Tax, Estate and Practical Issues in Divorce and Remarriage

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John J. Scroggin, J.D., LL.M.

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Additional Resources for Advisors

- *List of Helpful Resources*
- *Practical Remarriage Checklist*
- *Practical Post-Divorce Checklist*
- *Personal Property Disposition form for Married Clients*
- *Personal Property Disposition form for Single Clients*

Addendums from Federal Sources:

- *5 Things Every Woman Should Know About Social Security.*
- HANDBOOK, SOCIAL SECURITY ADMINISTRATION § 406.
- *Spouses of Medicaid Long Term Care Recipients.*
- *Spousal Medicaid Improvisation Limits for 2015.*

JOHN J. ("Jeff") SCROGGIN, AEP, J.D., LL.M.
The Brannon House
647 Mimosa Boulevard
Roswell, Georgia 30075
Phone: (770)640-1101
Fax: (770) 518-4124.
Email: John@scrogginlaw.com
Website: www.scrogginlaw.com

Mr. Scroggin has been married for 36 years to Lynn Geiger Scroggin and has three children. His oldest son is a professional blacksmith, his daughter works as a charitable event planner & fundraiser and his youngest son is an Iraq war veteran.

Jeff has practiced as a business, tax and estate planning attorney in Atlanta for 36 years. His practice is devoted to tax planning, estate planning, business representations, business succession and sales of businesses and properties. He is co-creator of the "Family Incentive Trust" and creator of the "The Family Love Letter." Jeff practices out of an 1883 house in the historic district of Roswell, Georgia. The building contains one of the largest collections of tax memorabilia in the US. The collection was featured in a front page article in the Wall Street Journal on April 15, 2015. Jeff is known for his ability to convert complex, technical information into practical, useable forms. He also hopes he is not as pompous as this bio would seem to indicate.

Jeff serves as a Member of the University of Florida Levin College of Law Board of Trustees. Jeff received the following degrees from the University of Florida: B.S.B.A. (Accounting), 1974; Juris Doctorate, 1977; Master of Laws in Taxation (LL.M.), 1979. Jeff has taught tax law at the University of Florida College of Law and College of Business. Jeff is a Founding Board member of the University of Florida College of Law Tax Institute and a Founding member of the University of Florida Advisor Network. He was a CPA with Arthur Andersen's nationwide estate planning group. He is a Nationally Accredited Estate Planner, is rated "AV" by Martindale Hubbell (since 1990) and has been named in Atlanta magazine as a Georgia "Super-Lawyer" (2009, 2010, 2011, 2012, 2013, 2014 and 2015) and "Five Star Wealth Advisor" (2009, 2010, 2011, 2013, 2014 and 2015). He holds a perfect 10 rating from AVVO. Jeff was Founding Editor-in-Chief of the *NAEPC Journal of Estate and Tax Planning* from 2006-2011 and was Co-Editor of Commerce Clearing House's *Journal of Practical Estate Planning* from 2004-2006.

Jeff's professional affiliations include: The State Bar of Georgia, the Florida Bar, American Revenues Society, American Tax Token Society, Atlanta Estate Planning Council, Buckhead Study Group, Georgia Planned Giving Council, and the North Georgia Estate Planning Council (President, 2002-2005). He was Chairman of the North Fulton Community Foundation from 2007-2009 and is a member of the Board of Directors of the National Association of Estate Planners and Councils (2002-2010) where he was Co-Chairman of the Long Range Planning Committee and served as Chairman of the Publications Committee. He is a member of the Board of Directors of the Historic Roswell Convention and Visitors Bureau (2004-present), and is a member of the Roswell Rotary Club. He served as Founding Chairman of the Friends of Barrington Hall (2008-2012).

Jeff is the author of over 250 published articles and columns. Among the publications are: *Estate Planning, Taxes, Financial and Estate Planning, Practical Tax Strategies, Leimberg Information Services, NAEPC Journal of Estate and Tax Planning, ABA Property and Probate, ABA Practical Tax Lawyer, ABA Practical Lawyer, AICPA Tax Advisor, Journal of Estates and Trusts, Trusts and Estates, Zaristky's Estate Planning Alert, Journal of Financial Services Professionals, Journal of Financial Planning, Financial Services Professionals Newsletter, CCH Journal of Practical Estate Planning, Advisor Today, RIA Tax Watch, Financial Planning, Georgia Society of CPAs Bottom Line, Broker World, Life Association News, The Atlanta Journal/Constitution, Atlanta Business Chronicle, National Underwriter, Insights and Strategies, Bank Investment Marketing, NAILBA Magazine, Financial Services Advisor, Business Valuation, Utah Society of CPAs Journal, the Atlanta Bar Journal* and the *Georgia Bar Journal*. He was a Columnist for Advisor Today Magazine (1997-2010) and a Contributing Writer to National Underwriter. He has written three books and was recognized by the CFP Board of Examiners for writing one of the best planning articles for the year 2000. His website has been recommended by the Journal of Accountancy for estate planning purposes.

Jeff is a frequent speaker on business, tax and estate planning issues. Among the groups he has spoken for are: The University of Florida College of Law Graduate Tax Program (2004, 2008, 2009, 2010, 2012, 2013, 2015), the Georgia State University MBA Program, the Million Dollar Roundtable, the State Bar of Georgia (1992, 1996, 1997, 1998, 1999, 2000, 2001, 2002, 2003, 2005, 2006, 2009, 2013), The National Convention of the Financial Planning Association (1997, 1998, 2003, 2004, 2005, 2006, 2007, 2008, 2011, 2014), the Financial Planning Association Annual Retreat(2000, 2002, 2014, 2015) (the Atlanta Bar Association (2005, 2013), Georgia Society of CPAs Annual Estate Planning Conference (2007, 2010, 2011, 2012), the Georgia Federal Tax Conference (2012, 2013, 2014), The Texas Society of CPAs, Georgia Planned Giving Council, the Columbus Ohio Community Foundation, the Dallas Foundation, the Naples Community Foundation, the Philadelphia Estate Planning Council (2007, 2010), the Estate Planning Council of Mississippi, the Central Texas Estate Planning Council, the Wilmington Estate Planning Council, the Spokane Estate Planning Council, the Stuart Estate Planning Council, the Northern Arkansas Estate Planning Council, the St. Louis Estate Planning Council, the Louisville Estate Planning Council, the Atlanta Estate Planning Council, the Estate Planning Council of North Georgia, Chattanooga Estate Planning Council, the Northern Michigan Estate Planning Council, Estate Planning Council of Winston Salem, the Detroit Estate Planning Council, Red River Estate Planning Council, North Alabama Estate Planning Council, the Wisconsin FPA & CPA Annual Symposium, Schwab Trust, Canada Life, Partners Financial, the Colorado Springs FPA, the San Diego FPA, the Wisconsin FPA, the College for Financial Planning, The Society of Financial Services Professionals National Convention, The National Business Institute, NAPFA National Convention, The National Convention of the U.S./Philippine Chamber of Commerce, The Annual Convention of the Southern Council of Optometrists, The International Forum (2009, 2010), the Society of Senior Risk Managers, Ascensus, Financial Service Corporation, NAIFA Annual Meeting, Producers Web, First Global, Subcenters, North Carolina Society of CPAs, North Carolina SFSP Annual Meeting, AXA Advisors, The Milner Group, ChFC Georgia Chapter, IAFP Georgia Chapter, NAIFA Georgia Chapter, Mid-South Society of the Institute of Certified Financial Planners, First Colony Life Insurance, CUNA Mutual Group, Metlife, Prudential Insurance Company, Family Wealth Counselors National Convention, Willis Corroon, Guardian Life Insurance Company, American General Life Insurance, Financial Network Investment Corp, Gulf States FPA, Tri-State FPA Annual Meeting, the Houston FPA, NAILBA Annual Meeting, Atlanta Life Underwriters EXPO, A.G. Edwards, Enterprise Group of Funds, and the Annual Convention of National Beer Wholesalers Association (2003, 2005, 2006, 2007, 2008 & 2009).

Jeff has been quoted in a number of media sources, including: the Wall Street Journal (1999, 2004, 2005, 2006, 2007, 2009, March 2010, August 2010, April 2015), CNN Headline News (on the Terri Schavio case), The New York Times (2005, 2013, 2014), USA Today (2014), Atlanta Journal/Constitution(1999, 2002, 2005, 2010), National Public Radio Marketplace Radio, National Public Radio Talk of the Town, Forbes Magazine (1999, 2001, 2012, 2014), Fortune Magazine (1998, 2000, 2001), Money Harvest, Dow Jones Investment Advisor, Worth Magazine, Registered Representative Magazine, Leads Magazine, Image Magazine, Financial Advisor, The Practical Accountant, National Underwriter, Bloomberg Wealth Management, Life Association News, Financial Planning, The Asian Wall Street Journal, New York Times International Herald Tribune, Planner Pavilion.com, Journal of Financial Services Professionals, Houston Chronicle, Fort Worth Star Telegram, Redbook, Kiplinger's, Money Magazine, Medical Economics, Smart Money Magazine, Wall Street Magazine, Minneapolis St Paul Business Journal, Investment News, South China Post, the Dallas Morning News, Secured Retirement, The LA Times, Advisor Today, Bank of America magazine, Fortune Investor, BNA Estates Gifts & Trusts Journal, Atlanta Business Chronicle, Newsday, Chicago Sun-Times, Bankrate.com, ABA Probate & Property, Clarion Ledger, Miami Herald, MSN (2010, 2013, 2015), New England Financial Journal, Baltimore Business Journal, and Knight-Ridder Tribune.

Tax, Estate and Practical Issues in Divorce and Remarriage

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"Marriage is often due to lack of Judgment, Divorce to lack of Patience and Remarriage to lack of Memory"

EXECUTIVE SUMMARY

The tax, estate planning and practical components of divorce or remarriage are normally not a major focus of clients or their advisors.

The unfortunate reality is that most divorces are largely unplanned, disorderly events. Emotion, not reasoned self-interest often governs the decision process. This is an area of tremendous self-inflicted damage by clients and their unwary advisors.

Moreover, in the excitement of an impending marriage, most clients fail to adequately investigate or plan for the tax and legal consequences of the marriages. Talking about the consequences of a divorce as your first marriage draws near tends to take some of the romance out of the event. By the time of a second or third marriage, the bride and groom are typically a bit more focused on the consequences of both the marriage and its demise.

All of the issues are further complicated by the proclivity of clients to move across state borders where different rules will apply.

There have been numerous articles which have discussed the rules governing alimony, property settlements and child support. This article will mainly focus on planning areas which have received less scrutiny and take a practical approach to the issues. To aid your own research, we have provided additional research sources. The rules governing divorce and marriage vary widely from state to state and can be extremely complex. This article will focus on general rules and will not focus on the myriad exceptions, limitations and exclusions to the general rules. Moreover, all issues of divorce and re-marriage are not covered. There are not enough pages to do so.

COMMENT:

The Statistics. There are lots of interesting statistics with regard to divorce and

marriage:[1]

What is the true divorce rate in America? There is a fair degree of controversy on that topic. The most often repeated statistic is that roughly 49% of all first marriages end in divorce. But, there is disagreement, with one author saying the first time marriage divorce rate is in the mid-20s.[2] What is clear is that divorce rates in most demographic groups have been diminishing since the 1970s.

- The divorce rate for Baby Boomers has been skyrocketing, even while it has been diminishing for other demographic groups over the last two decades.[3]
- The highest percent of divorces occur in the third year of marriage.[4] On average, divorces in second marriages generally occur by the sixth year, while most divorces in first marriages occur by the eighth year.[5]
- Wives initiate over 66% of all divorces.[6]
- "*It has been well documented that women and men who cohabit with their future spouse before first marriage are more likely to divorce than those who do not cohabit with their spouse before first marriage*."[7]
- 8% of newly married adults have been married three times or more.[8]
- 15% of divorced woman versus 29% of divorced men would like to remarry,[9]
- Women who first had sex in their teens have roughly double the risk of divorce later in life compared to women who had their first unmarried sexual experience in their adult years.[10]
- New Jersey and New York have the lowest percentage of divorced residents.[11]
- Over 75% of people who marry partners from an affair get divorced.[12]

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1 *See, e.g.*, *63 Interesting Facts About Marriage*, RANDOM FACTS, http://facts.randomhistory.com/interesting-facts-about-marriage.html (last visited June 1, 2015).

2 Shaunti Feldhahn, THE GOOD NEWS ABOUT MARRIAGE: DEBUNKING DISCOURAGING MYTHS ABOUT MARRIAGE AND DIVORCE (2014).

3 Susan L. Brown & I-Fen Lin, *The Gray Divorce Revolution: Rising Divorce among Middle-aged and Older Adults, 1990-2010*, 3 (Nat'l Ctr. for Fam. & Marriage Res., Working Paper Series WP-13-03, 2013); Susan Gregory Thomas, *Divorce Late in Life: The Gray Divorcés*, WALL ST. J., (Mar. 3, 2012).

4 TIME, Sept. 25, 2000.

5 *Id.*

6 Margaret Brinig & Douglas W. Allen, '*These Boots Are Made for Walking': Why Most Divorce Filers Are Women*, 2 AM. L & ECON. REV. 126 (2000).

7 CASEY E. COPEN, ET AL., CTR. FOR DISEASE CONTROL, FIRST MARRIAGES IN THE UNITED STATES: DATA FROM THE 2006–2010 NATIONAL SURVEY OF FAMILY GROWTH, NATIONAL HEALTH STATISTICS REPORT NO. 49, 2 (Mar. 22, 2012).

