

# *The* **Estate Analyst**<sup>®</sup>

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## **Death and Divorce**

### *Seven Strategic Planning Areas*

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The modern estates on which estate planning professionals are currently working are far more likely to experience divorce liabilities than estate tax liabilities. This calls for a reprioritization of planning that is already taking place under the general umbrella of “asset protection.”

However, divorce is a specialized problem that bears close attention. How prevalent is divorce? What

unique issues does it raise? Let’s review these issues and then identify seven strategic planning areas involving divorce.

### ***Luv U 4 Ever!***

Love may be eternal, but everything else about the marital relationship itself is of more finite duration.

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A University of Texas study found the average length of a premarital relationship to be 28.5 months. The average length of engagements is said to be 16 months. During that time, 7 to 12 months are spent planning the wedding. The average honeymoon lasts 7 days. The average marriage lasts 43 years.<sup>1</sup>

The longest marriage on record is 80 years. This particular record was recently set in 2005, just before 105-year-old Percy Arrowsmith passed away in Hereford, England, a bit north of London. His wife, Florence, age 100, was at his side.<sup>2</sup> And if you believe the Scriptures, Abraham was married to Sarah even longer.<sup>3</sup>

But marriage lasts only “until death do you part.” For legal purposes, a divorce is forever. The permanent severing of a marital relationship establishes a new divorced status which has legal, tax, and contractual ramifications which are permanent.

### ***Trends in Divorce***

One upon a time, one hundred years ago, divorce was a rarity for a variety of social, religious, and economic reasons, not the least of which was the prohibitive cost involved.

A gradual increase in divorce rates took place during the first half of the 20th century, but the most significant increase in divorce rates came during the 1960s and 1970s. It has been argued that liberal attitudes, relaxed social mores, and the economic liberation of women were contributing factors.

The divorce rate may have peaked and established a plateau of sorts at 50%. Once established, this oft-stated number has become accepted as dogma: Half of all marriages fail.

But there is more to it than that. Not all marriages are the same. For example, a first marriage of younger people has a relatively high failure rate during the first two years of marriage. The odds that a particular marriage will end in divorce cannot be predicted with absolute certainty, of course, but a couple married for 40 years who arrive at a lawyer’s office to draft a new will have a much smaller chance of being divorced than a younger couple. The likelihood of divorce varies based on multiple factors such as age, sex, race, and income.<sup>4</sup>

Some data indicate that the divorce rate has dropped off in recent years. Other research shows why divorce is not going out of style anytime soon. In about 25% of all marriages, both partners are happy, and in

another 25%, both spouses are unhappy. In the remaining 50%, one partner is happy and the other is not. The National Center for Health Statistics recently indicated that 30% of first marriages end within 10 years and 43% of first marriages end within 15 years; 37% of second marriages end within 10 years. Others argue that marriage rates have fallen as well.<sup>5</sup>

For estate planning purposes, the concept that many marriages fail is sufficient to put professionals on notice that divorce is generally prevalent regardless of whether the actual rate is 40%, 50%, or 60%. There are a great many divorced people out there. The number of divorced people in the U.S. population increased from 4.3 million in 1970 to 18.4 million in 1996.

### ***A Planner’s Perspective***

What conclusions may be drawn from these trends?

A) Divorce rates may have risen or fallen, but either way they remain high. Divorce is a prevalent condition that has to be anticipated as a significant change of circumstances or liability.

B) Even if a testator is not directly involved in a divorce, the odds are extremely high that some member of the testator’s family will be involved in a divorce.

C) If more people are living together without getting married, the potential for the subsequent breakup of those relationships without standard divorce rules must be considered.

D) Same-sex civil unions or same-sex marriages in jurisdictions that allow it can also end in a split-up or a divorce.

E) Notwithstanding all the other statistics, some marriages will go the distance. One in five first marriages will last 50 years. Note: This is actually a modern phenomenon attributable to increased longevity.

Several other variables now must be added to these discussions. What assets are involved? Are the assets jointly held? Are they appreciated capital assets? Are they retirement assets? Is there a will? How will state and federal laws affect an existing will, brokerage account, or retirement account?

