

SEPTEMBER 2006



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To Love, Honor and Manage Assets

FINDING LOVE AGAIN IS OFTEN EASIER THAN COMBINING ASSETS,
BUT SIMPLE PLANNING CAN HELP AVOID MOST PROBLEMS.

Marriage requires compromises in almost every aspect of a new couple's life. While many couples take the time to discuss numerous adjustments needed for their new union, they often fail to address one of the most necessary issues: money management. If it's a second or third marriage, this can be an especially important issue in the relationship since there can be additional complexities to iron out. Yet tying the knot again doesn't have to turn into an estate planning nightmare. Engaging in honest discussions and careful planning can ease the transition and fulfill both partners' wishes.

Before getting into the nitty-gritty of how to structure their financial relationship, couples need to have a conversation about money and what their expectations and desires are. "When people leave a first marriage or relationship, they typically know what they don't want. They never take the time to clarify what they do want," explains Jo Anne Musolf, an executive coach and couples coach in Phoenix, Ariz. That means each person should specifically define their financial plans. For instance, both partners may agree they want to give to charity, but for one that may mean donating a few dollars every Sunday while for the other it could mean large annual contributions. "When the money is planned, people are often talking apples and oranges," Musolf warns.

PENALTIES AND BENEFITS

Beyond understanding each other's financial philosophy, couples have a number of other

considerations, one of which is figuring out the tax implications that come with the new marriage. For one, there is the still-present "marriage penalty," which often strikes the more affluent couples by subjecting them to the alternative minimum tax (AMT), even if neither person may have been hit by the AMT individually, explains Mark Birge, a principal at AKT, an accounting firm in Portland, Ore. Couples should also know that they become jointly liable for any tax liabilities one partner may have outstanding—a minor, but sometimes significant, issue of which to be aware.

Yet for all the negative tax implications that might arise, marriages are generally more tax-friendly in the long run, adds Birge. For instance, gifting assets tax-free is unlimited between spouses, whereas with an unmarried partner, a person is limited to the federal gift exclusions—\$12,000 per person annually and \$2 million for estates in 2006, according to the Internal Revenue Service.

Another tax law might come in handy for couples with two residences between them. Generally, an individual can exclude up to \$250,000 of gains from the sale of a home if he or she used it as a principal residence for two out of the five years before the sale. For a couple, the exclusion is \$500,000 if they both meet the criteria of the use test. That may be a reason to reconsider disposing of property before remarrying, Birge suggests.

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YOURS, MINE AND OURS

An even greater financial concern can be how to divvy up assets each partner accumulated prior to the new marriage. Careful planning is necessary here in order to protect against financial heartache if divorce comes along, and also to ensure that your children from prior marriages are provided for. Usually, the most effective way for dealing with such concerns is a prenuptial agreement. “Many people who have substantial assets would benefit from a prenup,” says Linda J. Ravdin, an attorney and principal with Pasternak & Fidis, P.C., in Bethesda, Md. “It’s an insurance policy against a ridiculously expensive divorce proceeding.”

A prenup isn’t necessarily a must-have. Many couples can simply agree what assets belong only to one person and what will be communal. However, some states view all assets as communal in divorce or estate proceedings regardless of how the assets were

treated by the couple, notes Ravdin. A prenup can largely eliminate your being subject to differing judicial views. Still, even with a prenup, if assets classified as individual were commingled with community assets—like using one spouse’s account to pay a joint bill—it lays the groundwork for legal challenges later on.”

Couples about to marry also need to examine their retirement plans. Even if assets are kept separate, couples should assess their individual portfolios and rebalance, keeping the other’s portfolio in mind. This will prevent both portfolios from being overweighted in any one asset class or sector. If an ex-spouse still has a claim on a partner’s retirement funds, consider closing that account with a court-issued Qualified Domestic Relations Order, which allows tax-free distribution of retirement funds among a divorced couple.

ESTATE PLANNING

For all the income tax and asset management challenges that come with a second marriage, “the more practical obstacles tend to be in the estate planning and gifting area,” says AKT’s Birge. “That is where you are talking about, ‘Ultimately, what do I want to do with my wealth?’”

The main quandary tends to revolve around providing for the new spouse while ensuring that one’s own children aren’t locked out of any inheritance should your new spouse outlive you. One common solution is a Qualified Terminal Interest Property (QTIP) trust. This type of trust provides for

maintaining the standard of living of the surviving spouse, while also guaranteeing assets will get passed on to heirs. Typically, the QTIP provides the trust’s income to the spouse, with the principal going to the children of the person who set up the trust. (Usually in specifically defined situations, the surviving spouse can also tap the principal.) Often, two well-off spouses will set up mirror QTIPs so neither individual’s children will be locked out of any inheritance, Birge explains. In situations where someone will be disinherited, the easiest solution may be to instead give a token inheritance with a no-contest clause, stating that whoever challenges the will gets cut out completely.

Generally, everyone should take the time to review all accounts and estate planning documents for stated beneficiaries, since listed beneficiaries trump whatever is said in a will. That means if an ex-spouse is still listed as beneficiary on an old IRA account, he or she would have legal claim to the funds.

Every couple should take the time to have a frank discussion about their finances, whether it’s a second marriage or even the first. “People often don’t talk about money and what it means to them, and whether they want to save it or spend it,” says Ravdin. “Stuff like that makes people crazy.” But it’s even crazier not to discuss it at all. Solving the money puzzle could be one of the secrets to a happier marriage. ■

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