

Post-Divorce Planning

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Post-Divorce Planning

Practical Planning for Practitioners

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MEMORABLE QUOTE

● "Marriage is often due to lack of judgment, divorce to lack of patience and remarriage to lack of memory"

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Post-Divorce Planning

Divorce Statistics

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Divorce Statistics

● According to a March 3, 2012 article in the Wall Street Journal, entitled "The Gray Divorces," the divorce rate for Baby Boomers' is increasing, even while it has been diminishing for other demographic groups.

● "Among divorces by people ages 40-69, women reported seeking the split 66% of the time."

● 61% of widowers are engaged in a new romantic relationship within 25 months of their wife's death, versus 19% of widows

● 20% of men in second marriages marry someone who is at least 10 years Younger than them.

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Educate and Collaborate

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Educate and Collaborate

- Clients must be educated about the vital importance of post-divorce clean up and new planning. Few understand the ramifications and many, perhaps most, assume that once the final divorce decree is received they are finished with legal and related matters.
- Collaboration is essential to best helping post-divorce clients. Many of the planning steps discussed below involve multiple disciplines.

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Post-Divorce Planning

Difficulties and Importance of Post-Divorce Planning

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Importance of Post-Divorce Planning

- Critical steps are almost always missed in the divorce process itself.
- The follow up list might touch every aspect of the divorced client's life: financial planning, investments, insurance, legal, estate, etc.
- Matrimonial counsel often do not address the myriad of ancillary, multi-disciplinary issues in the divorce process itself.
- Failure to follow up on post-divorce loose-ends can undermine the client's financial security, retirement goals, and much more.

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Post-Divorced Clients are Often Loathe to Address These Issues

- Divorce is often a difficult, costly and unpleasant process and many recently divorced clients simply do not have the desire to deal with more issues once the divorce is finalized.
- After having just incurred the professional fees to complete the divorce process many clients will not be willing to incur yet additional professional fees.
- Not all advisers educate their clients as to the importance of post-divorce issues and hence the clients fail to understand how important the "clean up" process to the success of their post-divorce lives.

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Review the Divorce Documents

- General Caveat: Make sure any post-divorce changes are in compliance with the divorce decree and settlement.
- Consider Modification of the Divorce Documents if needed.

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Post-Divorce Planning

Step 1: Take an Inventory

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Assemble an Inventory - 1

- The threshold step to guiding any post-divorce client is so obvious that it might not need to be stated, but even if practitioners are aware, clients need to be informed.
- An inventory of assets, legal documents, financial details, etc. must be assembled. Even if the client was a client before the divorce much of the data has changed.

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Assemble an Inventory - 2

- During the divorce process the focus is often on settlement matters, not the nuances of implementation.
- The only way to know which beneficiary designations, asset titles, etc. need correction is to first identify the starting point of what exists, how it is held, what the divorce agreements provide for. Only then can the necessary steps be identified.

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Post-Divorce Planning

Budget and Investment Allocation

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Start the Post-Divorce Financial Plan from Scratch - 1

- Divorce changes every aspect of financial planning. Budgets change radically. Living separately is often not much less costly the living together. What are the new numbers?
- Assets are often divided to achieve a number of divorce goals, e.g. to allocate investment accounts to equalize capital gains exposure. In many divorces financial assets are allocated in whatever manner seems to expedite the conclusion of the divorce.
- The client needs to create a post-divorce budget that reflects new economic realities, including reasonable estimates of income from alimony (or the expense of paying alimony), income from child support relative to the actual anticipated costs of caring for the children (or the cost of paying child support plus the actual cost that the payor parent may incur in caring for the children).

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Start the Post-Divorce Financial Plan from Scratch - 2

- What is the financial impact of new post-divorce obligations? Example, the cost of housing plus the alimony component that was estimated for housing may be significantly more for the payor than the pre-divorce housing costs. There may be new expenses to fund divorce mandated life insurance.
- New retirement financial goals should be set reflecting the new realities.
- Financial forecasting should be completed to ascertain whether the client can realistically achieve the new targets or whether budget cuts or other steps should be taken.
- A new asset allocation model should be developed to reach the client's new post-divorce goals. That model should then be implemented with consideration to near term cash needs that may be one-time post-divorce events.
- The sooner the client addresses post-divorce financial planning (new budget, revised asset allocation targets, modification of existing investments to move towards the new targets, etc.) the better.

