In Tomorrow We Trust

Take a fresh look at your future and implement a new estate plan

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IN DIVORCE PROCEEDINGS, INDIVIDUALS EXPERIENCE EMOTIONAL TURMOIL, FINANCIAL UNCERTAINTY, AND PERSONAL CHALLENGES THAT ARE UNSETTLING, BUT EXPECTED. Peace of mind is illusory for a divorcing spouse. Death, serious illness, and disability, however, often occur when they are least expected. Anticipating the unexpected is a key underlying principle of estate planning, and with a sound estate plan in place during and following divorce, an individual can plan for peace of mind.

If you are planning for, anticipating, or responding to a divorce proceeding, consider your estate plan. Because states differ, you will need to talk with your lawyer about any changes you want to make. Mention, in particular, any prenuptial or postnuptial agreement you and your spouse have signed, because these may affect your estate-planning options.

Early stages of divorce

Absent extraordinary circumstances, such as a domestic violence incident that necessitates an immediate divorce petition, the spouse who files for divorce (petitioner) has time to obtain advice about revoking, amending, or revising estate-planning documents. Depending on your state laws, once a divorce petition has been filed and served, a preliminary injunction may prevent the answering spouse (respondent) from taking certain actions. Consult with your attorney to discuss any restrictions relating to a change of beneficiaries and any possible tax consequences. Most family-law attorneys do not practice estate planning but can provide referrals to other attorneys or professionals as needed during the divorce.

If you have no estate plan, there may be little to revise or revoke. If you and your spouse have prepared wills, a revocable trust, irrevocable trusts, powers of attorney for financial and health-care matters, advance directives, or engaged in succession planning for a business, then both of you will wish to revise your estate plans. Ask your attorney if there are any restrictions in the divorce case, such as a preliminary injunction that could prevent or limit your ability to change estate planning documents. Consult with an estate planning attorney, tax attorney, CPA, or corporate securities attorney for complicated estate plans, business succession plans, buy-sell asset agreements, and irrevocable life insurance trusts. It is easier to revoke or revise a less complex estate plan by complying with any state statutory formalities. The estate-planning document may specify how to revise or revoke it.

In some states, upon entry of a divorce decree, certain beneficiary designations are automatically revoked. Seek professional advice to prevent an unintended beneficiary from benefiting from an estate plan following a divorce.

Common documents

Wills and revocable trusts are the most common estate-planning documents by which a person names individuals or charities as beneficiaries of an estate upon his or her death. A will names another person or entity (such as a bank or trust company) to serve as the personal representative or executor who will administer the decedent's estate after death. There is a distinction between *probate* property, which transfers to beneficiaries through a will or trust, and *nonprobate* property, which transfers to beneficiaries by law. Nonprobate assets may include retirement plans, transfer-on-death financial accounts, jointly held property, and transfer-on-death deeds, all of which name a beneficiary.

A revocable trust can be amended and/or revoked during the lifetime of the person creating the trust (*grantor*). A revocable trust names a *trustee* (who can be the grantor during his or her lifetime) to administer the trust and manage the property owned by the trust, which can include both real property and tangible (e.g., jewelry, etc.) and intangible personal property (e.g., stocks and bonds, etc.). A *successor trustee* is named to manage the trust property after the grantor's death and to distribute assets to the beneficiaries. Although creating a revocable trust can be simple in situations involving a small estate, divorcing spouses should give substantial thought to the type of property that might be transferred to a trust and the characterization of that property as separate or community property—an important distinction in community property states—or marital and nonmarital property in noncommunity states. Otherwise, separate or nonmarital property might be transferred to a revocable trust, and despite your wish that such property remain separate or nonmarital property in the event of divorce, an improperly drafted, ambiguous, or contradictory trust clause may provide otherwise.

A *financial power of attorney* names someone (an agent) to make financial decisions if you cannot make them due to illness, disability, or incapacity. A *health-care power of attorney* names someone (an agent) to make health-care decisions in the event you are unable to do so. An *advance health-care directive*, which may be combined with a health-care power of attorney, states your wishes regarding end-of-life treatment, burial decisions, and organ donations. "Durable" powers of attorney remain effective despite a disability or incapacity, while "springing" powers of attorney become effective upon a designated event, such as an individual's incapacity.

The *Uniform Probate Code* (UPC), which has been enacted in some form in most states, provides that if an individual dies *after* a divorce is final, the ex-spouse will not be deemed a "surviving spouse." In such instances, the UPC also may prevent the appointment of an ex-spouse to a fiduciary role, such as serving as the agent in a power of attorney, the personal representative/executor, or a trustee. The UPC further may prevent the ex-spouse's family from inheriting property from the decedent's estate or serving in a fiduciary capacity. Each state's adoption of the UPC and probate laws varies, however, and consequently, it is *imperative* to determine exactly what your state's statutes provide with respect to this issue. State laws also determine exactly when a divorce decree is considered "final" in the context of the subsequent death of an ex-spouse.

Certain assets, called nonprobate assets, transfer at the owner's death to another party by law, rather than through an estate-planning document. Examples of such property include payable-on-death and transfer-on-death accounts, such as bank accounts, stocks, bonds, certain financial accounts, savings bonds, and in some states, vehicles.

Real estate, designated as "joint tenants with right of survivorship" or "community property with right of survivorship," is a nonprobate asset. In certain states, transfer-on-death deeds or beneficiary deeds also transfer real estate without having to go through a probate proceeding. Most state laws provide that certain beneficiary designations automatically are revoked upon entry of a final divorce decree, but a divorcing spouse should *not* assume so and should take steps to remove an ex-spouse as beneficiary if so desired.