8 Gretchen Livingston, *Four-in-Ten Couples Are Saying "I Do," Again*, PEW RES. CTR. (Nov. 14, 2014), http://www.pewsocialtrends.org/2014/11/14/four-in-ten-couples-are-saying-i-do-again/.

9 *Id.*

10 Anthony Paik, *Adolescent Sexuality and Risk of Marital Dissolution*, 73 J. MARRIAGE & FAM 472 (2011).

11 *Most Divorced Residents: States*, BLOOMBERG, http://www.bloomberg.com/visual-data/best-and-worst//most-divorced-residents-states (last visited June 1, 2015).

12 HOLLY HEIN, SEXUAL DETOURS: INFIDELITY AND INTIMACY AT THE CROSSROADS (2000).

- Roughly 20% of adults over age 25 have never been married, up from 9% in 1960.[13]
- Washington DC has the lowest marriage rate in the United States.[14]
- Rupert Murdoch's divorce from Anna Murdoch is reportedly the most expensive divorce, costing him $1.7 billion.[15]
- If only one spouse smokes, the likelihood of divorce increases by 75% to 91%.[16]
- The Air Force has the highest rate of divorce of all military services.[17]
- Children of divorced parents are more likely to divorce.[18]

The Quotes: There are more than a few funny quotes on marriage:

- *A husband is someone who, after taking the trash out, acts liked he cleaned the whole house.*
- *Marriage lets you annoy one special person for the rest of your life.*
- *Behind every great man is a surprised wife.*
- *I promise to take care of you when you are old, but if you hit me with your cane, I will wash your dentures in the toilet water.*
- *The longest sentence you can form with two words is I DO.*
- *Old people at weddings are always poking me and saying "You're next." So I started doing the same thing to them at funerals.*
- *If you think women are the weaker sex, try pulling the covers back to your side of the bed.*
- *Marriage is a bond between a person who never remembers an anniversary and one who never forgets one.*
- *Ever since it started snowing my husband is standing in front of the window and watching. If the snow gets much worse, I might let him inside the house.*

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13 Wendy Wang & Kim Parker, *Record Share of Americans Have Never Married*, PEW RES. CTR. (Sept. 24, 2014), http://www.pewsocialtrends.org/2014/09/24/record-share-of-americans-have-never-married.

14 Connolly, Katie. *Why So Few D.C. Residents Are Married*, Newsweek.com. October 20, 2009. Accessed June 4, 2015.

15 *The World's Most Expensive Divorce Settlements,* Yahoo Finance. July 9, 2012. Accessed: June 8, 2015.

16 Rufus, Anneli. *15 Ways to Predict Divorce,* The Daily Beast. May 19, 2010. Accessed: June 8, 2015.

17 Burton, Natasha. *Military Divorce: What It's Like to Split from Your Military Spouse*, Huff Post. May 28, 2012. Accessed: June 8, 2015.

18 NICHOLAS H. WOLFINGER, UNDERSTANDING THE DIVORCE CYCLE: THE CHILDREN OF DIVORCE IN THEIR OWN MARRIAGES (2005).

Marital Rights

The first recorded divorce in North America occurred in the Massachusetts Bay colony in 1639. The cause was the husband's bigamy.[19]

Every marriage (even second and third marriages) provides the new spouse a substantial number of new legal rights in the other spouse's assets and decision making, including (but certainly not limited to):

Spousal Share. "Spousal share" or "spousal elective share"[20] refers to a legal claim that a surviving spouse has against a portion of the assets of their deceased spouse, even if the deceased spouse disinherited the survivor.[21] The concept of spousal elective share evolved out of the common law concepts of dower and curtesy.[22] Every state except Georgia has a spousal share election available to a surviving spouse or a community property right in a spouse.[23] Some states provide that the elective share may be made only against the probate estate of a deceased spouse. In other states, the assets subject to the claim can be "augmented" to include some or all of the non-probate assets of the decedent. Generally, the elective share is in lieu of any inheritance under the deceased spouse's Will.

However, there is little commonality between the state laws, and the local nuances can create an easy trap for the uninitiated advisor and client.[24] For example, in North Carolina, the spousal elective share increases the longer the marriage lasts. For marriages that last less than 5 years, the spouse's claim is 15% of the estate, while spouses of marriages that last longer than 15 years have a 50% claim against the decedent's estate.[25]

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19 *Divorce Actions*, ANCESTRY.COM, http://www.ancestry.com/wiki/index.php?title=Divorce_Actions (last visited June 1, 2015).

20 The right is also referred to as "widow's share," "statutory share," "election against the will," and "forced share."

21 For a list of state spousal election rights, see JEFFREY A. SCHOENBLUM, MULTISTATE GUIDE TO ESTATE PLANNING, tbl.6.02 (CCH 2015) and LAWCHEK, *Can a spouse elect against a will in this state?* available at http://www.lawchek.com/Library1/_books/probate/qanda/spouse.htm (last viewed June 1, 2015).

22 A few states retain dower (e.g., Arkansas, Michigan, Ohio) and curtesy rights (e.g., Arkansas).

23 Tax Management Portfolio, *Spouse's Elective Share*, No. 841 T.M. Georgia has a concept called "Years Support" which provides for support to a surviving spouse while the estate remains open. See: GA. CODE ANN. § 53-3-1 et seq.

24 *See, e.g.*, Kevin R. Garrison, *The Ins And Outs Of The Alabama Elective Share*, 58 ALA. L. REV. 1161 (2007).

25 N.C. GEN. STAT. § 30-3.1 (2015); H. Chalk Broughton Jr., *Recent Changes To North Carolina's Elective Share Statute – A Trap For The Unwary Estate Planner*, POYNER SPRUILL (Apr. 07, 2014), http://www.poynerspruill.com/publications/Pages/RecentChangesNCElectiveShareStatuteTrapForUnwaryEstatePlanner.aspx.

There are ways of eliminating or at least limiting a spouse's separate share claim, but the approaches vary widely because of significant differences in state law. See the later discussion.

> ***Trap:*** In many states, the spousal elective share can be waived, but review the waiver requirements closely because inattentiveness to the details can make the waiver invalid (e.g., failure to make a "fair disclosure" of all financial resources).
>
> ***Trap:*** If a surviving spouse disclaims an elective share or fails to file an affirmative election, then Medicaid may still count the elective share as an asset for purposes of qualifying for Medicaid.[26]
>
> ***Trap***: Surviving spouses generally have a limited time in which to file the election for a spousal share. The period is normally in the range of 6 to 9 months.
>
> ***Trap and Opportunity:*** Clients continually seem to make mistakes in their retirement plan and IRA beneficiary designations. For example, many clients have named their estate as the beneficiary or failed to name a beneficiary. As a result, the funds from the plan or IRA must be paid out within five years after the participant's death.[27] This quicker payout accelerates the taxation of the funds when compared to the potential life expectancy payout of an individual beneficiary.[28] However, a spouse may be able to make a spousal election (in states with an "augmented" spousal elective share) against the retirement account or IRA and eliminate or minimize this mistake.[29] The IRS has ruled[30] that a spousal elective share made against an IRA can be rolled over to the surviving spouse's IRA on a tax-free basis.
>
> ***Trap or Opportunity***? Does the spousal elective share receive an allocated part the estate's taxable income pursuant to Internal Revenue Code (I.R.C.) section 662? In Deutsch v. Commissioner,[31] the Tax Court ruled that there was not an allocation of income to the spouse because of the spousal election, while in Bingham v. U.S.,[32] a Massachusetts district court came to a different

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26 *See* I.G. v. Dept. of Human Servs., 900 A.2d 840 (N.J. Super. Ct. 2006); *In re* Mattei, 647 N.Y.S.2d 415 (Sup. Ct. 1996).

27 See Treas. Reg. § 1.401-(a)(9)-3 (2015). If the decedent was over 70½, then the decedent's life expectancy is used. See Treas. Reg. § 1.401-(a)(9)-5 (2015).

28 See: John P. Dedon and Pamela M. Buskirk, *IRA Beneficiary Designations Stretch or Shorten Payout Period*, EST. PLAN. J. (February 2011).

29 See: I.R.S. Priv. Ltr. Rul. 95-24-020 (June 16, 1995); I.R.S. Priv. Ltr. Rul. 96-26-049 (June 28, 1996).

30 PLR 200438045.

31 74 T.C.M. 935 (1997).

32 983 F. Supp. 46 (D. Mass. 1997).

conclusion.

> ***Trap***: In some "augmented" states, self-settled trusts, including Charitable Remainder Trusts ("CRT"), can be subject to the spousal elective share. The existence of that right is generally a disqualifying event for the CRT.[33] In order to avoid that disqualification, the IRS requires that a spouse must irrevocably waiver any right to make a claim against the CRT.[34]

Community Property Rights. The following nine states have enacted community property laws: Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, Washington, and Wisconsin.[35] Alaska[36] and Tennessee[37] permit their residents to elect into community property treatment. Fundamentally, the laws provide that "marital assets" acquired during the marriage are jointly owned by both spouses. The community property rules vary significantly from state to state. States with community property rights do not generally provide for a statutory spousal elective share because the surviving spouse is entitled to half of the marital estate.[38]

Homestead Rights. A number of states grant a "homestead allowance" to a surviving spouse. The homestead allowance is generally a priority claim that a surviving spouse has against the homestead of a deceased spouse.

In many states, the allowance can be very small. For example, the Alabama statute[39] reads: "*A surviving spouse of a decedent who was domiciled in this state is entitled to a homestead allowance of $6,000.00. . . . The homestead allowance is exempt from and has priority over all claims against the estate. Homestead allowance is in addition to any share passing to the surviving spouse or minor or dependent child by the will of the decedent unless otherwise provided in the will, by intestate succession or by way of elective share.*"[40]

Florida has unique rules that govern the devise of a married couple's homestead. In Florida, a surviving spouse has a constitutional right to a life estate in the homestead,[41]

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33 I.R.C. §§ 664(d)(1)(B), 664(d)(2)(B). But see: Longue Vue Foundation v. Comr., 90 T.C. 150 (1988), *acq.,* 1989-1 C.B. 1

34 Notice 2006-15, 2006-8 I.R.B. 501 (2/21/06); Rev. Proc. 2005-24, 2005-16 I.R.B. 909 (4/18/05).

35 U.S. DEP'T OF TREASURY, INTERNAL REVENUE SERV., PUBLICATION 555, COMMUNITY PROPERTY 2 (2014).

36 Id.

37 The Tennessee Community Property Trust Act of 2010, TENN. CODE ANN. §35-17-101 to -108 (2015); Dan Holbrook, *Where There's a Will*, TENN. B.J., Dec. 2010, at 26; William Roberts, *A Cautionary Tale Community Property Trusts*, TENN. B.J., July 2011, at 24.

38 Terry L. Turnipseed, *Community Property v. The Elective Share*, 72 La. L. Rev. (2011) Available at: http://digitalcommons.law.lsu.edu/lalrev/vol72/iss1/8

39 ALA. CODE § 43-8-110 (2015).

40 ALA. CODE § 43-8-110 (2015).

41 FLA. CONST. art. X, § 4(c).

or the spouse can elect to take an undivided one-half interest in the homestead as a tenant in common.[42] These rights exist even if the spouse was not on the title and even if the residence was held in trust.[43] As long as there is either a surviving spouse or one or more minor children, the Florida homestead cannot be devised by the owner to another person. The statute reads: "*As provided by the Florida Constitution the homestead shall not be subject to devise if the owner is survived by a spouse or a minor child or minor children, except that the homestead may be devised to the owner's spouse if there is no minor child or minor children.*"[44] Florida homestead rights can be waived.[45]

> ***Trap***: Because of the spousal rights to the residential homestead, creditors may require the non-owner spouse to either be liable for any mortgage debt on the homestead residence or waive or subordinate the spouse's legal rights to the homestead.[46]
>
> ***Caution***: The Florida homestead rules are very complex and should not be handled without a thorough knowledge of their unique provisions.[47]
>
> ***Trap:*** Clients who move their residency to Florida after having signed a marital agreement should have a local attorney review the agreement to determine if it effectively waives the Florida homestead rights.

<u>Spousal Support</u>. A number of states provide for support rights to a surviving spouse.[48] For example, the Georgia "Years Support" claim is a priority claim that a surviving spouse and/or minor child can make against a deceased spouse's testate or intestate estate.[49] The Georgia statute[50] provides: "*The surviving spouse and minor children of a testate or intestate decedent are entitled to year's support in the form of property for their support and maintenance for the period of 12 months from the date of the*

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42 FLA. STAT. § 732.401(2) (2015).

43 FLA. STAT. § 732.401 (2015).

44 FLA. STAT. § 732.4015(1) (2015).

45 FLA. STAT. § 732.702 (2015) ("Each spouse shall make a *fair disclosure* to the other of that spouse's estate if the agreement, contract, or waiver is executed after marriage. *No disclosure* shall be required for an agreement, contract, or waiver executed *before marriage*.") (emphasis added).

46 *See also National State Requirements*, WORLD WIDE LAND TRANSFER (Feb. 26, 2012), http://worldwidelandtransfer.com/marital-signature-requirements (summarizing these state rules).