Several strategic planning areas now take shape. What should a prenuptial agreement try to accomplish? What mechanisms may be useful in a postnuptial agreement? Which arrangements should same-sex or unmarried couples utilize? Let’s review seven strategic planning areas.

## SEVEN STRATEGIC AREAS

**1. Prenuptial Agreements:** Earlier planning is almost always preferable. With enough time, you can anticipate and avoid problems. And because of the time value of money, time itself can be an advantage that can be exploited.

But the advance planning of a prenuptial agreement between spouses is critically important for additional reasons. A prenuptial agreement is more effective if made before marital rights are created. (Note: Full disclosure of assets and unbiased representation should be documented.) In addition a premarital “discussion” is a less stressful and more cooperative time to resolve issues as compared to when a marriage is on the rocks.<sup>6</sup>

**2. Postnuptial Arrangements:** Even after a marriage has taken place and appears sound, anticipation of divorce may still be relevant in various circumstances.

Parents of one spouse make a significant loan to a recently married and still childless couple. An agreement establishes how the repayment is to be made in the event of death. Or one spouse has shares in a family business and wants to reduce to writing a previously expressed “understanding” of how that business would pass after his or her death.

Quite practically, if you were on a plane with a 43% chance of breaking up, you’d want to make every possible arrangement while you can.

**3. Divorce and Will Revocation:** Most states have adopted rules comparable to the Uniform Probate Code which provides that if, after executing a will, a person is divorced (or the marriage is annulled), any provisions in favor of the former spouse are revoked unless the will expressly provides otherwise. Any provisions thus revoked will be revived upon the testator’s remarriage to the former spouse.

There are state variations on this, however. In fact, certain states treat the entire will as being revoked by operation of law upon a divorce. There are also a few states that take the position that the will is not altered by divorce in any way.<sup>7</sup>

**4. Who’s The Boss:** Planning well means knowing where you are and who is making the rules. We live in a big world with multiple entities vying to impose their own jurisdiction. Make too many assumptions and you will be blindsided.

At one time, in a world when the husband worked and the wife stayed home, the widespread approach to wife’s estate was to treat a divorcée’s dower right as

being vested in a life estate in one-third of the husband’s lands. These laws have since given way to modern statutory schemes of great variety.

A couple considering a relocation to another state based on state income taxes or decoupled state death taxes may subsequently break up and then find different laws governing their divorce.

Different state rules also apply to different types of assets. For example, some of the larger and more progressive states such as California and New York have treated unexercised stock options as though part of the marital estate and not separate property. Treating the wife (or homemaking spouse) as having a share of the overall estate is a departure from when the wife’s alimony was simply based on what was needed to live comfortably.<sup>8</sup>

There are pre-nupts, post-nupts, real estate deeds with different types of joint ownership or tenancies in common, contracts, insurance policies with named beneficiaries, and retirement accounts. Every asset must be evaluated based on what state laws would apply. Special care must be taken when marital partners reside in a community property state.

Note also that the Congress intervened in the protection of spousal rights to qualified retirement plan assets when it enacted the Retirement Equity Act of 1984. The Retirement Equity Act of 1984 redefined the rights of spouses in qualified retirement plans, making it difficult to waive rights to a spouse’s retirement benefits in a divorce setting. Federal law preempts state law in this area.<sup>9</sup>

**5. Alternative Dimensions:** At one time there was one type of Coca-Cola. Today, the variations require a city block for a full display. The same is true of marriage. In addition to the traditional marriage, there is cohabitation, civil unions (including same-sex civil unions), and same-sex marriages from certain jurisdictions.

This raises strategic considerations in many contexts. For example, protecting the interests of someone in an unconventional union may require an irrevocable transfer.<sup>10</sup>

A divorce per se may not be in mind when planning a gift to someone who is not in a conventional marriage, yet partners in a civil union, cohabitation, or same-sex marriage recognized in Canada or elsewhere, assets could end up being held in joint ownership, divided by law or subject to legal settlement.

Uncertainty as to applicable laws supports the use of long-term dynastic trusts that can protect assets for

family members regardless of what relationship they form and then dissolve.

**6. Alimony, et al.:** Spouses may no longer want to remain married and may even hate each other, yet if there is a common interest of providing for a child or increasing available funds by limiting adverse tax consequences, continued cooperation is vital.