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Start the Post-Divorce Financial Plan from Scratch - 3

- Some estate planners and even CPAs view these financial steps as not within their purview. Whether or not that is the case, it is vital for all planners, of any discipline to educate and encourage clients to follow up on revising their financial planning post-divorce.
- The results of the financial forecasts should be considered in reassessing all estate planning documents. While every estate planner knows that documents must be revised to at minimum name new agents and change dispositive schemes, the new financial realities must be considered as well:
 - If the client created a hybrid DAPT (a domestic asset protection trust of which the client can be added as a beneficiary) might it be necessary for that trigger to be pulled making the client a real beneficiary?
 - If the client has irrevocable grantor trusts that have not reimbursed the client for tax costs might that now be necessary from a financial planning perspective? If the existing irrevocable trusts do not have the ability to reimburse perhaps they can be decanted into trusts that do permit tax reimbursements.
 - Annual and other gift programs should be evaluated.

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Post-Divorce Planning

**Beneficiary Designations;
Retirement Plans;
IRAs**

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Beneficiary Designations Should Be Updated - 1

Change Beneficiary Designations on:

- ERISA Qualified Plans, but only after the divorce is finalized, or with signed spousal approval before divorce.
- IRAs.
- Deferred Compensation Plans.
- Stock Option Plans.
- Life Insurance Policies.
- Accounts Paid to the Order of, or Paid at Death (POD) to the Ex-Spouse.

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Beneficiary Designations Should Be Updated - 2

- Evaluate the benefit of naming trusts as beneficiaries even if this had not been done in the past. The post-divorce client may wish to protect a child's inheritance from what they might now fear could be inappropriate influence by the now ex-spouse.

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IRAs and Retirement Plans

- The 4th Circuit Court awarded all of a Decedent's ERISA Retirement Funds to an Ex-wife because a Beneficiary Change (made 3 months before the divorce was finalized) was not signed by the Ex-wife
- In Merchant v. Corder, (1999 WL 486590 (unpublished opinion) (4th Cir. 1998)), the Fourth Circuit Court of Appeals ruled that a change in beneficiary designation to a retirement plan prior to the issuance of a final judgment of divorce was invalid. Because the ex-spouse had not agreed to the relinquishment of her rights to the plan at the time of the change and there was not a qualified domestic relations order, when the former husband died the ex-spouse received the entire retirement fund.

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Pension Plans and Domestic Relations Orders

A divorced Wife's failure to file a valid Domestic Relations Order with the Pension Administrator before the former Spouse's Retirement, Eliminated the Wife's rights to the Pension Plan. Langston v. Wilson McShane Corporation.

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Failed IRA Decisions

A divorcing Husband cashed out an IRA and paid cash to the Ex-Wife instead of 50% of his IRA, expecting the Ex-Wife to be Taxable on the Cash Out

- > All Taxable Income to Husband.
- > 10% Early Withdrawal Penalty.
- > Husband paid an extra \$68,750.
- > Wife Received \$111,000 Tax Free.

One case may give a client pause when trying to extract revenge from a wife in divorce. In the ruling, a couple divorced and the wife was entitled to half of the husband's IRA. The husband cashed out the IRA and paid the cash to her. He apparently anticipated that she would be responsible for both the income taxes and the early withdrawal penalty on the \$111,600 withdrawal. Instead, it was ruled that all the taxable income went to the husband, and he was responsible for the 10% early withdrawal penalty, resulting in his paying all of the taxes and penalties, while the wife got \$111,600 tax free. To avoid this situation, the husband should have either directed the plan administrator to change the name on the IRA account, or make a trustee to trustee transfer to the wife's IRA account. *Bunney 114 TC 259 (2000)*.

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Post-Divorce Planning

Revise Asset Titles

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Review and Revise Title to Assets

- Residence ownership.
- Bill of Sale on Personal Property
- Other real estate ownership.
- Automobiles, boats, etc.
- Stock or equity rights in a business or investment (be certain the client obtains any original certificates held by the now ex-spouse).
- Brokerage accounts.
- Life Insurance (e.g., ex-spouse owns policy).
- Fertilized Embryos & Reproductive Assets
- Hotel, Airline & Other Travel Perks
- Relinquishment of any rights to a family burial plot. It may be easier to surrender the plot and have the client purchase new plots or make new arrangements.