47 Jeffrey A. Baskies, *Florida Homestead Laws Present Malpractice Traps for the Unwary*, 35 EST. PLAN. J. 23 (May 2008); Jeffrey A. Baskies, *New Florida Homestead Laws Add Flexibility in Estate Planning*, 38 EST. PLAN. J. 13 (Mar. 2011); Jeffrey A. Baskies, *Please Don't Plan with Your Clients' Florida Homesteads*, ASSET PROTECTION PLAN. NEWSLETTER (LISI), no. 209, Sept. 24, 2012; Chuck Rubin, *Restrictions on Transfers of Florida Homestead Property Chart*, ASSET PROTECTION PLAN. NEWSLETTER (LISI), no. 210, Oct. 4, 2012.

48 For a list of spousal rights in addition to the spousal election, see JEFFREY A. SCHOENBLUM, MULTISTATE GUIDE TO ESTATE PLANNING, tbl.6.01 (CCH 2015).

49 GA. CODE ANN. § 53-3-1 to -20 (2015).

50 GA. CODE ANN. § 53-3-1(c) (2015).

decedent's death." A number of states have similar rights that are often called a "family allowance."

> ***Drafting***: Unless contrary language is provided in the Will, the right to claim Years Support or a family allowance may be in addition to any bequests to the surviving spouse. It generally makes sense to provide that any spousal bequests are "in lieu" of any such rights to avoid an unexpected increase in the passage of assets to the spouse.
>
> ***Opportunity***: In many states, the spousal support claim is a priority payment that steps in front of other claims against the estate. For example, the Alabama statute reads: "*The family allowance is exempt from and has priority over all claims, but does not have priority over the homestead allowance.*"[51] As a consequence, these rights may be used to pass assets to a surviving spouse and/or minor child even if the estate is insolvent.

Personal Property Rights. A number of states provide that a surviving spouse has a priority claim to some of the tangible personal property of a deceased spouse. The right may be to particular tangible personal property or may be expressed in a monetary value. For example, the Uniform Probate Code provides:[52] "*In addition to the homestead allowance, the decedent's surviving spouse is entitled from the estate to a value, not exceeding $15,000 in excess of any security interests therein, in household furniture, automobiles, furnishings, appliances, and personal effects.*"

Intestate Claims. If a married client dies without a Will (or similar dispositive documents), then the surviving spouse is entitled to a share of the estate, generally limited to the intestate estate (e.g., jointly held bank accounts generally pass to the co-owner, IRAs pass to the named beneficiary, etc.). If the decedent left no descendants, then the spouse will receive 100% of the intestate estate in most states. The spouse's rights may be reduced if there are other statutory intestate heirs of equal rank, which may include the parents or the descendants of the deceased.[53] In some states, the surviving spouse receives at least a minimum dollar amount or minimum percentage of the intestate estate.

ERISA**.** The Employee Retirement Income Security Act of 1974 (ERISA)[54] governs qualified retirement plans. Upon marriage a spouse normally and automatically becomes the primary beneficiary of the other spouse's ERISA defined contribution

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51 ALA. CODE § 43-8-112 (2015).

52 UNIF. PROB. CODE § 2-403 (UNIF. LAW COMM'N 2014).

53 *See, e.g.*, ALA. CODE § 43-8-41(2015)which provides that "[*i]f there is no surviving issue but the decedent is survived by a parent or parents, the first $100,000.00 in value, plus one-half of the balance of the intestate estate*" passes to the surviving spouse with the parents equally taking the remainder of the estate.

54 Pub. L. No. 93-406, 88 Stat. 829 [hereinafter ERISA].

account.[55] In a defined benefit or money purchase plan, unless both spouses choose otherwise, the form of payment must be a qualified joint and survivor annuity, providing payments over the participant's lifetime and then a surviving spouse's lifetime.[56]

In addition, changes in beneficiary designations of an ERISA retirement plan generally require written approval of a spouse if the participant is married.[57]

IRAs do not have a similar mandatory spousal rights or spousal approval requirements in changing the IRA beneficiary.[58]

Survivor Benefits. A surviving spouse who is named as beneficiary of a retirement plan or IRA can elect to either to roll over the IRA to the spouse's own IRA[59] or to maintain the deceased spouse's IRA. If the spouse elects to maintain the deceased spouse's IRA, they have the option of delaying required minimum distributions until the end of the year in which the deceased spouse would have reached age 70½.[60]

> ***Resource***: Natalie B. Choate, Life and Death Planning for Retirement Benefits (2011).

Social Security Benefits. A spouse has two possible benefits from social security. First, if the couple gets divorced, the divorced spouse may have claims to a portion of their ex-spouse's social security benefits. Second, a surviving spouse may have rights to a portion of their deceased spouse's benefits. See the two page statement from the Social Security Administration summarizing the rights of a spouse to Social Security benefits, which is appended to the end of this article.

> ***Trap***: Social security benefits can be subject to income tax, with high income earners having up to 85% of their social security benefits subject to income taxation.[61] This may be one more reason to delay social security benefits.

> ***Opportunities***: There are various strategies by which married couples can significantly increase their social security benefits. See the resources below.

> ***Resources***:

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55 I.R.C. § 401(a)(11)(B)(iii) (2015). I.R.C. § 401(11)(D) (2012) permits a retirement plan to require that the marriage must meet a one year requirement, but, in the author's experience, most plans have not adopted this exception.

56 I.R.C. § 401(a)(11).

57 29 U.S.C. § 1055(c)(2)(A) (2012).

58 29 U.S.C. §§ 1051–1061 (2012).

59 I.R.C. § 408(d)(3)(C)(ii)(II) (2015).

60 I.R.C. § 401(a)(9)(B)(iv) (2015).

61 IRC§ 86(a)(2) (2015).

- LAURENCE J. KOTLIKOFF, ET AL., GET WHAT'S YOURS: THE SECRETS TO MAXING OUT YOUR SOCIAL SECURITY (2015).
- *How to Maximize Your Social Security Benefits*, AARP, available at www.aarp.org.
- Kenneth A. Hansen and Steven J. Carlson, *Maximizing After-Tax Social Security Lifetime Payouts*, 1 *Taxes* 55-62 (November 2013).

Filial Support Laws. According to the Statute of Frauds, an individual cannot generally be held liable for the debts of another person without agreeing to such liability.[62] However, as many as 30 states have adopted Filial Support statutes, in which family members can be held legally liable for the support obligations of spouses, parents and other family members. These costs include health care and long term care costs, even if the family member has not signed a document guaranteeing those liabilities or received any assets from the needy family member. According to a 2011 MetLife Survey,[63] an average private room in a nursing home cost $87,235 per year. Costs have only gone up since 2011.

In California,[64] Connecticut,[65] Indiana,[66] Massachusetts,[67] North Carolina,[68] Ohio,[69] failure to provide the necessary support to a spouse can be a criminal felony or misdemeanor.

> ***Trap:*** Studies consistently show that Baby Boomers have not been saving for their retirement. Moreover, their parents are living longer than expected, and as a consequence, are outliving their assets. The increased life expectancy of Americans, combined with their lack of adequate financial preparation for their long term care, will cause increased enforcement of Filial Support Laws against family members. This right may prove to be particularly problematic in second and third marriages, even when there is a prenuptial agreement in place.[70]

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62 *See, e.g.*, FLA. STAT. § 725.01 (2015) (Florida's version of this provision of the Statute of Frauds).

63 MARKET SURVEY OF LONG-TERM CARE COSTS, METLIFE (2011), *available at* https://www.metlife.com/assets/cao/mmi/publications/studies/2011/mmi-market-survey-nursing-home-assisted-living-adult-day-services-costs.pdf; *see also* COST OF CARE SURVEY, GENWORTH (2014), *available at* https://www.genworth.com/dam/Americas/US/PDFs/Consumer/corporate/130568_032514_CostofCare_FINAL_nonsecure.pdf.

64 CAL. PENAL CODE § 270(a) (2015) provides that non-support of a spouse is a Misdemeanor.

65 CONN. GEN. STAT. § 53-304 (2015) provides for up to a year of imprisonment.

66 IND. CODE § 35-46-1-6 (2015) provides that non-support of a spouse is a Class D Felony.

67 MASS. GEN. LAWS ch. 273, § 1 (2015) provides that non-support is a felony.

68 N.C. GEN. STAT. § 14-322 (2015) provides that non-support of a spouse is a Class 1 or 2 Misdemeanor.

69 OHIO REV. CODE ANN. § 2919.21 (West 2015) provides that non-support of a spouse is a misdemeanor of the first degree.

70 *See* Susan T. Peterson, *The Price of Admission: Liability and Responsibility for Nursing*

Opportunity: On the other side of the coin, if you represent an impoverished elder or incapacitated client, do you raise the specter of Filial Support Laws to family members?

Opportunity: If the client's state of residency has a strong Filial Support statute, consider obtaining a Long Term Care policy for the spouse to insure against the cost and avoid Medicaid issues on the couple's joint assets (see comments below).

Resources:

- For a summary of state statutes on Filial Responsibility, see:
  - Katherine C. Pearson, *Filial Support Laws in the Modern Era: Domestic and International Comparison of Enforcement Practices for Laws Requiring Adult Children to Support Indigent Parents*, 20 ELDER L.J. 269 (2013).
  - Jane Gross, *The New Old Age*, graphics8.nytimes.com/packages/pdf/health/NOA/30states.pdf (last visited June 1, 2015);
  - Kelly Greene, *29 States That Could Make Adult Children Pay for Mom's Care*, WALL ST. J. (June 25, 2012, 10:28 AM), http://blogs.wsj.com/ totalreturn/2012/06/25/29-states-that-could-make-adult-children-pay-for-moms-care/
- For more detailed information on Filial Responsibility, see:
  - Shannon Frank Edelstone, *Filial Responsibility: Can the Legal Duty to Support our Parents be Legally Enforced?* 36 FAM. L.Q. 501 (2002)*;*
  - Ben Matlin, *Providers Pursue Kids For Parents' LTC Costs*, FIN. ADVISOR (Aug. 4, 2014), http://www.fa-mag.com/news/providers-pursue-kids-for-parents--ltc-costs-18763.html;
  - Northwestern MutualVoice Team, *Who Will Pay for Mom's or Dad's Nursing Home Bill? Filial Support Laws and Long-Term Care*, FORBES (Feb. 3, 2014, 8:45 AM), http://www.forbes.com/sites/northwesternmutual/2014/02/03/who-will-pay-for-moms-or-dads-nursing-home-bill-filial-support-laws-and-long-term-care/.
  - Katherine C. Pearson, *Filial Support Laws in the Modern Era: Domestic and International Comparison of Enforcement Practices for Laws Requiring Adult Children to Support Indigent Parents*, 20 ELDER L.J. 269 (2013).

Home Expenses, MINN. BENCH & B. (2009), http://www2.mnbar.org/benchandbar/2009/mj09/nursing_home.html (discussing spousal responsibility in Minnesota).

Incapacity Decision-Making. Only 33% of adult Americans have executed a medical directive.[71] In 2000, the AARP reported that only 45% of Americans over the age of 50 have executed a durable general power of attorney.[72]

Some states provide that marriage automatically revokes a Medical Directive, except with regard to the spouse. For example, Georgia law provides: "*Unless an advance directive for health care expressly provides otherwise, if after executing an advance directive for health care, the declarant marries, such marriage shall revoke the designation of a person other than the declarant's spouse as the declarant's health care agent….*"[73]

In the absence of Medical Directives and/or Durable General Powers of Attorney, most states provide that the current spouse has the highest priority to serve as Guardian over the assets and/or person of an incapacitated spouse. For example, Georgia provides a statutory order of preference for Guardians: "*Individuals who are eligible have preference in the following order: (1) The individual last nominated by the adult in accordance with the provisions of subsection (c) of this Code section; (2) The spouse of the adult or an individual nominated by the adult's spouse in accordance with the provisions of subsection (d) of this Code section;(3) An adult child of the adult or an individual nominated by an adult child of the adult in accordance with the provisions of subsection (d) of this Code section….*"[74]

> ***Drafting***: If a client is entering into a new marriage and wants to name someone other than the new spouse as incapacity decision maker, then the client should execute a new Medical Directive and Durable General Power of Attorney as soon as possible, even before marriage (with language that the documents were executed in contemplation of the impending marriage). Moreover, incapacity documents should provide for when (e.g., upon the filing of a divorce complaint) and how (e.g., treat the power holder as predeceasing the maker of the instrument) any divorce impacts the appointments of the power holder.

Estate Representation. In the event of an intestate estate or the failure of all named Personal Representatives to serve, the surviving spouse generally has a priority right to be the Executor/Personal Representative of the deceased spouse's estate, even if there are children from a prior relationship. For example, the State of Washington provides: "*Administration of an estate if the decedent died intestate or if the personal*

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71 *See* MYTHS AND FACTS ABOUT HEALTH CARE ADVANCE DIRECTIVES, AM. B. ASS'N, (2013).

72 *Where There is a Will…Legal Documents Among the 50+ Population: Findings from an AARP Survey,* AARP (Apr. 2000), http://www.aarp.org/money/estate-planning/info-2000/aresearch-import-424.html.

73 GA. CODE ANN. § 31-32-6(b) (2015).

74 GA. CODE ANN. § 29-4-3 (2015) (emphasis added)

representative or representatives named in the will declined or were unable to serve shall be granted to some one or more of the persons hereinafter mentioned, and they shall be respectively entitled in the following order:(1) The surviving spouse or state registered domestic partner, or such person as he or she may request to have appointed. (2) The next of kin in the following order: (a) Child or children; (b) father or mother; (c) brothers or sisters; (d) grandchildren; (e) nephews or nieces."[75]

Veterans Benefits. The Veterans Benefits Administration offers a variety of benefits and services to spouses, children, and parents of former military members and veterans who are deceased or totally and permanently disabled by a service-connected disability.