Income taxation of alimony as compared with treatment of trust distributions or payments made toward educational expenses needs to be considered based on the applicable tax rules and circumstances of a given time and fact pattern.

**7. The Remarriage Scenario:** The divorce is over and the assets are divided. It is the end of the story...and also the beginning.

Individuals from one marriage (85% of divorced men and 75% of divorced women) go on to another marriage. That leads to three major planning areas—complying with legally binding divorce settlements, shepherding assets to children of a prior marriage and other heirs, and protecting against the even larger potential that a second marriage will also end in divorce.

Several options may be useful: inter vivos gifts, irrevocable gifts in trust, joint accounts with rights of survivorship, and life insurance policies with named beneficiaries.

One recurring issue in remarriages is balancing marital income rights with rights to remainder beneficiaries who are children from decedent's former marriage. It has been suggested that marital unitrust can be an ideal tool. Such a total return unitrust qualifies for the marital deduction where unitrust payment is equivalent to some percentage of the total value of the trust on a given date, at least annually.<sup>11</sup>

## Final Thoughts

Does marriage still matter?

The argument can be made that, at least for legal and tax purposes, the lines creating separate rights for married and unmarried people have been blurred.

- The tax code's "marriage penalty" has been somewhat addressed in recent years.
- The unlimited marital deduction, which has been a long-standing benefit for those with marital status, is on the verge of becoming moot with the repeal of the estate tax.

- Civil union arrangements convey many of the same benefits on couples who are not married.

But all of that begs the question about human beings. We are a social animal that forms unions and households with others of our kind, yet remain restless and change over time, forming new relationships. Good estate planning has to anticipate all of this.

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## TECHNICAL REFERENCES

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1. The National Association of Wedding Ministers website has additional statistics. For example, about 2.4 American weddings take place each year, creating a \$50 billion industry.
2. In June, 2005, just before Mr. Arrowsmith's death, the couple was also recognized by the Guinness Book of World Records for having the greatest aggregate age of any couple, i.e., 205. However, shortly after Mr. Arrowsmith's death, Herbert and Magda Brown of Philadelphia equaled that record while Yoichi and Kazono Gomi of Yokohama, Japan, ages 103 and 104, respectively, are claiming an aggregate age of 207. They've been married 72 years.
3. *Genesis*, first book of the Old Testament, indicates that Abraham and Sarah were married for over 100 years and had an aggregate age of 264 when Sarah died at age 127. That marriage produced a son when Sarah was 90 and Abraham was 100. The son's name, Isaac, is derived from the word for "laughter," which is about all one can do under those circumstances.
4. A number of divorce statistics and resources can be found at: <http://www.divorcereform.org/rates.html#anchor1223885>.
5. Ahlburg and DeVita, *New Realities*, cited in of Gallagher, *The Abolition of Marriage*, state that the marriage rate has fallen nearly 30% since 1970 while the divorce rate has increased about 40%.
6. Wolven, *An estate planner's guide to advising couples about divorce*, 31 *Estate Planning* 9, p. 427 (Sept., 2004).
7. Mississippi is among the states that enforce an existing will despite a subsequent divorce. See, Volkmer, *Effect of divorce upon estate plan*, 30 *Estate Planning* 3, p. 141 (March, 2003), discussing property settlement cases, revocation by divorce statutes, and the Mississippi case of *Hinders v. Hinders*. Note that even in states upholding an existing will, an implied revocation could be argued but such a case would be fact dependent.
8. Moshman, *The Wife's Estate*, *The Estate Analyst* (May, 1998).
9. Choate, *Love, marriage and the retirement plan*, 142 *Trusts & Estates* 11, p. 58 (Nov., 2003).
10. Levitan and Berkowitz, *Unmarried but protected*, 142 *Trusts & Estates* 9, p. 28 (Sept., 2003). Cohen, *Estate planning for the unique needs of unmarried partners*, 30 *Estate Planning* 4, p. 188 (April, 2003).
11. Baskies and Samuels, *The marital unitrust: A new planning strategy for the remarried spouse*, 27 *Estate Planning* 10, p. 480 (Dec., 2000).