

Family Law Note

Recent Cases Regarding Division of Military Retired Pay When the Servicemember Elects to Receive Disability Compensation

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Family law practitioners should understand that the Uniformed Services Former Spouses' Protection Act (USFSPA)¹ permits states to divide servicemembers' disposable military retired pay² as marital property in a divorce and to pay a portion of that disposable retired pay to the members' former spouse. For example, a court order might provide that the former spouse is entitled to fifty percent of the servicemember's disposable military retired pay as part of a property division pursuant to a divorce. In this simple scenario, assuming the servicemember's disposable retired pay is \$2,000 per month, the court-ordered division requires the servicemember to pay \$1,000 per month to the former spouse.

Federal law, however, permits servicemembers to waive a portion of their disposable retired pay in exchange for a correspondingly equal amount of nontaxable³ disability compensation from the Veteran's Administration.⁴ The financial benefits to the servicemember of such a practice are obvious: receipt of nontaxable disability pay in return for waiving an equal portion of *taxable* military retired pay. Moreover, the U.S. Supreme Court has declared that state courts have no authority to treat the amount of disability payments that the servicemember elects to receive as marital property.⁵ The effect of the Supreme Court's holding is that the disability payments that the servicemember receives are his, exclusively.

In the above example, for instance, if the servicemember-recipient of \$2,000 in retired pay opted to receive \$600 of disability pay, his remaining disposable retired pay would be reduced to \$1,400 per month. Absent any provision in a court order or separation agreement that protects the former spouse's interest in her share of the servicemember's disposable retired pay, the effect of the Supreme Court's holding in *Mansell* would normally reduce the former spouse's monthly payment to only \$700.⁶

As most legal assistance practitioners understand, where the servicemember's military retired pay is divided under the terms of a separation agreement or court order, either of those documents are likely to contain an indemnity clause.⁷ The effect of such a clause, typically, is to preserve a former spouse's share of the servicemember's retired pay in the event the member chooses to accept disability compensation.⁸ When preserving the former spouse's "share," these indemnity clauses typically intend to preserve the *dollar amount*—rather than percentage amount—to which the former spouse remains entitled.

¹ 10 U.S.C. § 1408 (2000).

² "Disposable retired pay" includes a servicemember's gross retired pay less any amounts defined in 10 U.S.C. § 1408(a)(4). Section 1408(a)(4) includes recoupment by the government for overpayments, amounts of retired pay waived to receive disability pay, waiver of retired pay adjudged at court-martial, and Survivor Benefit Plan premiums. *Id.* § 1408(a)(4).

³ 38 U.S.C. § 3101(a).

⁴ 10 U.S.C. § 1408(a)(4)(B); *see also* *Mansell v. Mansell*, 490 U.S. 581, 583 (1989) (describing the procedure for waiving a portion of retirement pay in exchange for an equal amount of nontaxable disability compensation from the Veteran's Administration).

⁵ *Mansell*, 490 U.S. at 594-95.

⁶ This \$700 is arrived at by reducing the servicemember's disposable retired pay to \$1,400 and then allotting fifty percent of that amount to the former spouse in accordance with the terms of the hypothetical court order.

⁷ For example, the indemnity clause might contain language to the effect that, if the servicemember takes any action to decrease the amount of money payable to the former spouse (for instance, by application for or award of disability compensation), the servicemember must make payments directly to the spouse in an amount sufficient to compensate the spouse for the offsetting amount. *See generally* MARSHAL S. WILLICK, *MILITARY RETIREMENT BENEFITS IN DIVORCE* 230 (1998).

⁸ In some state court cases, where no indemnity clause protected the former spouse's entitlement to retired pay, the servicemember's unilateral action of reducing his disposable retired pay by accepting disability compensation left the former spouse without a financial remedy. *See, e.g.,* *Williams v. Williams*, No. COA04-21, 2004 N.C. App. LEXIS 2157 (N.C. Ct. App. 2004) (holding that the absence of a clause providing that the servicemember would indemnify his former spouse in the event he elected to reduce his disposable retired pay by receiving disability compensation left the former spouse without a financial remedy); *In re Marriage of Pierce*, 982 P.2d 995 (Kan. Ct. App. 1999) (refusing to require a servicemember to indemnify his former spouse with other assets after he reduced his disposable retired pay by electing to receive disability compensation because the couple's separation agreement contained no indemnity clause).