> ***Trap***: For some veterans, their VA medical benefits are based upon their lack of income or assets. Getting married can change that financial calculation.
>
> ***Resource***: For a comprehensive list of veterans' benefits to dependents and surviving spouses, see: U.S. DEP'T OF VETERANS AFFAIRS, OFFICE OF PUB. & INTERGOVERNMENTAL AFFAIRS, FEDERAL BENEFITS FOR VETERANS, DEPENDENTS, AND SURVIVORS, ch. 13 (2014), *available at* http://www.va.gov/opa/publications/benefits_book/benefits_chap13.asp; DEP'T OF VETERANS AFFAIRS, SPOUSE'S PLANNING GUIDE (2011), *available at* http://www.independenceplaceky.org/spouse_planning_guide.htm.

Military Benefits and Divorce. The rules governing benefits for divorced spouses of military personnel are rather unique, probably because of the singular nature of military service.

> ***Resource***: For a summary of the rights of a divorcing spouse who is or was married to an active member of the military, see: *Rights and Benefits of Divorced Spouses in the Military.*[76]

Military Residency. The Military Spouses Residency Relief Act ("MSRRA")[77] provides spouses of active duty military similar (but not identical) rights to those of the military member to elect to retain residency in another state in which they were previously domiciled even when they have moved out of that state as a result of their military service.

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75 WASH. REV. CODE § 11.28.120 (2015) (emphasis added).

76 MILITARY ONESOURCE, *available at* http://www.militaryonesource.mil/legal?content_id=271162 (last visited June 7, 2015); *see also Benefits*, NAT'L MILITARY FAMILY ASS'N, http://www.militaryfamily.org/info-resources/marriagedivorce/benefits.html (last visited June 7, 2015).

77 Pub. L. No. 111-97, 123 Stat. 3007 (2009) (codified in scattered sections of 50 U.S.C. app.); *see also* Marc Soss, *Military Spouses Residency Relief Act*, EST. PLAN. NEWS., no. 1569 (Dec. 30, 2009); *Military Spouse Act – Residency Relief (MSRRA)*, MILITARY BENEFITS, http://militarybenefits.info/military-spouse-act-residency-relief-msrra/ (last visited June 3, 2015).

> ***Opportunity***: MSRRA provides that a military spouse does not have to go through all of the normal residency requirements of a new state (e.g., new driver's license, voter registration, etc.) and, if the previous state of residency has a lower income tax, save income taxes.

Tax Benefits. Married couples can file joint tax returns,[78] unless the couple is divorced or legally separated at year end[79] or the "abandoned spouse" rule[80] applies. When a spouse dies before year end, the surviving spouse can still file a final joint return for the year of death.[81]

> ***Opportunity***: Non-resident aliens can elect to be treated as be treated as a resident of the United States for joint return filing purposes.[82] The non-resident alien election remains in place until revoked by the spouse, death of a spouse, legal separation, or divorce.[83]

Married couples enjoy a number of federal tax benefits. For example (but not limited to):

- The right to contribute to an IRA for a non-working spouse.
- A potentially lower marginal income tax rate if one spouse does not work or has lower income.
- A higher standard deduction.
- A higher exclusion upon sale of the residence.
- Tax-free passage of assets to the other spouse by gift or bequest.
- Lower transfer taxes using the portable transfer tax exemption of the first to die spouse.

Gift-Splitting. A spouse can elect to be treated as co-donor of the other spouse's gifts under the gift-splitting rules.[84] However, with the large transfer tax exemptions currently available, this approach will normally only be favorable if one or both of the spouses are very wealthy. See the later discussion of gift-splitting in this article.

No Due-on-Sale. A spouse, at either death or divorce, may have the right to receive a personal residence without the lender being able to call the loan, pursuant to any due on sale clause.[85] However, lenders will sometimes try to coerce the heirs into paying a mortgage assumption fee.

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78 I.R.C. § 6013 (2015).

79 I.R.C. § 7703(a)(2) (2015).

80 I.R.C. § 7703(b) (2015) for the abandoned spouse rules. See the later discussion in this article.

81 I.R.C. § 7703(a)(1) (2015).

82 I.R.C. § 6013(g)(1) (2015).

83 I.R.C. § 6013(g)(4) (2015).

84 I.R.C. § 2513(a)(1) (2015).

85 For more information see: Erik J. Murdock, Note, *The Due-on-Sale Controversy: Beneficial*

FDIC regulations[86] provide: "*With respect to any loan on the security of a home occupied or to be occupied by the borrower, (1) A lender shall not (except with regard to a reverse mortgage) exercise its option pursuant to a due-on-sale clause upon: ….*

(iii) A transfer by devise, descent, or operation of law on the death of a joint tenant or tenant by the entirety;

(v) A transfer, in which the transferee is a person who occupies or will occupy the property, which is:

(A) A transfer to a relative resulting from the death of the borrower;

(B) A transfer where the spouse or child(ren) becomes an owner of the property; or

(C) A transfer resulting from a decree of dissolution of marriage, legal separation agreement, or from an incidental property settlement agreement by which the spouse becomes an owner of the property;"

Protected Divorce Claims in Bankruptcy. The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005[87] added new bankruptcy provisions providing that unpaid child support and alimony are not dischargeable in bankruptcy[88] and entitling a first priority claim over other creditor claims, including taxes owed.[89] The former spouse must file a proof of claim with the bankruptcy court to receive payment.

Trap: If the payment is not a "domestic support obligation,"[90] then it may be discharged in bankruptcy (e.g., an obligation to pay a debt of the former married couple).

Trap: If the alimony claim is assigned to another person, the payor may be able to wipe out the debt in bankruptcy.[91]

Tenancy by Entireties. Unlike unmarried individuals, married couples can own their property as "tenants by entirety" in states which permit such ownership. Such ownership can provide unique asset protection possibilities for the couple.[92]

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Effects of the Garn St. Germain Depository Institution Act of 1982, 1984 DUKE L.J. 121.

86 12 C.F.R. § 591.5.(b) (2015) (emphasis added); *see also* Garn-St Germain Depository Institutions Act of 1982, Pub. L. No. 97-320, § 341, 96 Stat. 1469, 1505–07 (codified at 42 U.S.C. § 5402 (2012)).

87 Pub.L. No. 109-8, 119 Stat. 23 (2005) (codified in scattered sections of 11 U.S.C.).

88 11 U.S.C. § 523(a)(5) (2012).

89 11 U.S.C.. § 507(a)(1) (2012).

90 11 U.S.C. §101(14A) (2012).

91 11 U.S.C. §101(14A)(D) (2012) (defining "domestic support obligation," which excludes certain assignments of the rights).

92 For more information see: Fred Franke, *Asset Protection and Tenancy by the Entirety*, 34 *ACTEC J.* 210-233 (Spring 2009).Fred Franke and David Sessions, *Self-Settled Asset Protection Trusts for Married Couples in Maryland*, LISI Asset Protection Planning Newsletter #292, (April 23, 2015);

Resources:

- Robert B. Joslyn, *Surviving Spouse's Rights To Share In Deceased Spouse's Estate,* ACTEC Study 10 (August 2004).
- Christopher P. Cline, *Spouse's Elective Share*, 841-1st TAX MGMT (BNA).

Some Detriments of Marriage and Re-Marriage

Traditionally, bridesmaids would be dressed in similar bride-like gowns to confuse rival suitors, evil spirits, and robbers.[93]

While marriage creates a plethora of spousal rights, marriage or remarriage can also create some negative results, including (but not limited to) those noted below:

<u>Rights of the Spouse</u>. As noted in the previous section of this article, marriage can create significant rights to your decisions, assets and income in your new spouse.

<u>Loans of the Other Spouse</u>. Especially since the Great Recession, banks have become more adamant about spouses of borrowers agreeing to be personally liable for the debts of the other spouse (particularly business debts and investment debt). If both spouses are not joint owners of the business or investment, the author's firm advice to clients is to take the position: "*I do not guarantee my spouse's business debts and my spouse does not guarantee my business debts.*"

> ***Trap***: In states with strong spousal homestead rights (e.g., Florida), mortgage lenders on the homestead may insist that the non-owner spouse either guaranty the mortgage debt or waive or subordinate any spousal homestead rights.[94]

<u>Spousal Medicaid Claims</u>. Even if the clients live outside one of the Filial Support states, marriage creates a potential indirect claim on the income and assets of each spouse under Medicaid.[95] To qualify for Medicaid, the joint assets and income of a married couple are taken into account. Married couples may need to spend down both spouses' non-exempt assets before either spouse can qualify for Medicaid, even if there is a prenuptial agreement that provides that certain spousal assets are separate. Note that the rules governing Medicaid vary significantly from state to state.[96]

> ***Trap***: Because Medicaid is a governmental support program, its qualification rules are not affected by a prenuptial agreement. The government can ignore any support restrictions contained in the prenuptial in determining Medicaid qualifications of either spouse.

Spousal Impoverishment: When the assets of a married couple are taken into account in determining the disabled spouse's qualification for Medicaid, the healthy spouse

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93 BRIDE'S MAGAZINE, BRIDE'S BOOK OF ETIQUETTE 13 (2002).

94 *See the discussion at* notes 39–47 *supra*.

95 *Spouses of Medicaid Long Term Care Recipients*, DEP'T OF HEALTH AND HUMAN SERVICES (Apr. 2005), http://aspe.hhs.gov/daltcp/reports/spouses.htm. A copy of the HHS report is attached to the end of this article.

96 *See* Cynthia L. Barrett, *Advising the Elder Client: Trusts and Medicaid Eligibility*, 43 PRAC. LAW., Oct. 1997, at 57.

could be left destitute in order to meet the qualification rules. The Medicaid website notes: "*The expense of nursing home care — which ranges from $5,000 to $8,000 a month or more — can rapidly deplete the lifetime savings of elderly couples. In 1988, Congress enacted provisions to prevent what has come to be called 'spousal impoverishment,' leaving the spouse who is still living at home in the community with little or no income or resources. These provisions help ensure that this situation will not occur and that community spouses are able to live out their lives with independence and dignity. Under the Medicaid spousal impoverishment provisions, a <u>certain amount of the couple's combined resources is protected for the spouse living in the community</u>. Depending on how much of his or her own income the community spouse actually has, a certain amount of income belonging to the spouse in the institution can also be set aside for the community spouse's use.*"[97] The minimum and maximum resources that can be protected for a non-disabled spouse in 2015 are shown as an addendum at the end of this article. When you examine the numbers, there is not much protection granted to the non-disabled spouse.

Medicaid Divorce: Some couples will consider initiating a divorce to reduce the pay down of assets and income of the healthier and sometimes wealthier spouse in order for the incapacitated spouse to obtain Medicaid benefits.

Resources: A detailed discussion of Medicaid rules is beyond the scope of this article. Review the following for more information:

- MEDICAID*:* http://medicaid.gov.
- *Medicare and Medicaid Guide*, WOLTERS KLUWER, http://www.wklawbusiness.com/store/products (subscription required) (last visited June 5, 2015).
- K. GABRIEL HEISER, MEDICAID PLANNING: FROM A TO Z (2015).

<u>Veterans Benefits</u>. In general, widows and widowers who remarry before they reach age 57 cannot continue to collect veterans' survivor benefits.[98] If the marriage occurs after age 57 and the new spouse was receiving veterans' payments before remarriage, the spouse can continue receiving those benefits.

<u>Social Security Benefits</u>. Widows and widowers who remarry before they reach age 60 (or before age 50 if the widow or widower is disabled) lose the right to their prior deceased spouse's survivor benefits.[99]

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97 MEDICAID, http://medicaid.gov/ (last visited June 1, 2015) (emphasis added).

98 *See Dependency and Indemnity Compensation*, U.S. DEP'T OF VETERANS AFFAIRS, http://benefits.va.gov/compensation/types-dependency_and_indemnity.asp (last visited June 4, 2015). This rule is effective for remarriages that occur on or after December 16, 2003.

99 HANDBOOK, SOCIAL SECURITY ADMINISTRATION § 406, *available at* https://www.socialsecurity.gov/OP_Home/handbook/handbook.04/handbook-0406.html (last visited June 4, 2015), a copy of which is attached to the end of this article as an Addendum. *See* Michael J. Brien, et al., *Widows Waiting to Wed? (Re)Marriage and Economic Incentives in Social Security Widow*

> ***Opportunity***: If the second marriage ends (by divorce or death of the new spouse), then the widow or widower may have those benefits restored.[100]

Limits Under Trusts. Many non-marital trusts (particularly in second marriages) are drafted to provide that the remarriage of a former spouse will reduce or eliminate trust benefits and/or remove the spouse from acting as a Trustee.

Portability. If a widow or widower remarries, they run the risk of losing any remaining transfer tax "portable" exemption of a deceased former spouse.[101] Under the "last deceased spouse rule" if the new spouse dies before the widow or widower has used the former spouse's transfer tax exemption, the widow or widower will be limited to the exemptions of the second deceased spouse. However, as long as the new spouse is not deceased, the widow or widower can use the former spouse's unused exemptions, including if the widow or widower predeceases the new spouse.