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Stored Reproductive Assets

[Redacted]

Alabama Statute 26-17-706(a):

If a marriage is dissolved before placement of eggs, sperm, or embryos, the former spouse is not a parent of the resulting child unless the former spouse consented in a signed record, maintained by the licensed assisting physician, that if assisted reproduction were to occur after a divorce, the former spouse would be a parent of the child.

Danger: Placement of eggs during the divorce proceeding

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Travel Perks

[Redacted]

“Miles are not the property of any member. Except as specifically authorized in the Membership Guide and Program Rules or otherwise in writing by an officer of Delta, miles may not be sold, attached, seized, levied upon, pledged, or transferred under any circumstances, including, without limitation, by operation of law, upon death, or in connection with any domestic relations dispute and/or legal proceeding.

Source: Delta Airlines website

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Post-Divorce Planning

Terminate Joint and Other Liabilities

[Redacted]

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Terminate Liabilities - 1

- Terminate joint or other liabilities that might still affect your client:
- Credit cards. Merely cancelling a card may be insufficient. Confirm with each credit card company that the client has been removed.
- Lines of credit. Inquire about standby lines, etc. that may have been established years earlier and which no one remembers.
- Utilities. Clients may assume that if they have moved out and the have no responsibility for utilities in the old marital home that they have been removed from liability. But if they have not updated records with the utilities they may be still held responsible.

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Terminate Liabilities - 2

- Personal guarantees for ex-spouse's liabilities (e.g., for loan to ex-spouse's business).
- Mortgages unless relief of liability is not be permitted by the terms. If not, were reporting requirements instituted as part of the divorce settlement? If not is it feasible to get reporting now? Might the lender be willing to send default notices to the client/guarantor?
- Review the client's personal income tax return Form 1040 and pre-divorce financial statements for clues as to possible liabilities, as well as the body of and exhibits to the divorce documents.
- Consider ordering lien and judgement searches to identify possible liabilities that the client may not remember.

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Post-Divorce Planning

Terminate Joint Accounts

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Terminate Joint Accounts - 1

- Terminate joint accounts (and change direct deposits to these accounts) unless expressly mandated to be retained pursuant to the marital settlement agreement.
- Bank accounts, including checking, savings, etc.
- Review the client's personal income tax return Form 1040, Schedule B for possible accounts, as well as the body of and exhibits to the divorce documents.
- Brokerage accounts. Look for items not held at the brokerage firm but simply noted on a statement as a memorandum entry as separate steps may be required to address those.

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Terminate Joint Accounts - 2

- Safety deposit boxes. Not only should the title be changed by the key as well. It may be simpler, safer and potentially less costly, to have the client surrender the old box and open a new one. Recommend the client inventory the box. Also, if the client should consider whether a secondary person can be granted access to the box in the event of disability or death.
- Terminate automatic withdrawals (e.g. to ex-spouse's account or benefit).

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Post-Divorce Planning

Remove Ex-Spouse as Authorized Signer

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Remove Ex-Spouse as Authorized Signer or Person to Access Account Information

- Terminate permitted access or signing authority previously granted to the ex-spouse, for example:
 - Personal banking (i.e., checking, savings, etc.)
 - Business payroll service. Business checking accounts, and accounts with vendors.
 - Personal brokerage accounts.
 - Credit card accounts. This can be separate from being able to access credit. That may have been terminated but the ex-spouse may be listed on credit card records as a person authorized to call and inquire as to account matters.

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Post-Divorce Planning

Address Changes

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Address Changes - 1

- File a change of address and/or name change wherever appropriate.
- Notice to post office.
- IRS notification. For tax filings file IRS Form 8822 for address changes, Form 56 to report a change in fiduciary (e.g. client's ex-spouse resigned as trustee of insurance trust pursuant to terms of divorce).
- Employer payroll and benefit plans.
- Creditor, credit card, bank, and financial accounts.
- Insurance policies, including: auto, property, casualty, liability, etc.
- Medical coverage.