Several state court decisions from 2006 scrutinized *Mansell's* effect on former spouses, where servicemembers choose to waive a portion of their disposable retired pay in order to receive disability compensation. The following recent cases illuminate some general principles upon which state courts rely and of which legal assistance practitioners should take note when advising their clients. While several of these recent cases relied on the express terms of indemnity clauses contained in agreements or court orders, other cases addressed the effect on the former spouse when no indemnity clause purported to protect the former spouse's financial interests.

The Colorado Court of Appeals exercised its equitable powers, in the absence of an indemnity clause, to enforce the provisions of a separation agreement in order to preserve a former spouse's financial interests. In the case of *In re Warkocz*,⁹ the ex-wife of a servicemember appealed a lower court's refusal to enforce the provisions of a separation agreement into which the wife and servicemember had entered in 1996.¹⁰ The separation agreement provided that the wife would receive "22.5% of the service member's military retirement." The agreement apparently contained no specific indemnity clause¹¹ that would protect the former spouse's entitlement to retired pay should the servicemember choose to receive disability payments and thereby waive a portion of his retired pay. The servicemember, after retiring in May 2002, received a 40% disability rating and, predictably, waived a corresponding amount of his military retired pay.¹² In 2004, the ex-wife filed an action to collect \$5,000 in unpaid military retired pay.¹³ The servicemember, however, argued that in the absence of specific language in the separation agreement (i.e., an indemnity clause that protected the ex-wife's share of retired pay), the ex-wife was entitled only to a 22.5% share of the servicemember's reduced military retired pay.¹⁴

The lower court found that the separation agreement stated only a formulaic percentage (22.5%) of the servicemember's disposable retired pay that the ex-wife should receive, rather than a specific dollar amount.¹⁵ On appeal, the Court of Appeals of Colorado reversed, finding that the ex-wife should have continued to receive the same *dollar amount* of money she would have received if the servicemember had not applied for and received disability pay.¹⁶

The *Warkocz* court held that a court can equitably enforce the agreement of the parties, even in the absence of a specific indemnity clause that would preserve the former spouse's entitlement to a certain amount of the member's military retired pay.¹⁷ The court stated that "[m]any jurisdictions have recognized that the USFSPA does not limit the equitable authority of a state court to grant relief"¹⁸ when a member converts his military retired pay to disability pay. The court found that the economic consequences for the former spouse demand that courts consider the ramifications of the servicemember's action when crafting this equitable solution.¹⁹

The second case involves a court's reliance on the finality of court-ordered property division in a marital dissolution action. *Gurtz v. Gurtz*²⁰ addressed the effect of a servicemember's exercise of his right to receive disability payments and the resulting financial effects on his ex-wife. *Gurtz*, similar to *Warkocz*, involved the financial effects on a former spouse when the servicemember chose to receive disability pay and waive a portion of his military retired pay. Also similar to the facts in *Warkocz*, the facts in *Gurtz* revealed that no indemnity clause protected the ex-wife's entitlements to the servicemember's disposable retired pay in the event the servicemember chose to waive a portion of his military retired pay.

⁹ No. 04CA2031, 2006 Colo. App. LEXIS 480 (Colo. Ct. App. 2006).

¹⁰ *Id.* at *1.

¹¹ The court noted only that the separation agreement contained a "general indemnification clause," which apparently did not address specifically the contingency under which the servicemember opted to receive disability pay. *See id.* at *2.

¹² *Id.* at *2-3.

¹³ *Id.* at *3.

¹⁴ *Id.*

¹⁵ *Id.* The lower court concluded that ordering the member to continue to pay his ex-wife an amount of money equal to a *percentage share* of his military retired pay prior to his waiver of a portion of his retired pay would be impermissible. *Id.*

¹⁶ *Id.* at *5-6.

¹⁷ *Id.* at *7-8.

¹⁸ *Id.* at *7.

¹⁹ *Id.* at *9-10.

²⁰ No. 27134, 2006 Mo. App. LEXIS 312 (Mo. Ct. App. 2006).