A recent United States Supreme Court case held that an ex-spouse, rather than the current spouse, was entitled to the proceeds of the deceased employee's ERISA-protected retirement plan, because the decedent failed to remove his ex-spouse as the plan beneficiary, despite the ex-spouse's waiver of those benefits in the divorce decree. ERISA, which stands for the Employee Retirement Income Security Act of 1974, regulates certain employer-provided retirement plans.

Assuming you do not want your ex-spouse to be the beneficiary of a retirement plan, you *must* change the beneficiary designation of any retirement plans, including 401(k) retirement plans, pensions, or employer-provided insurance plans. The employer's human resources department or benefits department must provide you with the forms required by the plan's administrators, but the responsibility to follow through and confirm those changes is yours.

Guardians for minor children

A parent can name a guardian and alternative guardian for minor children in estate planning documents. The *guardian* is the person designated in a will to take custody of a minor child in the event of a parent's death; an *alternative guardian* is the person who will serve if the originally named guardian is unable or unwilling to do so. This is a tremendously important decision because the minor child will live with and be raised by the guardian. Depending on your state's statutes, the parent also will name either a guardian or conservator (which may be the same person) to manage and invest any property or funds the minor child inherits.

A divorced parent's designation of a guardian will *not* take priority over a surviving parent's presumed right to custody of the minor child. After a divorce, the surviving parent usually will serve as the minor child's guardian/conservator, but may not be able to do so if he or she is incapacitated or unfit or unable to parent the minor child. This is an important issue for a parent divorcing a spouse who committed acts of domestic violence, struggles with drug or alcohol abuse, or suffers from mental-health issues.

In planning for a minor child's support needs, consider the need to protect a child's interest in the estate of the parent obligated to pay child support. Negotiate a provision in

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the property settlement agreement requiring the obligor to obtain and maintain a life insurance policy on his or her life, which would specify an amount for the minor child in the event the paying parent dies. The paying parent (*obligor*) may be concerned with the cost of such a policy, whereas the parent receiving support (*obligee*) should focus on the soundness of the insurance company. The insurance provision should address several specific issues, including the amount of coverage needed for the total support obligation, the type of insurance to be used (which will depend on the age and health of the insured), and the term of the insurance.

Ideally, the property settlement agreement should identify the insurance company, the policy number, and the primary and contingent beneficiaries. The property settlement agreement should require the obligor to provide the other parent with annual proof that the life insurance policy is in effect and that premiums are paid. It also should require the insurance company to notify the other parent of any attempts to borrow against the policy or to change the beneficiary. Divorcing spouses may want to create a child support trust for the minor children as part of the divorce resolution.

Similarly, a divorcing spouse who anticipates receiving spousal support should include an insurance provision in the property settlement agreement to protect the support. This is particularly true when the spouse will be receiving a lifetime award of spousal support or maintenance. Spousal support may be modifiable, and in most cases, state law provides that the obligations terminate upon the death of the payor spouse. If the payor spouse is older or has medical issues, he or she may not be insurable. An impartial insurance specialist can provide advice on these issues.

Postdivorce

Following a divorce, consult with your attorney or other professionals to revise or create new estate plans and to replace your ex-spouse on beneficiary designations of retirement plans, IRA accounts, and life insurance policies (other than those insuring support obligations). A divorced parent, in particular, shoulders the tremendous responsibility of trying to ensure a child will obtain some measure of security in the aftermath of a parent's death, which is why an updated estate plan is essential. It is equally important to update financial and health-care powers of attorney, to name a trusted agent to replace an ex-spouse, and to revise advance health-care directives. Disability is always a frightening possibility, and as a newly divorced person, you should investigate disability insurance coverage and/or identify family or friends who could assist in such situations.

If college looms on the horizon, divorced parents with small estates can establish a Uniform Transfers to Minors Act (or Uniform Gift to Minors Act) account, through which a parent, grandparent, relative, or friend can invest money for a minor child and appoint a guardian to manage the funds during the child's minority. There are two *significant* disadvantages to this type of investment. The funds must be released to the child upon reaching the age of majority, and the funds from such accounts may have a negative effect on a child's eligibility for financial aid.

529 plans

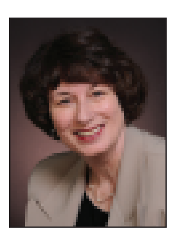
Another method for establishing a college savings plan is through use of a "529 plan," named for the section of the Internal Revenue Code that creates this tax-advantaged investment plan. A 529 plan permits a parent to set aside money for the higher education needs of a designated beneficiary, including a minor child, through a plan operated by a state, state agency, or educational institution.

The 529 plan offers tax incentives for the donors, because the earnings on the savings are not taxable for either federal or state tax purposes. The donor retains control of the funds in the 529 plan, however, and because those funds remain subject to the parent's control, the plan may count against the student for "needs based" financial aid. As a cautionary note, certain state-sponsored 529 plans recently have come under fire during the recent economic downturn, for poor management and unwise investments. Careful investors should check the viability, soundness, and investment returns provided by any 529 plan under consideration.

Special needs trusts

Finally, in planning for a divorce involving a spouse or minor or adult child with physical, mental, or emotional disabilities, seek the advice of an attorney who has expertise in establishing "special needs trusts." Through the use of a special needs trust, the disabled spouse or child may receive special protection for public benefits and/or means-tested benefits, including financial assistance programs provided by large pharmaceutical companies.

The divorce process is tremendously stressful for most people. Not only does it create financial uncertainty, but it also diverts the divorcing spouse's attention from other life-preserving matters, such as estate planning. Even in this most difficult time, seek assistance to create peace of mind for both your own well-being and that of your children. **FA**



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