Joint Tax Filings. If spouses file their income tax return as married filing jointly, then each spouse has joint and several liability for the taxes, penalties and interest due as a result of the filing of the return,[102] unless a spouse can successfully invoke the "Innocent Spouse" rule.[103] See the later discussion in this article.

> ***Opportunity***: If a deficiency is assessed on a joint return, and the individuals filing the joint return are no longer married or no longer reside in the same household, then upon request in writing by either taxpayer, the IRS is required to disclose in writing to the requesting taxpayer whether the IRS has attempted to collect such deficiency from the former spouse, the general nature of such collection activities, and the amount collected.[104]

Marriage Income Tax Penalty. The combination of the couple's collective income can result in their paying more in income taxes than they would have paid as single taxpayers. To calculate the additional tax cost of getting married, go to the following website: http://taxpolicycenter.org/taxfacts/marriagepenaltycalculator.cfm.

Intestacy and a Deceased Spouse's Family. While the general rule is that step-children (or other blood relatives of a deceased spouse) cannot statutorily inherit from a step-parent, a number of states[105] permit such an inheritance by intestacy if the decedent's

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Benefits (ORES, Working Paper no. 89, 2001), available at: http://www.ssa.gov/policy/docs/workingpapers/wp89.html.

100 HANDBOOK, *supra* note 99.

101 *See* Marvin D. Hills*, Subsequent Remarriage Complicates Exclusion Amount Portability*, 38 EST. PLAN. 3 (May 2011).

102 IRC§ 6013(d)(3) (2015).

103 *See* IRC. § 6015(2015).

104 IRC§ 6103(e)(8) (2015). The disclosure does not apply to any deficiency which may not be collected by reason of § 6502.

105 FLA. STAT. § 732.103(5) (2015); CAL. PROB. CODE § 6454 (2015); MD. CODE ANN., EST.

remaining statutory intestate heirs are more remote. For example, the language of the Florida statute provides: "*If there is no kindred of either part* [i.e., lineal descendants of the blood line of the maternal and paternal grandparents of the deceased]*, the whole of the property shall go to the* <u>*kindred of the last deceased spouse of the decedent*</u> *as if the deceased spouse had survived the decedent and then died intestate entitled to the estate.*"[106] Note that the use of the word "kindred" would appear to include all intestate heirs of the pre-deceased spouse, not just the spouse's lineal descendants.

> ***Drafting***: Wills should always have a "common disaster" provision that dictates how the assets will pass if none of the expected heirs survive the disposition. However, in states with the foregoing statutes, a final passage "*to my intestate heirs*" could potentially result in the kindred of a deceased spouse inheriting. Clients should consider adding a Will provision that overrides the local intestate inheritance law. For example: "*Notwithstanding applicable state law, under no condition shall my deceased spouse's blood family members be considered to be my intestate heirs.*"
>
> ***Resource***: Jeffery A. Schoenblum, *Family, Kinship, Descent, and Distribution* § III.F., 858-1st TAX MGMT. (BNA) (discussing stepchildren).

<u>Other Considerations</u>. There are a plethora of other issues to consider in getting remarried and which can lead to unintended conflict if not addressed before the marriage. Issues include:

- How will children from a prior marriage be raised? What discipline will the non-parent be permitted? What education will the children receive (e.g, homeschool, public or private school)?
- What costs for the children will the non-parent bear?
- Will the children from the other spouse's marriage have any right to inherit from the non-parent spouse?
- How will costs of the marriage be shared?
- What will the family's religious affiliation be, if any?

> ***Opportunity***: Consider recommending that new couples prepare a written Family Mission Statement that addresses these issues in advance of the wedding.
>
> ***Resource***: For more information, do a Google and/or Yahoo search on "Family Mission Statement" and "Marriage Mission Statement" to obtain examples.

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Checklist: Go to www.scrogginlaw.com for a checklist of items that clients who are remarrying should consider completing.

& TRUSTS § 3-104(e); and OHIO REV. CODE ANN. § 2105.06(J) (2015).

106 FLA. STAT. § 732.103(5) (2015). (emphasis added)

Practical Issues in Multiple Marriages

Statistics show that 67% of second marriages and 74% of third marriages end in divorce.[107] The rate of divorce was 2.5 times higher for those in remarriages versus first marriages.[108]

Dad's New Girlfriend. As married couples age, one of them will pass first. According to a 1996 University of California study, [109] 61% of widowers are engaged in a new romantic relationship within 25 months of their wife's death, while only 19% of the widows have a new relationship. According to an AARP report, [110] at age 70 men are twice as likely to have a current or recent sexual partner as women of the same age.

Dad's marriage to a woman 20 years his junior has created heartburn for many children who have been anticipating a larger and quicker inheritance. The children may attempt to aggressively insert themselves into their parent's estate planning process, creating new ethical and legal complexities for estate planning attorneys.

> ***Drafting***: Having watched their friends' experiences, wives are increasingly raising the issue of how to prevent their husband's new spouse from obtaining the family assets if the first wife is predeceases the husband.
>
> ***Opportunity:*** See the discussion in the next section on annulling a marriage after the death of a spouse.[111]

Orphaned Fathers. 8% of newly married adults have been married three times or more.[112] One unexpected consequence of this high divorce rate is increased number of divorced men who are entering their elder years without a family support structure - the "Orphaned Fathers." The dysfunctional families created by high divorce rates occasionally mean that the children and step-children are unwilling to take on the burden of aiding elderly fathers or step-fathers in their later years (e.g., declining to serve as decision makers on Medical Directives or Powers of Attorney). Interestingly, the studies report that step-children are often more willing to take care of a step-mother than a father or step-father.

Ownership of Personal Property. On February 3, 2015, the front page of the Arts section of the New York Times reported that Robin Williams' widow and his three

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107 SARÍ HARRAR & RITA DEMARIA. THE 7 STAGES OF MARRIAGE: LAUGHTER, INTIMACY, AND PASSION (2007).

108 *Id.*

109 Danielle S. Schneider, *Dating and Remarriage over the First Two Years of Widowhood*, ANN. CLIN. PSYCHIATRY 51-7, (Jun. 8, 1996).

110 LINDA L. FISHER, AARP, SEX, ROMANCE AND RELATIONSHIPS (2010). This 92-page report describes the issue in detail.

111 Discussion at notes 122-138, *supra*.

112 Gretchen Livingston, *Four-in-Ten Couples are Saying "I Do," Again*, Pew Research Center (November 14, 2014).

children from his two prior marriages were in conflict over the issue of how his assets, particularly his "*cherished belongings that include his clothing, collections and personal photographs*" should be passed.[113] As this example illustrates, conflicts often arise between children of prior marriages and the surviving spouse over the disposition of the decedent's personal property. The conflicts arise in at least two primary ways. First, the ownership of a particular asset may be in question. Unlike real property or securities, there is generally no title document evidencing ownership of personal property. A decedent who says "*pass my tangible personal property to my children*" without providing some evidentiary proof of what property he legally owns is asking for a family conflict. The surviving spouse may argue that the spouse owns the asset (e.g., "*your deceased father gave me your mother's jewelry when we married*"), or the spouse might claim the asset as part of a statutory spousal share, intestate share or personal property share.

Second, as a result of ambiguities in the disposition documents, the surviving spouse may assert that the spouse should inherit some or all the personal property of the deceased, to the detriment of the decedent's children. If such a transfer occurs, family heirlooms or sentimentally valued personal property may end up passing to relatives of the surviving spouse - to the detriment of the decedent's family.

Clients who have children from a prior relationship will sometimes say that they are not concerned about giving all personal property to the surviving spouse because the surviving spouse will "do the right thing" and pass their personal property to the client's heirs. But what happens if things do not go as planned? For example:

> ***Trap***: Suppose both spouses had children from a prior marriage. The husband died in a car accident, and the wife died the next morning. His Will passed all the tangible personal property and family heirlooms to the wife if she survived him—on the assumption she would return his family's heirlooms to his children. Her Will passed all of her tangible personal property to her husband if he survived her, and if not, to her children. Unfortunately, her children insisted that his personal property assets were their property because it belonged to their mother during the 12 hours she survived her husband.
>
> ***Trap:*** Suppose that a husband, in his second marriage, dies. His Will indicates that all of his personal property should pass to his second wife. The Personal Representative finds a safety deposit box in the husband's name that contains his deceased former wife's jewelry. The husband's daughter (who has joint signature authority on the box) says that her father always intended that her mother's jewelry go to her (and had gifted the items in the box to her), but she has no written evidence of that gift. The second wife demands the jewelry and

113 Dave Itzkoff, *Robin Williams's Widow and Children Tangle Over Estate*, N.Y. TIMES, Feb. 3, 2015,http://www.nytimes.com/2015/02/03/movies/robin-williamss-widow-and-children-tangle-over-estate.html.

argues that the daughter was just a co-lessee of the safety deposit box, rather than an owner of its contents.[114] In the absence of strong evidence of the decedent's intent, the Personal Representative could be in a difficult conflict.

Trap: We have had multiple situations in which children from prior marriages held keys to their deceased parent's residence and have gone into the house without talking to the surviving spouse or looking at the dispositive documents because "*I know mom wanted me to have all of her jewelry and art*," or some similar justification. These takings can constitute criminal theft. Moreover, it can create ill will with the surviving spouse who wanted time to grieve and handle the transfer. Unfortunately, that ill will at the start of the probate process can sour the rest of the dealings between the surviving spouse and the deceased spouse's heirs.

Trap: The wife died and the husband received all of her personal property, including a number of her family heirlooms. The widower never executed a Will and has no living descendants. At age 80 he remarried. After his death, the surviving spouse received all of his and his former wife's assets in intestacy. She sold off a significant portion of the personal property (particularly the family heirlooms) on eBay.

Caution: As soon as the client becomes disabled, or immediately upon death, we typically advise the Personal Representative (sometimes even before an appointment) to immediately change the locks on any residence or other locations holding personal property so that the Personal Representative is in control of the property. If there is a security system, the company should be notified and all codes changed as soon as possible. There may be a number of people who have access to the property. These people may think they are entitled to some particular asset and take it without consulting the Personal Representative.

Resource:

- John Scroggin & Michael Burns, *Tangible Personal Property: The Most Forgotten Part Of An Estate Plan?*, EST. PLAN. NEWSLETTER (LISI), no. 2284, Feb. 19, 2015;
- Allen L. Venet, *From the Bazaar to the Bizarre: Planning for and Administering Unusual Assets in Estates and Trusts*, 47th HECKERLING INST. ON EST. PLAN (2013).

Personal Property in Trust. If the client intends to place personal property in a marital trust (e.g., "*I give my art collection to a qualified terminable interest property (QTIP) trust for the benefit of my husband, Frank and at his death to the Getty Museum*"),

114 *See* Longstreet v Decker, 717 S.E.2d 513 (Ga. Ct. App. 2011).

then it is important to provide language allowing the surviving spouse to sell the property in the trust so it can be converted to income producing property. The failure to give the spouse this power will result in the denial of the federal marital deduction.[115] However, with the large federal transfer tax exemptions, the client might consider using a Bypass/Exemption Trust in lieu of a Marital Trust.

Reproductive Personal Property. Given the modern post-death reproductive possibilities with frozen eggs and sperm, clients who have stored their reproductive personal property should specifically provide for how the reproductive assets are to pass (e.g., to family members, to science, to charity or be destroyed).[116] Equally interesting is how the courts are handling children conceived by assisted reproductive procedures after the parent is dead.[117]

Digital Ownership and Transfers. Estates are increasingly dealing with how digital assets (e.g., websites and stored documents) are disposed of. Facebook recently provided for a process for the treatment of accounts of deceased customers.[118] To the extent an intangible digital asset has tangible or sentimental value, the estate plan should deal with how it will pass.[119]

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Checklists:

- See the personal property checklist and the Married and Single decedent personal property disposition forms at www.scrogginlaw.com
- See the Re-Marriage Checklist at www.scrogginlaw.com

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115 I.R.C. § 2056(b)(7) (2015); Treas. Reg. § 20.2056(b)-5(f) (2015).

116 For a more detailed analysis of this issue, see Jeff Pennell, *The Supreme Court Decision in Caputo: An Update on the New Biology*, EST. PLAN. NEWS. (LISI), no. 1966, May 22, 2012; Stephanie Rapkin: G*enetic Material and the Estate Plan Part 2 - Disposition of Gametes by the Donor at Death*, EST. PLAN. NEWSLETTER (LISI), no. 2228, May 27, 2014.

117 *See* JEFFREY A. SCHOENBLUM, MULTISTATE GUIDE TO ESTATE PLANNING, tbl.11 (CCH 2015); Sharon L. Klein, *The Issue With Issue: Rights of Posthumously Conceived Children,* 41 EST. PLAN. 14 (Nov. 2014).

118 *See What is a Legacy Contact*?, FACEBOOK, https://www.facebook.com/help/1568013990080948 (last visited June 2, 2015).

119 For a more detailed analysis of this issue James D. Lamm, *Digital Death: What to Do When Your Client Is Six Feet Under but His Data Is in the Cloud*," GPM LAW, http://www.gpmlaw.com/portalresource/lookup/wosid/cp-base-4-14880/media.name=/James%20Lamm%20-%20Digital%20Death%201172013.pdf; Rachel Emma Silverman, *When You Die, Who Can Read Your Email?*, WALL ST. J., (Feb. 1, 2015), http://www.wsj.com/articles/when-you-die-who-can-read-your-email-1422849600.