In *Gurtz*, a 2002 court order required the servicemember to pay his ex-wife 42.5% of his “Military Retirement”²¹ as property, pursuant to their divorce. The servicemember had been adjudged 10% disabled, and as a result, received \$1,061 in disposable military retired pay.²² Accordingly, the servicemember paid his wife approximately \$451 each month—the 42.5% share pursuant to the court order.²³

In September 2004, however, the Department of Veteran’s Affairs notified the servicemember that his disability rating had increased to 60% disabled.²⁴ Predictably, the servicemember opted to waive his military retired pay in an amount that equaled the increased disability payments.²⁵ As a result, beginning in November 2004, the servicemember was to receive only \$350 in military retired pay, rather than the former amount of \$1,061.²⁶ In his petition for declaratory judgment to the court, the servicemember alleged that, as a result of his choice to receive disability compensation and thus reduce the amount of retired pay he would receive, he should only be required to pay his ex-wife \$149 per month.²⁷

The Missouri Court of Appeals refused to grant the servicemember’s request, finding that the previous distribution of the servicemember’s military retired pay, as part of the 2002 court-ordered property division, was not amendable.²⁸ Relying on Missouri caselaw principles of finality in matters affecting property division, the court declared that “the trial court’s marital property distribution contained in its dissolution decree became final.”²⁹ The court ultimately declared that “[o]nce it has been divided as part of a final decree, a pension may not be redivided after circumstances have changed.”³⁰

Several recent cases have also addressed the enforceability of express indemnity provisions affecting entitlement to military retired pay. *Poziombke v. Poziombke*,³¹ decided by the Virginia Court of Appeals, involved the interpretation and effect of an indemnity clause that purported to protect an ex-wife’s financial interests in a servicemember’s disposable military retired pay. The indemnity clause, included in the couple’s 1995 divorce decree, provided that the servicemember would “not take any action which would defeat, reduce, or limit [the ex-wife’s] right to receive her share of [the servicemember’s] military pension benefits.”³² The clause continued by providing that if the servicemember did take any such action, such as “waiving any portion of retired pay in order to receive increased disability pay,”³³ the servicemember would indemnify his ex-wife and pay directly to her “all sums reduced by such action.”³⁴

In June 1998, the servicemember retired and began paying to his wife approximately 28% of his disposable retirement pay each month under the terms of the 1995 dissolution order.³⁵ In October 1998, the servicemember opted to accept disability payments,³⁶ and in 2005, his ex-wife petitioned the court for payment of the amount of retired pay due to her, as a result of his waiver of retired pay.³⁷

²¹ *Id.* at *2.

²² *Id.*

²³ *Id.*

²⁴ *Id.* at *4.

²⁵ *Id.* at *3.

²⁶ *Id.*

²⁷ *Id.* This \$149 per month, the servicemember petitioned, equaled the court-ordered 42.5% share of his disposable retired pay that his ex-wife should receive after he reduced his disposable retired pay to \$350 per month. *Id.*

²⁸ *Id.* at *9.

²⁹ *Id.* (citing *Wandfluh v. Wandfluh*, 716 S.W.2d 420, 422 (Mo. Ct. App. 2003)).

³⁰ *Id.* (quoting *In re Marriage of Strassner*, 895 S.W.2d 614, 618 (Mo. Ct. App. 1995)).

³¹ No. 1150-05-1, 2006 Va. App. LEXIS 61 (Va. Ct. App. 2006).

³² *Id.* at *3.

³³ *Id.*

³⁴ *Id.* at *3-4.

³⁵ *Id.* at *4. The court order required the servicemember to pay 28.3591% of his disposable retired pay. *Id.*

³⁶ *Id.* The wife showed that the total amount of disability payments that the servicemember received, and the corresponding amount of retired pay that he waived, from October 1998 to November 2004 equaled \$34,988. *Id.*

³⁷ *Id.* The ex-wife petitioned the court for 28% of the nearly \$35,000 in retired pay that the servicemember waived. *Id.*

In April 2005, the trial court ordered the servicemember to indemnify his ex-wife and pay to her the amount of money to which she would have been entitled, had he not elected to receive disability payments beginning in October 1998.³⁸ Citing the finality of the order dividing the couple's property in the 1995 divorce action, the court required the servicemember to indemnify the ex-wife; the court did not, however, require the servicemember to pay her directly from the disability benefits he received.³⁹

The servicemember appealed, arguing that absent an indemnity clause in a property settlement agreement—as opposed to one contained in a court order—federal law prohibits a court from ordering servicemembers not to take actions that have the effect of reducing a former spouse's entitlement to military retired pay.⁴⁰ The Virginia Court of Appeals rejected the servicemember's argument. In its opinion, the Virginia Court of Appeals declared that a court may order a servicemember to pay a sum *equivalent* to a percentage of military retired pay or disability pay, where an indemnification clause protects the former spouse's right to such an amount.⁴¹ The only caveat, the court declared, was the prohibition on ordering the servicemember to make such payments from the disability payments themselves.⁴²