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Address Changes - 2

- Driver's license.
- Voter registration.
- Firearms registrations.
- Passport.
- Military and Veterans Benefits.
- Social Security Administration (go to www.ssa.gov for the form).

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Post-Divorce Planning

Update Estate Planning Documents

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Update Estate Planning Documents - 1

- Revise, all estate planning documents to reflect the divorce.
- Revise will especially if revoked by divorce under state law.
- Revocable trust modifying gift provisions if appropriate, removing ex-spouse and family members as fiduciaries or beneficiaries, etc.
- Medical directive or healthcare power of attorney removing ex-spouse and relatives as fiduciaries.
- Powers of attorney. Endeavor to collect any original powers the ex-spouse holds for destruction. The client should sign new powers naming new agents.
- Reconsider gift strategies and other provisions in light of the client's new financial realities.

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Update Estate Planning Documents - 2

- Decide whether to retain or fund any irrevocable trusts (insurance or otherwise) which name spouse as beneficiary or in fiduciary and non-fiduciary capacities.
- Notify third parties of changes made to fiduciaries.
- If the client has named the ex-spouse or relatives of the ex-spouse as beneficiaries and/or fiduciaries determine if they have renounced their rights or if not whether their renunciations can be obtained.

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Update Estate Planning Documents - 3

- Remember to evaluate all positions/appointments in irrevocable trusts, including powers that might be exercised in a non-fiduciary capacity. Consider all fiduciary positions which might include: investment trustee, trust protector, and specialized functions.
- If the ex-spouse or family member is unwilling to cooperate evaluate options.
 - Can a trust protector terminate that recalcitrant ex's position?
 - Can the trustee decant and remove that person or the position?
 - Might a non-judicial modification accomplish the same result or will that person's consent be necessary?

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Adopting an Adult

In *Goodman v. Goodman* the divorced creator of a 1991 Irrevocable Trust for the benefit of "my children" adopted his 42 year old girlfriend so she could gain access to a portion of the \$300 million in trust funds. The ex-wife as legal guardian of the two current trust beneficiaries objected. The court terminated the adoption on a procedural basis.

- It should be noted that Florida's law, like many states, specifically permits the adoption of adults. Florida statute section 63.042(1) provides: "Any person, a minor or an adult, may be adopted." The core issue is whether public policy should override a state statute because of the illegal incestuous relationship that such an adoption creates. Authorities differ in their perspectives.
- For a more detailed analysis of this issue, see: Baskies: "Goodman v. Goodman: Florida's 3rd District Court of Appeal Addresses Intriguing Adult Adoption Case, Was the Adoption of Goodman's Girlfriend a Bright Idea or Bad Public Policy?" LISI Estate Planning Email Newsletter - Archive Message #2089 (April 16, 2013); *In re Adoption of Robert Paul P.*, 63 N.Y. 2d 233, 236 (1984); Review this website: <http://adoptingback.com/adopting-back/united-states-adult-adoption-law/>.

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Post-Divorce Planning

Agency and Other Designations on Ancillary Documents

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Agency and Other Designations on Ancillary Documents - 1

- Review all estate and ancillary documents and appointments to identify a range of possible agent or similar appointments that might have been given to the ex-spouse any of which may be independent of the clients' estate planning documents. Determine if the ex-spouse should be removed and if so the steps or mechanism for doing so.
- Brokers may be required, under FINRA Rule 4512, "Customer Account Information," to make reasonable efforts to obtain the name of and contact information for a trusted contact person for a customer's account.
- Lapse designee on long term care insurance policy. The insurance contract itself may provide for the designation of a person to receive secondary notice before a lapse can occur. Some state laws require such a procedure.

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Agency and Other Designations on Ancillary Documents - 2

- Account Holders on 529 and 529A plans, and successors. Bear in mind the account holder can withdraw all funds in a 529 plan.
- Agent for Funeral Decisions. Some state laws permit the appointment of an agent to control the disposition of a person's remains.
- Social Security Representative Payee.
- If the ex-spouse was designated as an agent under funeral home documents or state law to make funeral arrangements revoke those appointments.
- Remove the ex-spouse as an officer or director of any business entities; Revise the filing with the applicable Secretary of State.

