT.** In addition to the QDRO provisions, certain other provisions relating to "spousal rights" were added to ERISA 10 years after ERISA was passed. These provisions appear in the Retirement Equity Act of 1984, often referred to as "REACT." (REACT—what a great acronym for a federal law–it's often the way federal laws get passed—as a REACTion to something.) Specifically, REACT mandated certain required "survivor benefits" for the surviving spouse of a plan participant on the participant's death. In the case of defined benefit plans (pension plans), on the participant's death, the surviving spouse is entitled to a survivor's annuity for her life. In the case of defined contribution plans (such as 401(k) plans), the surviving spouse must be named as the participant's primary beneficiary. These REACT requirements can be overcome if the participant waives them and the participant's spouse consents to that waiver in a timely manner, using the necessary written documentation. However, these spousal rights added by REACT are "default rules" that apply to all married participants (a one year marriage requirement can apply if the particular plan so provides).

Think about these spousal rights added by REACT. As we have discussed, in the common law states, the husband was often the owner of virtually all of the assets accumulated during the marriage. The husband was also usually the participant in one or more retirement plans. As noted, elective share statutes were passed in the common law states to require the deceased spouse to leave at least a portion of his assets to his surviving spouse on his death. However, in many common law states, those elective share statutes did not apply to retirement plans. Thus, the surviving spouse in a common law state may not have received sufficient assets pursuant to the particular state's elective share statute for her support after her spouse's death. So, REACT was deemed to be necessary–based on the laws in the common law states–to insure support for surviving spouses of retirement plan participants.

Remember that, per state law, in a community property state, the nonparticipant spouse would have been considered to be the *owner* of 50% of the participant's retirement plans accumulated during the marriage. Further consider this: in the common law states, the nonparticipant spouse did not acquire *any* ownership interest in the participant's retirement plans. Compare what the nonparticipant spouse was deemed to own under state law: 50% interest versus 0% interest–that's a HUGE difference!

We wonder: if the United States had been a community property <u>country</u> in 1984 (i.e., if all 50 states had community property as their marital property system), would the spousal rights provisions in REACT have been enacted? It just seems as if REACT was designed to address "support problems" for surviving spouses (and, especially, women) in the common law states. President Reagan specifically mentioned helping married women who don't work or who work part-time to explain why REACT was passed. In any event, REACT is the law.

**The Concepts Of Federalism And Federal Preemption.** A very old but still very "hot" issue is the division of powers between the federal government and the states. Remember your high school government class? We all learned that the federal government's powers were limited to the powers enumerated in the US Constitution and that all other powers were reserved to the states. This makes sense! The federal government wasn't designed to deal with "local" or "domestic" issues, such as marital property matters and estate planning matters. So those legal matters have historically been handled by the states. However, in recent years, federal laws have been encroaching into those realms. The problem is that persons serving in Congress who make these laws and the federal agents who enforce these laws often lack sufficient knowledge regarding the many different issues implicated by these legal matters.

In many federal court cases, federal judges have stated that ERISA is a "comprehensive" statute and that is why state law is preempted. ERISA may well be deemed to be *comprehensive* (and exclusive) in terms of certain administrative matters, such as reporting and disclosure. However, nothing in the legislative history of ERISA indicates that ERISA was intended to replace otherwise applicable state law dealing with traditional wealth transfer matters that are implicated when people die owning an interest in retirement plans. ERISA does not specifically address many matters that are involved in the transfer of wealth. ERISA was not designed primarily to deal with the *transfer* of retirement plans. ERISA was designed primarily to make sure participants' retirement plans would be secure and available to them in their retirement years.

**Federal Preemption Of Community Property.** Unfortunately, the trend in recent years has been for federal judges and IRS agents to determine that state laws relating to retirement plans (of all types) conflict with federal law and, therefore, federal law preempts (overrides) state law. The result has been a "massive taking" of property from married persons living in community property states. Consider the fact that approximately 100 million people live in the nine community property states. That's close to 1/3 of the US population (not a small minority). Not all of those residents of community property states are married but a significant portion of them are. Consider also that the estimated amount held in US retirement plans as of December 2017 was $28 trillion. Thus, the effect of the US Supreme Court's decision in the *Boggs* case, for example, is to deprive millions of married people (i.e., nonparticipant spouses) of billions of dollars' worth of assets (their community property interest in their spouses' qualified employee benefit plans) due to federal preemption of state community property laws.

**Opinion.** Here are *some* of the reasons we do not agree with the majority's decision in the *Boggs* case.

- Nothing in the legislative history of ERISA indicates that Congress intended to preempt community property law with respect to qualified plans.

- By the time Mr. Boggs died, the only qualified plan subject to ERISA in which he was still a participant was his pension plan. So, even conceding that ERISA preempted community property law with respect to Mr. Boggs' pension plan, so that the second Mrs. Boggs (i.e., "Feisty" in our Ward and June Story) was entitled to her survivor's annuity from that pension plan, the IRA rollover and stock owned by Mr. Boggs when he died were no longer held in qualified plans governed by ERISA. Therefore, ERISA should not have been applied to those assets. (The US Supreme Court framed the issue as whether the first Mrs. Boggs had the right to dispose of

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her community property interest in Mr. Boggs' qualified plans that were in existence when she died, but based their ruling on the spousal rights of the second Mrs. Boggs when Mr. Boggs died.)

• The *Boggs* decision is "bad" public policy. It "rewards" the nonparticipant spouse who divorces her participant husband, rather than staying married to him until her death. If the nonparticipant spouse divorces her participant husband, she can obtain a QDRO and secure her community property ½ ownership interest in her husband's qualified plans. In other words, by getting divorced, the nonparticipant spouse can legally obtain what she owns under state law, due to specific federal law authorization (i.e., the QDRO provisions). In contrast, if the nonparticipant spouse stays married to her husband until she dies, her interest in her husband's qualified plans evaporates into thin air. In other words, by staying married to her husband until her death, she loses the right to leave to anyone any part of what she *owns* and accumulated during her marriage–ever–even if that disposition is deferred until after her husband's later death. Therefore, the *Boggs* decision favors (and, perhaps, "promotes") divorce over marriage.

**The Killing Of Community Property.** As noted in our prior newsletter, a legal article written by Karen Gerstner has been published by Texas Tech Law School's *Estate Planning and Community Property Law Journal*. That article was titled, *The Killing of Community Property*. This series of newsletters addresses many of the same issues discussed in that article. Hopefully, the discussion in our newsletters will be at least somewhat less technical than the discussion in that legal article.

In our next edition in this series of newsletters, we will focus on IRAs, rather than qualified plans. So stay tuned.

<u>Contact us</u>:

If you have any questions about the material in this publication, or if we can be of assistance to you or someone you know regarding estate planning or probate matters, feel free to contact us by phone, fax or traditional mail at the address and phone number shown above, or by email sent to:

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