The Texas Court of Appeals case of *Loria v. Loria*,⁴³ similar to the *Poziombke* decision, examined the validity of a court order that contained an indemnity clause. At issue in *Loria* was court-ordered indemnity language that provided that the servicemember agreed “not to pursue any course of action that would defeat [the spouse's] right to receive a portion of the disposable retired pay of [the servicemember].”⁴⁴ The clause further provided that the servicemember would not “take any action . . . so as to cause a limitation in the amount of the total disposable retired pay in which [the servicemember had] a vested interest.”⁴⁵ The indemnity clause further provided that if the servicemember took any action to reduce the amount of his disposable retired pay, he must pay directly to his ex-wife an amount equal to the amount of disposable retired pay that the court ordered paid to his ex-wife.⁴⁶

The servicemember objected to the court order, alleging that the language in the indemnity clause impermissibly proposed to divide any disability benefits he might elect to receive.⁴⁷ On appeal, the Texas Court of Appeals agreed with the servicemember, finding that the language “has the impermissible effect of precluding [the servicemember] from choosing, as is his right, to waive a portion of his retirement pay for disability.”⁴⁸

The full ramification of the *Loria* decision is unclear at this point. *Loria* represents a departure from the majority of state court decisions which, up to this point, permitted the indemnification of a former spouse on the theory that the servicemember remained free to waive retired pay in order to receive disability pay, so long as he paid to the former spouse the share that she otherwise would forfeit due to his actions. Numerous state courts have validated courts' indemnity provisions, finding that the requirement to make the former spouse “whole” did not impermissibly require the servicemember to pay the former spouse directly from the disability funds that the servicemember elected to receive.⁴⁹

Legal assistance practitioners who advise clients on the interplay between receipt of disability pay and military retired pay must ensure that they address the issue of indemnification. Practitioners must understand—or be prepared to research—the approach used by state courts in addressing the issue of indemnification of a former spouse. Practitioners must understand whether a state might enforce the original intent of a court order or agreement through the employment of

³⁸ *Id.* at *4-5.

³⁹ *Id.* at *5-6.

⁴⁰ *Id.* at *7.

⁴¹ *Id.* at *5-6.

⁴² *Id.* at *6.

⁴³ No. 01-05-00380-CV, 2006 Tex. App. LEXIS 322 (Tex. App. 2006).

⁴⁴ *Id.* at *2.

⁴⁵ *Id.* (emphasis in original).

⁴⁶ *Id.*

⁴⁷ *Id.* at *4.

⁴⁸ *Id.* at *6.

⁴⁹ See, e.g., *In re Gahagen*, No. 4-272/03-1731, 2004 Iowa App. LEXIS 926 (Iowa Ct. App. 2004); *Nelson v. Nelson*, 83 P.3d 889 (Okla. Civ. App. 2003); *Janovic v. Janovic*, 814 So.2d 1096 (Fla. Dist. Ct. App. 2002).

equitable remedies when no indemnity clause exists.⁵⁰ The better practice, of course, is to ensure that an indemnity clause specifically protects the former spouse's entitlement to retired pay in the event the servicemember reduces his disposable retired pay by electing to receive disability compensation. Finally, practitioners must understand which state courts might order the servicemember to make the former spouse whole by indemnifying the former spouse from funds other than the disability pay that the servicemember elects to receive.⁵¹

⁵⁰ See, e.g., *Surratt v. Surratt*, 148 S.W.3d 761 (Ark. Ct. App. 2004); *Black v. Black*, 842 A.2d 1280 (Me. 2004); *Whitfield v. Whitfield*, 862 A.2d 1187 (N.J. Super. Ct. App. Div. 2004).

⁵¹ See generally ADMINISTRATIVE & CIVIL LAW DEP'T, THE JUDGE ADVOCATE GENERAL'S SCHOOL, U.S. ARMY, JA 274, UNIFORMED SERVICES FORMER SPOUSES' PROTECTION ACT (Nov. 2005) (examining state courts' treatment of indemnity clauses and the interplay between waiver of military retired pay and the receipt of disability pay).