Limiting Spousal Rights

A number of insurance companies offer wedding insurance, which can cover any retaking of photographs, wedding cancellations, wedding attire, wedding gift replacements, and/or public liability.[120]

Perspective: Couples entering into a new marriage (particularly widows and widowers and people who have previously divorced) often have concerns about limiting the potential claims of a new spouse in the event of death or divorce. The requirements of state and federal law, as well as the couple's particular assets and facts, dictate how a spouse's rights can be reduced or eliminated. These techniques are largely "state specific" and competent local counsel are a vital element in making these decisions.

Eliminate Probate. In those states in which the spousal claim is not "augmented" by the non-probate assets of a deceased spouse, it may be possible to eliminate a spousal elective share by not having assets in the probate estate.

> ***Opportunity***: For clients in second and third marriages, eliminating the probate of any assets by beneficiary designations, "pay on death" designations and use of trusts may allow them to eliminate spousal elective shares. However, ERISA retirement plans still require a qualified spousal waiver to eliminate the surviving spouse's rights.[121]

Eliminate the Marriage. The Census Bureau reports that over 10 times as many widowers as widows over age 65 remarry.[122] In a number of states, marriages are voidable after the marriage, even by a decedent's heirs. For example:

- In a recent Wisconsin Supreme Court decision[123] the court ruled that a marriage could be voided after the death of a spouse if it was found that the decedent lacked sufficient capacity to enter into the marriage.
- Wisconsin is not alone in permitting annulment of marriages after the death of a spouse. Some states (e.g., Florida,[124] Texas[125] and New York[126]) have statutes that allow the voiding of a marriage after a spouse's death.
- In many states, the death of either of the spouses can effectively close the right of

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120 Post, Peggy. Emily Post's Wedding Etiquette. New York, NY: HarperCollins Publishers Inc. (2006); http://www.protectmywedding.com/products-services/, Accessed June 9, 2015; http://www.markeleventinsurance.com/wedding-insurance, Accessed June 9, 2015.

121 Discussion at notes 54-58, *supra*.

122 The Census Bureau reports that the highest percentage of widowers and widows are in the South.

123 McLeod v. Mudlaff (In re Estate of Laubenheimer), 2013 WI 76, 833 N.W.2d 735, 2013 Wisc. LEXIS 287 (2013);

124 FLA. STAT. § 732.805(3) (2015).

125 TEX. ESTATES CODE § 123.102 (2015).

126 N.Y. EPTL § 5-1.2(a)(1) (2015).

heirs to claim that the marriage be voided or annulled.[127]

- Lack of mental capacity is not the only basis for voiding or annulling a marriage. Other grounds for voiding a marriage can include:
  - a spouse being impotent,[128]
  - a "want of understanding" by one of the spouses,[129]
  - a spouse having a venereal disease,[130]
  - a spouse having been convicted of a felony before the marriage,[131]
  - prior to the marriage, either party had been with a prostitute, without the knowledge of the other party,[132]
  - the wife, without the knowledge of the husband, was with child by some person other than the husband,[133]
  - the husband, without knowledge of the wife, had fathered a child born to a woman other than the wife within ten months after the date of the solemnization of the marriage,[134]
  - the marriage was entered into as a result of fraud,[135]
  - a spouse being underage and marrying without any required parental consent,[136]
  - a spouse being under the influence of drugs or alcohol at the time of the marriage, or
  - on the grounds of incest or bigamy.[137]

Caution: Recognize that some marriages are automatically void and treated as a nullity from the time they were created (e.g., because of bigamy or incest). Other marriages are voidable only after a judicial hearing has made a determination of the relevant facts. The central question from an estate perspective is who can challenge a voidable marriage and what is the result of the death of one of the spouses? The rules vary widely from state to state.

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127 C.f., California statute § 2211(c) which provides that death of either spouse terminates any right of heirs to challenge the validity of the marriage.

128 C.f., TEX FA. CODE ANN. § 6.106 (2015).

129 C.f., NRS § 125.330 (2015).

130 Christensen v. Christensen, 144 Neb. 763, 14 N.W.2d 613 (1944). Generally, the other spouse must not have had knowledge of the disease when the marriage occurred.

131 C.f., VA CODE. § 20-89.1(b)(2014) - and the other spouse had no knowledge of the felony at the time or marriage.

132 Id.

133 Id.

134 Id.

135 C.f., NRS § 125.340 (2015).

136 Underage varies widely from state to state. For example, in Alabama the minimum age is 14, while in South Carolina it is 14 for a female and 16 for a male. In Kansas it is 15, unless a court allows marriage at a younger age. In Mississippi, potential spouses under the age of 21 must obtain parental consent in order to marry.

137 C.f., NRS § 125.290 (2015).

Trap: Alaska, Connecticut, New Hampshire, New Mexico (underage marriages only), New York, Oregon, Virginia, and Washington provide that alimony be paid even if the marriage has been annulled.[138]

Resources:

- Hon. C. Raymond Radigan and Jennifer F. Hillman, *'Til Death Do Us Part: Post-Death Annulment of Marriage and the Right of Election*, 42 NYSBA Trusts and Estates Law Section Newsletter No.4 (Winter 2009).
- Stephanie Rapkin, In re Estate of Laubenheimer: *Does Probate Court Have Authority to Invalidate Marriage Based on Decedent's Lack of Mental Capacity at Time of Marriage?* LISI Estate Planning Newsletter #2150 (October 2, 2013).

Exceptions to the Spousal Share Right. States have adopted a number of provisions that can deny a surviving spouse the right to claim an elective share. For example, a spousal elective share may be denied, if certain conditions apply, including:

- The marriage was void under state law (e.g., bigamy, incest, fraud) or was annulled after a judicial determination has been made.
- The claimant spouse has abandoned the deceased spouse.[139]
- Oregon provides:[140] "*If the decedent and the surviving spouse were living apart at the time of the decedent's death, whether or not there was a judgment of legal separation, the court may deny any right to an elective share or may reduce the elective share*."
- New York provides:[141] "*The right of election granted by this section is not available to the spouse of a decedent who was not domiciled in this state at the time of death, unless such decedent has elected, under paragraph (h) of 3-5.1, to have the disposition of his or her property situated in this state governed by the laws of this state*."
- The electing spouse dies before filing a claim for their elective share.[142]
- The electing spouse fails to file the election within the period provided for in the statute.

Opportunity: In some states, the spouse's elective share can also be reduced to the extent the claimant spouse received non-probate assets as a result of the decedent spouse's passing.[143] This rule may effectively permit the decedent to plan for the

138 Social Security Administration Program Operations Manual System, GN 00305.130 *Voidable Marriages*.

139 C.f., CONN. GEN. STAT. § 45a-436(g) (2015); NY CODE § 5-1.2(a)(5) (2015).

140 ORS § 114.725 (2015).

141 NY CODE § 5-1.1-a(c)(6) (2015).

142 C.f., NY CODE § 5-1.1-a(c)(3) (2015); NC GEN. STAT. § 30-3.4(a) (2015); ORS § 114.625 (2015).

143 C.f., FLA. STAT. § 732.2075(1) (2015).

particular assets (excluding the homestead) they want to pass to the spouse as an elective share. For example, the decedent may have structured his estate to assure that the family business passes to his descendants, while other (perhaps less favorable assets) pass to the surviving spouse.

Apportioning Expenses and Taxes. To limit the funds passing to a surviving spouse as an elective share and or homestead claim, clients should consider having a specific language in the dispositive documents that provides for an apportionment of part of any state or federal death taxes, debts and expenses of the estate to assets passing to a surviving spouse that are elected by the spouse against the Will. The specific language should also provide a specific and reasonable method for calculating the apportionments. Recognize that any statutory language detailing the calculation will probably govern.

> ***Caution***: The elective share is an election against the decedent's Will – effectively a rejection of the Will. As such it can be argued that a surviving spouse cannot take advantage of terms of the Will which may eliminate any apportionment of death taxes and/or expenses against the marital share.[144]
>
> A similar argument could deny the estate the right to limit the spousal elective share by allocating costs and taxes to the surviving spouse by the terms of the Will.[145] Moreover, some state statutes[146] specifically provide that the elective share cannot be reduced by the apportionment of death taxes to the share.
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> ***Trap***: The reduction of the marital deduction by the apportionment of death taxes can create a tax-spiral, effectively increasing the total estate taxes which may be due from the estate. But, if the desire is to reduce the assets passing to the surviving spouse, the client may view this additional tax cost as a penalty or disincentive for electing outside the Will.
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> ***Resource:*** BNA Portfolio 841-1st: Spouse's Elective Share, § VII._Impact on Other Beneficiaries, § C. Estate Tax.

Gifts in Contemplation of Death. Connecticut is the only state with a state gift tax. Minnesota adopted a gift tax on June 30, 2013 and then retroactively revoked it on March 21, 2014. For clients facing a tax gap between the state and federal death tax exemptions, making lifetime gifts may be a way to reduce the state death tax.[147] Making gifts of assets proximate to the donor's passing can also potentially

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144 See: DeShazo v. Smith, No. 1:05-cv-01046 (E.D. Va. 11/22/06) and In re Estate of Thompson, 512 N.W.2d 560 (Iowa 1994).

145 See: Weeks v. Vandeveer, 233 N.E.2d 502 (Ohio 1968).

146 C.f., OHIO REV. CODE §2113.86(D) (2015): TENN. CODE § 31-4-101(d) (2015).

147 For a more detailed analysis of this issue, see Debra L. Stetter, *Deathbed Gifts: A Savings Opportunity for Residents of Decoupled States,* 30 EST. PLAN. 270 (June 2004).

eliminating the spousal elective share of a surviving spouse. However, the Uniform Probate Code provides that the spousal elective share is only eliminated if the donor survives the gift by two years.[148]

Trap: Some states have rules that provide that certain "gifts in contemplation of death" remain subject to a state death tax. As of January 1, 2015, these states include Iowa, Kentucky, Maryland, Nebraska, New Jersey, and Pennsylvania.[149] The rules vary widely (e.g., the period of "contemplation") and in some cases are rebuttable. There are a number of other states which had contemplation of death inclusions, but the repeal of their state death taxes effectively eliminated the issue. These states include Indiana,[150] Ohio,[151] and Tennessee.[152]

If a gift is taxable for state death tax purposes after the donor's death, then a number of issues can arise, including:

- The client has not eliminated the state death tax on the gifted assets, but for federal tax purposes, they may have lost the potential for a step up in basis of the gifted assets.
- Does the inclusion of the gift result in an estate becoming taxable for state tax purposes?
- Does the donee have the funds to pay any state death tax? Is the state death tax allocable to the residuary of the estate versus the donee?
- What fiduciary responsibilities does the estate administrator have for determining the gifts that were made and reporting them to the state Department of Revenue?
- Are exceptions made for annual exclusion gifts?

Trap: Make sure the gift transfer is completed before the donor's passing.

Life Insurance. Life insurance owned by the decedent/insured in those states which have augmented spousal shares can increase the claim of a surviving spouse, even if the insurance is paid to a named beneficiary.

Opportunity: Clients who want to eliminate spousal elective shares should consider moving new or existing life insurance into an Irrevocable Life Insurance Trust to eliminate a spousal claim.

Trap: Beware of the two year contemplation of death rule in the Uniform

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148 *UNIFORM PROBATE CODE § 2-205-(3)(C) (as Amended in 2010). Note that a number of states that have adopted the UPC have not adopted this two year rule.*

149 JOEL MICHAEL, RESEARCH DEP'T, MINN. HOUSE OF REPRESENTATIVES, SURVEY OF STATE ESTATE, INHERITANCE AND GIFT TAXES 12 (2014).

150 Indiana repealed its inheritance tax effective as of January 1, 2013.

151 Ohio has repealed its state estate tax and inheritance tax effective as of January 1, 2013.

152 Effective January 1, 2016, Tennessee's inheritance tax will be eliminated.

Probate Code[153] and the three year federal estate tax inclusion rule for the transfer of existing life insurance policies.[154]

Waivers. Given all of the marital rights noted in the prior section of this article, reducing or eliminating those rights may be vitally important, particularly when second and third marriages occur and one or both of the spouses want to limit the rights of the other spouse. In many states, spousal rights may be waived by the new spouse before or after the wedding if required standards are met.[155] For example, the Alabama code[156] provides: "*The right of election of a surviving spouse and the rights of the surviving spouse to homestead allowance, exempt property and family allowance, or any of them, may be waived, wholly or partially, before or after marriage, by a written contract, agreement, or a waiver signed by the party waiving after fair disclosure. Unless it provides to the contrary, a waiver of 'all rights' (or equivalent language) in the property or estate of a present or prospective spouse or a complete property settlement entered into after or in anticipation of separation or divorce is a waiver of all rights to elective share, homestead allowance, exempt property and family allowance by each spouse in the property of the other at death and a renunciation by each of all benefits which would otherwise pass to him from the other by intestate succession or by virtue of the provisions of any will executed before the waiver or property settlement.*"

Prenuptial Agreements. Prenuptial agreements have become a significant part of the estate planning and asset protection process. Probably the last thing an engaged couple wants to do is meet with their paranoid lawyers to discuss the possibility of their premature death, incapacity or divorce. Nonetheless, it should also be a vital part of the preparation for marriage. Prenuptial agreements tend to take a bit of the romance out of the first marriage, but by the second or third marriage the historic reality of divorce often creates a different perspective.