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Post-Divorce Planning

Insurance

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Update Insurance Coverage - 1

- Changes in personal or employer-based insurance coverage that names ex-spouse if permitted by the divorce decree (perhaps obtain a refund).
- Life insurance. Review new post-divorce other insurance needs and financial resources.
- If the settlement agreement mandates the ex-spouse provide coverage for your client endeavor to have the insurance company notify your client in the event that the required policy is in default so it can be cured before lapse.
- Health insurance. Can the client continue existing coverage? Obtain coverage through the client's employer? How will changes in coverage affect financial security?

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Update Insurance Coverage - 2

- Long term care insurance. If coverage had not been previously purchased because of a perceived family safety net the same analysis now might suggest the need for insurance.
- Disability insurance. Review not only address and other administrative data, but does the coverage and cost remain appropriate in light of new financial realities? If financial reserves have been depleted might a shorter waiting period or lower cost be advisable?
- Property, casualty and liability insurance (e.g., auto, home, umbrella) should be updated to reflect change in risks and assets (e.g. post-divorce the family boat was sold).

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Post-Divorce Planning

Change Access Codes and Passwords

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Change Access Codes and Passwords

- Change access codes and passwords, for all accounts.
- Web or app that holds passwords (e.g., Keeper Security).
- Web based access (e.g., bank, brokerage)
- Credit, debit and ATM Cards
- Frequent flyer accounts.
- Email accounts. If there personal or family website, Twitter account, or email account has this been addressed? Who retains it? Who has access?
- Personal safe.
- Alarm and security codes for properties such as residence, vacation home, public storage facility.

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Post-Divorce Planning

Change Locks

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Change Locks

- Change access and the locks to all assets.
- Change the location of any hidden keys (do not just have the client take back keys).
- Personal home.
- Homes or apartments used by children or other family members.
- Vacation Home.
- Office.
- Personal Safe.
- Mailbox.

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Post-Divorce Planning

Income Tax Considerations

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Income Tax Considerations - 1

- Be certain that the client is correctly reporting receipts or disbursements resulting from the divorce. Review the governing documents and confirm to post-divorce tax filings.
- Alimony is Earned Income. I.R.C. §219(f)(1) provides that alimony is considered earned income for IRA funding purposes. Allocating a portion of any settlement to alimony creates an income tax deduction for the payer and allow the payee to fund a tax-deductible IRA contribution I.R.C. § 219(f)(1) (2016).

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Income Tax Considerations - 2

- Review all irrevocable trusts to be certain that they have been properly reported for income tax purposes. Sometimes the ex-spouse will be found to be the grantor for income tax purposes of a trust that had been treated as a complex trust.
- Any divorce settlement agreement should require that the transferor spouse provide the transferee spouse with sufficient records to support both the basis of the property and its holding period. Without such information, the IRS could challenge the transferee's unsupported tax filings. Was this information obtained? In some cases the provisions of the marital settlement agreement mandate that such information be provided but sometimes this was never followed up on.

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Alimony Mistakes

- If there is any Obligation to make an alimony payment (or a substitute payment) after the Recipient's death, all such payments, including those paid before death, are not Deductible Alimony.
- Payments made to a Spouse before a Divorce or Separation Agreement is signed may not qualify as Alimony.
- Caution: The Alimony Deduction Claw-back rules of IRC § 71(f).

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Expect More Alimony Audits

- CAUTION: A 2014 Treasury report noted that 47% of the examined tax returns claimed alimony deductions for which income was not reported on a corresponding recipient's tax return or the amount of alimony income reported did not agree with the amount of the deduction taken.
- Expect more Audits on this Issue.

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Trust Reporting

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Trust Reporting

- Many irrevocable trusts, or applicable state law, require that beneficiaries receive notice concerning the trust. Your client might want to assert this right on behalf of minor children beneficiaries and demand notice in the form of annual trust statements for trusts.
- If your client is the settlor or trustee and wants to thwart an ex-client from receiving details about a trust for the children, it may be possible to appoint a designated representative other than the ex-spouse to receive that notice.

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Conclusion and Additional Information

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Conclusion

- Almost invariably every divorce leaves many loose-ends that should be addressed.
- Practitioners will have to educate clients about the importance of this follow up and assure them that the costs and difficulties should not deter them.

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Additional information

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