Drafting: The pre-nuptial agreement must be carefully drafted. Among the ways to increase the enforceability of the prenuptial agreement are:

- Prenuptial agreements are governed by state law and the state laws vary significantly. Make sure the agreement addresses the unique requirements and rulings in the domiciliary state of the couple.
- Make sure the document contemplates the impact of the couple moving to a state with differing laws (e.g., the homestead rights of a surviving spouse in Florida).
- Make sure that the pre-nuptial thoroughly discloses the income, assets and liabilities of each person. Be as specific as possible. Listing specific account

153 *Supra*, Note 148.

154 I.R.C. § 2035 (2015).

155 *See* UNIF. PREMARITAL AGREEMENT ACT; UNIF. PROB. CODE § 2-213 (UNIF. LAW COMM'N 2008).

156 ALA. CODE § 43-8-72 (2015).

numbers and the date of valuation may be an important element when a judge or jury subsequently reviews the agreement. Consider attaching copies of each party's state and federal income tax returns and financial account statements to the agreement. If a client anticipates a sizable inheritance, it may even be advisable to disclose the existence and possible ranges of value of such an inheritance.

- Make sure that each party has competent (e.g., has the attorney ever dealt with a prenuptial agreement before?) and independent legal representation in the negotiation and drafting of the agreement with the attorneys also signing the agreement. A court might rule that the less wealthy spouse lacked an adequate understanding of the agreement because competent counsel was absent. One attorney should never represent both parties. It might even make sense to have the signing of the document videotaped to show that each party was represented by counsel who thoroughly explained the document to the client.
- Sign the agreement well in advance of the marriage. If one of the spouses has not had adequate time to review the agreement (e.g., it is delivered the day of the marriage), the court could focus on whether the signature was coerced, and if so, invalidate the agreement.[157]
- The agreement should not create an "unconscionable" result. This is an ambiguous concept at best,[158] but planners must take into account the potential review by the court as to the fairness and reasonableness of the document.
- Make sure the agreement provides for relinquishment not only of rights in divorce, but also deals with the rights of either spouse against the estate of a deceased spouse.[159] Consider providing that any un-waived spousal elective share must be held in trust and pass to the first to die spouse's heirs at the death of the surviving spouse.
- As noted previously in this article, marriage can make each spouse legally liable for the long term care costs of the other. To protect against those claims, consider having the prenuptial agreement waive any such rights, but recognize that state statutes may effectively override the prenuptial agreement.[160]

Resources:

- DAVID WESTFALL & GEORGE MAIR, ESTATE PLANNING AND TAXATION ch.

157 Flaherty v. Flaherty, 128 So. 3d 920 (Fla. Ct. App. 2013); *see also* Chuck Rubin, Flaherty v. Flaherty*: Spouse Need Not Challenge a Voidable Prenuptial Agreement during the Marriage*, EST. PLAN. NEWS. (LISI), no. 2184, Jan. 16, 2014.

158 For example, in *Dematteo v. Dematteo*, 762 N.E.2d 797 (2002), the Massachusetts Supreme Judicial Court provided that upon a divorce from a husband worth $83–$108 million, a prenuptial agreement which provided the ex-spouse an annual payment of $35,000, the marital home, an automobile and medical insurance until death or remarriage was not unconscionable.

159 For example, in *Pysell v. Keck*, 559 S.E.2d 677 (Va. 2002), the Virginia Supreme Court ruled that the prenuptial agreement's failure to specifically waive rights against the estate of a deceased husband allowed the surviving wife to make certain statutory spousal survival rights against the estate—even when the Will made no provision for the surviving wife.

160 Peterson, *supra* note 70.

11 (WG&L 2015).
- Linda J. Ravdin, *Marital Agreements*, 849-2nd TAX MGMT. (BNA).
- Arlene G. Dubin & Carole M. Bass**,** *Ten Tips for Estate Planners Who Draft Prenuptial Agreements*, 42 EST. PLAN. 3 (June 2015).
- Carlyn S. McCaffrey*, With All My Worldly Goods I Thee Endow, Except as Provided in Article Five,* 47TH HECKERLING INST. ON EST. PLAN. (2013).
- Cohen and Schlissel, *Thinking Through the Tax Ramifications of a Prenup*, 33 Family Advocate No. 3.

Post-Nuptial Agreements. An increasing phenomenon has been the development of post-nuptial agreements. These agreements are drafted after marriage and provide for the treatment if the parties subsequently divorce. In most cases, they are a result of some traumatic event in the marriage (e.g. an affair). Such agreements are similar to legal separation agreements, but rather than focusing on separation, they are designed to foster reconciliation. They can also be a punitive mechanism fostered upon a wayward spouse who is unwilling to terminate the marriage.

Resources:
- Judith E. Siegel-Baum & Josh W. Averill, *Post-Nuptial Agreements can Resolve Personal and Estate Planning Issues*, 29 EST. PLAN. 405 (Aug. 2002);
- PETER SPERO, ASSET PROTECTION: LEGAL PLANNING, STRATEGIES AND FORMS § 4.10 (2015);
- DAVID WESTFALL & GEORGE MAIR, ESTATE PLANNING AND TAXATION ch. 12 (WG&L 2015).
- Linda J. Ravdin, *Marital Agreements*, 849-2nd TAX MGMT. (BNA).

ERISA and Waivers. In a series of decisions, the federal courts have ruled that a spouse's right to an ERISA retirement plan cannot be waived prior to the marriage of the parties.[161] Thus, if the parties intend for such waiver, a renunciation of such rights should be signed after the marriage occurs. A waiver before marriage may be void. However, although the pre-marriage waiver may not be effective upon the death of the plan participant, it might be effective upon the divorce of the parties.[162]

Opportunity: Clients are well advised to consider having a spouse waive any ERISA retirement rights after the marriage is completed. Just because the current value of the retirement accounts are relatively insignificant does not

161 *See* Hagwood v. Newton, 282 F.3d 285 (4th Cir. 2002); Nat'l Autos. Dealers & Assoc. Ret. Tr. v. Arbeitman, 89 F.3d 496 (8th Cir. 1996); Howard v. Branham & Baker Coal Co., 968 F.2d 1214 (6th Cir. 1992); Hurwitz v. Sher, 982 F.2d 778 (2nd Cir. 1992); *see also* 26 U.S.C. §§ 417(a), 1055 (2012); Treas. Reg. § 1.401(a)-20 Q&A 28 (2015). *But see* Strong v. Dubin, 75 A.D.3d 66 (N.Y. Sup. Ct. 2010).

162 *See In re* Rahn, 914 P.2d 463 (Colo Ct. App. 1995)

mean they will be small when a divorce occurs.

Opportunity: Treasury Regulation § 1.401(a)-20, Answer 27 provides a number of exceptions to the ERISA spousal consent rights: It reads: "*If it is established to the satisfaction of a plan representative that there is no spouse or that the spouse cannot be located, spousal consent to waive the QJSA or the QPSA is not required. If the spouse is legally incompetent to give consent, the spouse's legal guardian, even if the guardian is the participant, may give consent. Also, if the participant is legally separated or the participant has been abandoned (within the meaning of local law) and the participant has a court order to such effect, spousal consent is not required unless a QDRO provides otherwise.*"

ERISA and IRAs. IRAs are not governed by ERISA. Subject to state laws, an IRA owner may be able to eliminate a spouse's right to inherit or make a claim against an IRA.

Opportunity: In Charles Schwab v. Debickero,[163] a husband rolled a 401(k) into an IRA after retirement. The husband named his children as the IRA beneficiaries. When the IRA owner passed away, his wife argued that because her husband had rolled his 401(k) into the IRA, she should receive the same protections that his ERISA qualified retirement plan had provided to her. The Ninth Circuit disagreed: "*Thus, under both § 401(a) and the accompanying regulations, there is no basis for imposing on the Schwab IRA the automatic survivor annuity requirements of § 401(a)(11) and overriding the beneficiary designations rightfully made by Wilson in establishing the account.*"[164]

Opportunity: Because the ERISA rules do not apply to IRA accounts,[165] any spousal elective rights that might include an IRA account can be waived before the marriage, if permitted by state law.

Trap: A Tax Court ruling, Bunney v. Commissioner,[166] may give a client pause when trying to extract revenge from a spouse 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, the court ruled that all the taxable income went to the husband, and he was responsible for the 10% early

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163 593 F.3d 916 (9th Cir. 2010); *see also* Brad Dewan, *Charles Schwab & Company v. Chandler – Surviving Spouse Benefits & IRAs*, EMP. BENEFITS & RET. PLAN. NEWS., no. 519, Mar. 17, 2010.

164 Id.

165 29 C.F.R. § 2510.3-2(d) (2015); I.R.C. § 417 (2015).

166 114 T.C. 259 (2000).

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.

IRA Trusts. Many clients in second and third marriages are concerned that passing their substantial IRA accounts directly to a spouse will either result in a rapid dissipation of the IRA or result in IRA funds that remain upon the spouse's death ultimately passing to someone other than the clients' family members (e.g., a new spouse or children from a prior marriage). To provide current benefits to a spouse while placing a "gate keeper" trustee between the spouse and the assets, the clients should consider the use of a "Qualifying Trust" or a "Conduit Trust."[167] These trusts can also limit the claims of creditors on a spousal inherited IRA after the Clark v. Rameker decision.[168]

Trap: In states which have a broad augmented spousal elective share, the surviving spouse may be able to make a claim against the IRA, notwithstanding the decedent's intentions.

Drafting: When drafting a IRA trust for the benefit of a spouse, particularly a second or third spouse, consider having the spouse waive any rights (e.g., spousal elective share in an augmented state) to the IRA as a part of the documents being signed. Because the couple might move to an "augmented" state, this waiver should be made even if the domicile state has limited spousal rights to make claims against an IRA.

Resource: Natalie B. Choate, Life and Death Planning for Retirement Benefits (2011).

State Elimination of Claims. Largely because of continual mistakes by divorced residents, at least 23 states have adopted statutes which provide that divorce automatically results in a deemed elimination of beneficiary designations for the benefit of the former spouse.[169] For example, Florida provides that a former spouse is treated as predeceasing the decedent when a divorce occurs.[170]

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167 See: Dedon and Buskirk, supra note 28.

168 134 S. Ct. 2242 (2014). See the discussion of the Clark decision in the final section of this article.

169 See the excellent article by Leslie A. Shaner, *When Clients Fail to Change Beneficiary Designations*, FAM. L. MAG. (Dec. 10, 2013), http://www.familylawyermagazine.com/articles/beneficiary-designations. *See also* UNIF. PROB. CODE § 2-804 (UNIF. LAW COMM'N 2014)

170 FLA. STAT. § 732.703 (2015); *See* Jeff Baskies, *New Florida Statute Clarifies Impact of Divorce on Non-Probate Assets*, EST. PLAN. NEWS. (LISI), no. 1990, July 23, 2012.

Trap: A number of Supreme Court decisions[171] have indicated that state statues that automatic rescissions upon divorce do not apply to ERISA retirement plans and other federally provided benefits because federal law preempts state law with regard to such rights.[172] Therefore, clients are well advised to promptly review and modify all beneficiary designations as a part of their marriage or divorce.

Resources:

- John H. Langbein, *Destructive Federal Preemption of State Wealth Transfer Law in Beneficiary Designation Cases: Hillman Doubles Down on Egelhoff*, 67 VAND. L. REV. 1665 (2014).
- Leslie A. Shaner, *When Clients Fail to Change Beneficiary Designations*, FAM. L. MAG., (Dec. 10, 2013), *available at* http://www.familylawyermagazine.com/articles/beneficiary-designations.
- Albert Feuer, *Determining the Death Beneficiary Under an ERISA Plan and the Rights of Such A Beneficiary*, 54 TAX MGMT. MEMO. 323 (2014).
- Albert Feuer, *The Supreme Court Finds Federal Life Insurance Rules Preempt State Law in Hillman v. Maretta and Reinforces ERISA Protections for ERISA Plan Participants and Beneficiaries*, 32 TAX MGMT. WEEKLY J. (Aug. 2013).

Self-Settled Spendthrift Trusts. Prenuptial agreements can take a lot of the romance out of the impending marriage and create some tense negotiations. An alternative may be the creation of a self-settled trust before the marriage. Traditionally, states have not allowed individuals to set up “self-funded” spendthrift trusts. That is, the grantor of a trust was not allowed to set up a trust against which his creditors (including a divorcing spouse) could not make claim. As a result many clients have created overseas asset protection trusts to restrict the claims of future creditors.

In recent years, a number of states have provided limited protection for a grantor of self-settle spendthrift trusts. For example, Alaska allows the creation of self-funded spendthrift trusts, which deny spousal claims even if the marriage existed at the time of the trust’s creation.[173] These trusts (and similar trusts in other states) may open up an opportunity for a client to create a self-funded spendthrift trust, which is protected from a new spouse without using an unromantic prenuptial agreement.

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171 Hillman v. Maretta, 133 S.Ct. 1943 (2013); Kennedy v. DuPont Savings and Investment Plan, 555 U.S. 285 (2009); Egelhoff v. Egelhoff, 532 U.S. 141 (2001); Ridgeway v. Ridgeway 454 U.S. 46 (1981); Wissner v. Wissner, 338 U.S. 655 (1950). A number of state courts have issued similar rulings (*see, e.g.*, *In re* Sauer, 32 A.3d 1241 (Pa. 2011)).

172 ERISA § 514(a) (codified at 29 U.S.C. §1144(a) (2012)) provides that ERISA “*shall supersede any and all State laws insofar as they may now or hereafter* relate *to any [ERISA] employee benefit plan.*”

173 *See* Douglas J. Blattmachr & Richard W. Hompesch II, *Alaska and Delaware: Heavyweight Competition in New Trust Laws*, 12 PROB & PROP. 32 (Jan/Feb. 1998).

While a comparison of the state and foreign trust rules are beyond the scope of this article, planners should carefully consider the advantages and disadvantages of creating self-funded spendthrift trusts in one of the states which offer greater creditor protection.[174] Such trusts may be created in lieu of or as part of a prenuptial agreement. If created as a part of prenuptial agreement, the client should fully disclose the existence of the trust. Preferably, the trusts should be created before the marriage occurs.

> ***Caution***: A Bankruptcy Court may disagree with the protections potentially obtained by the use of a self-settled spendthrift trust.[175]

> ***Resource***: Daniel S. Rubin, *Protecting Assets Without the Pre-Nup: Use a Self-Settled Trust*, 47TH ANNUAL HECKERLING INST. ON EST. PLAN. (2013).

Transfers in Contemplation of Divorce. Divorce is rarely a surprise. As a result many clients attempt to reduce the potential claims of a divorcing spouse. These techniques can include:

- Hiding assets to minimize the allocation of marital assets upon divorce. This approach is extremely dangerous because the divorcing spouse may require statements about assets under penalties of perjury. The deceptive practice can also tick off the judge hearing the divorce case.
- Some planners have advised moving assets off-shore. Some have questioned whether the use of such off-shore trusts provide better divorce protection than a U.S.-based spendthrift trust. Consider Reichers v. Reichers, in which the court recognized that it had no jurisdiction over off-shore trust assets and did not require the movement of the off shore trust assets back to the U.S.[176] Instead, the court took into account the off-shore assets in awarding Dr. Reicher's assets to Mrs. Reichers.
- If justifiable for other purposes, it may make sense to move assets into vehicles which restrict the ability of a spouse to access the underlying assets. For example, it might be possible to move assets into a family limited partnership that has both estate planning and asset protection benefits. Recapitalization of a family company and the passage of voting control of the company to entities (e.g., trusts) outside the client's control may make sense.
- It may make sense to exchange assets for another right which limits the benefit to an ex-spouse. For example, a client could sell a piece of real estate for a

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174 *Id.*; RICHARD W. NENNO & W. DONALD SPARKS, DELAWARE DYNASTY TRUSTS, TOTAL RETURN TRUSTS, AND ASSET PROTECTION TRUSTS (2002); RICHARD W. NENNO, PERPETUAL DYNASTY TRUSTS (2010); ALA-ABA, *Planning Techniques for Large Estates* (Apr. 2002).

175 C.f., In re Castellano, 2014 WL 3881338 (Bk.N.D.Ill., Aug. 6, 2014); Jay Adkisson, David Slenn & Philip Martino, *In re Castellano: A Wake-Up Call for Self-Settled Trusts and Spendthrift Provisions*, LISI Asset Protection Planning Newsletter #258, (September 8, 2014).

176 679 N.Y.S.2d 233 (N.Y. Sup. Ct. 1998).

private annuity payable over the client's lifetime. As a further example, a client might transfer the residence into a qualified residential trust, retaining a limited term of years, with the remainder passing to heirs.

- The gifting of important family assets might also make sense. For example, the use of annual exclusion gifts to gift a family farm to descendants might make sense. It might even make sense to have the spouse agree to gift-split the gift.

Caution: To minimize fraudulent conveyance issues, any transfer in contemplation of divorce should be made as far in advance of the divorce as possible. In addition, if the transferor receives no consideration for the transfer or the court deems the actions were intended to defraud the soon to be ex-spouse, the transfers may be rescinded.

Trust Payments in Divorce. A number of states have ruled that mandatory distributions (e.g., mandatory payout of trust income or a uni-trust) and distributions in accordance with an ascertainable standard can be taken into account in setting the alimony of a beneficiary. For example, see:

- Delaware – Garretson v. Garretson, 306 A.2d 737 (1973).
- New Hampshire – N.H. REV. STAT. ANN. § 564-B:5-503(b)(1)–(2) (2015).
- Florida – FLA. STAT. ANN. §§ 736.0503–0504 (West 2015).

Drafting: To reduce this exposure, clients should avoid mandatory trust distributions and ascertainable standards for their heirs,[177] replacing them with discretionary trusts. To the extent mandatory trust distributions and ascertainable standards are used, consider providing that upon the filing for divorce of an heir, all distributions to the heir become at the sole discretion of an independent trustee.

However, in some states the right to payments of alimony and/or child support may still be made from discretionary trusts.[178] Attorneys should discuss these issues with clients and discuss whether it makes sense to move the situs of trusts to jurisdictions with better asset protection for beneficiaries.

Moreover, if a beneficiary has a legal ability to obtain the trust property (e.g., a general power of appointment), the divorcing spouse may be able to claim that the assets subject to the power are a property right to be taken into account in the divorce proceedings.

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177 i.e., "*maintenance and support*" obligations in an ascertainable standard may be construed to include alimony payments.

178 *See, e.g.*, Berlinger v. Casselberry, 113 So. 3d 961 (Fla. Ct. App. 2013); *see also* Jonathan Gopman, et al., Berlinger v. Casselberry*: Why the Decision Was Wrong and Florida May Not Be a Bad Trust Jurisdiction for Discretionary Trusts,* ASSET PROTECTION PLAN. NEWSLETTER (LISI), no. 237, Feb. 13, 2014; Barry Nelson, *Berlinger v. Casselberry: Discretionary Trust Held to be Available to an Alimony Creditor*, ASSET PROTECTION PLAN. NEWSLETTER (LISI), no. 231, Dec. 10, 2013.

Resources:

- Peter Spero, ASSET PROTECTION: LEGAL PLANNING, STRATEGIES AND FORMS ¶ 6.12;
- Steve Oshins & Bob Keebler, *The 40th Anniversary of Garretson v. Garretson: Spendthrift Trusts and Divorce Protection,* ASSET PROTECTION PLAN. NEWSLETTER (LISI), no. 217, Jan. 10, 2013;
- Edward D. Brown & Hudson Mead, *Protecting Family Inheritances From Divorce,* Trusts and Estates (June 2013).

Change of Residency. Spousal rights vary widely from state to state. Moving to another state can change the inheritance rights and powers of a surviving spouse.

Opportunity: The amount of the spousal elective share can vary widely from state to state. Georgia is the only state that does not permit a spouse to make a spousal elective share claim.[179] The Georgia statues[180] provide: *"A testator, by will, may make any disposition of property that is not inconsistent with the laws or contrary to the public policy of the state and may give all the property to strangers, to the exclusion of the testator's spouse and descendants."*

Opportunity*:* Moving to a state with a little to no augmentation of the spousal share could provide opportunities to reduce the value upon which the spousal elective share is computed.

Trap: Clients may inadvertently and unexpectedly increase the rights of a spouse when they change the state of domicile (e.g., a move from Georgia to Florida). When changing residency it makes sense to evaluate the rules governing the rights of spouses and children in the new state of domicile, particularly in Community Property states.

Opportunity or Trap? Depending upon which side of the inheritance you are on, moving an incapacitated spouse to a jurisdiction with greater benefits for the surviving spouse may be a method of increasing the surviving spouse's inheritance. For example, a couple in their second marriage with children from prior marriages resides in Georgia. Each spouse executed a Will that disinherits the surviving spouse in favor of the testator's descendants. The husband is now in an Alzheimer unit and the wife (who holds a general power of attorney and medical directive) wants both of them to "retire" to Florida. Neither spouse has waived any marital rights. The change of domicile could result in the wife being able to claim a Florida spousal elective share and make a claim against the homestead property.

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179 But in Georgia a surviving spouse will be entitled to some estate funds using a statutory rule called "Years Support." GA. CODE ANN. § 53-3-1 to -20 (2015).

180 GA. CODE ANN § 53-4-1 (2015).

Trap: A martial agreement that waives all spousal benefits before the couple moved to another state may not be enforceable to the extent the spousal rights were only acquired when the couple became a resident of the second state. The argument of a surviving spouse may be similar to the ERISA issues on prenuptial waivers – you cannot prospectively waive a right you do not yet have. Moreover, the new state's law may require a "fair disclosure" as part of any waiver to spousal rights – a requirement that the previous waiver may not satisfy.

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Resources:

- Steve Oshins & Martin Bearg, *Tannen v. Tannen: Keeping Trust Assets off the Table in a Divorce*, EST. PLAN. NEWS. (LISI), no. 1904, Dec. 12, 2011.
- Jeffery Pennell, *Minimizing the Surviving Spouse's Elective Share*, ALI Estate Planning in Depth (2014);
- Christopher P. Cline, *Spouse's Elective Share*, 841 TAX MGMT. § VI;
- Laura Rosenbury, *Two Ways to End a Marriage: Divorce or Death*, 2005 UTAH L. REV. 1127.
- Terry L. Turnipseed, Community Property v. The Elective Share, 72 La. L. Rev. (2011) Available at: http://digitalcommons.law.lsu.edu/lalrev/vol72/iss1/8

Negotiation of Divorce Decrees and Marital Agreements

Facebook use seems to be connected to the increased possibility of divorce.[181]
In 2015 a New York court allowed a wife to serve divorce papers on her elusive husband using Facebook.[182]

Planning for dissolution of a marriage raises a number of complicated issues. It's more than just signing a standard form document to dissolve a marriage. The issues include:

Net After-Tax Value. The basis of assets transferred as a result of divorce should be an important part of the divorce negotiating process. However, courts may be reluctant to get embroiled in speculative tax consequences of a divorce. For example, in In Re Marriage of Fonstein,[183] the California Supreme Court stated: "*Regardless of the certainty that the tax liability will be incurred if in the future an asset is sold, liquidated or otherwise reduced to cash, the trial court is not required to speculate on or consider such tax consequences in the absence of proof that a taxable event has occurred during the marriage or will occur in connection with the division of the community property*."

While the court may refuse to get involved with tax basis issues, divorce negotiations should take into account the after-tax value (including the cost of satisfying any secured debt) of an asset, not just its fair market value.

> ***Example***: Assume a spouse has a choice between taking $1.0 million in cash or $1.2 million in stock which has a zero basis. Which is the better option? For tax purposes (assuming an immediate stock sale), the $1.0 million in cash may be a better choice. Why? Assuming a combined state and federal capital gains tax rate of 30%, the $1.2 million is stock carries an inherent tax cost of roughly $360,000, meaning the stock has a true after-tax value of only $840,000.
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> ***Trap***: Do not assume that your client's divorce attorney understands the tax ramifications of the divorce settlement. Many divorce attorney engagement letters specifically disclaim the attorney's responsibility for any tax or estate planning issues involved in the settlement. If you know a client is going

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181 *See* Sebastián Valenzuela, et al., *Social Network Sites, Marriage Well-Being And Divorce: Survey And State-Level Evidence From The United States*, 36 COMPUTERS IN HUM. BEHAV. 94 (July 2014); *see also* Neal Augenstein, *Study: Facebook Affects Divorce Rates, Marital Satisfaction*, WTOP (July 14, 2014), http://wtop.com/news/2014/07/study-facebook-affects-divorce-rates-marital-satisfaction/ (discussing the Valenzuela study).

182 Barbara Ross & Dareh Gregorian, *Judge Says Brooklyn Woman Can Use Facebook to Serve Divorce Papers*, N.Y. DAILY NEWS (Apr. 6, 2015, 2:30 AM), http://www.nydailynews.com/new-york/brooklyn/exclusive-woman-facebook-serve-divorce-papers-article-1.2174577.

183 522 P.2d 1169 (Cal. 1976).

through a divorce or legal separation, advise them in writing that it is in their best interest to have a competent tax advisor be an integral part of any settlement negotiations.

Caution: Clients and their advisors should be aware of the potential adverse result of a spouse receiving an asset which is secured by a liability that exceeds the tax basis of the asset. See the discussion in the next section of this article.

Tax Basis Records. There are no federal laws mandating that the transferor spouse provides basis and holding period information to the recipient spouse. Although Treasury Regulations[184] require that such information be provided at the time of any transfer, there are no penalties for failing to provide the information.

Drafting: Any property 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 client's unsupported tax filings.

Alimony is Earned Income. I.R.C. §219(f)(1) provides that alimony is considered earned income for IRA purposes.

Opportunity: Assume a non-working 51-year-old spouse is getting divorced. Allocating a portion of any "property" settlement to long term alimony (e.g., $6,500 per year) would create an income tax deduction for the payer and allow the payee to fund a tax-deductible IRA contribution.

Interestingly, I.R.C. §219(f)(7) provides that non-taxable combat pay is also treated as earned income for IRA contribution purposes. Is there a theme here?

Dependency Deductions. The tax savings from being entitled to the dependency deduction for a couple's children should be a part of the negotiations. Assuming all of the dependency exemption requirements are met,[185] the parents can enter into a written declaration[186] governing which of them will be entitled to the exemption for a dependent child.[187] While the parent in the higher income tax bracket will normally receive the greater tax benefit for the dependency exemption, the phase-out of personal and dependent exemptions for higher income taxpayers should be taken into account in making this decision. Before making a final decision, run the projected tax benefits for each spouse over the years they might be entitled to the deduction.

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184 Temp. Treas. Reg. § 1.1041-1T, Q&A-14 (2015).

185 I.R.C. § 152(e) (2015).

186 The form's requirements are provided for in Treas. Reg. § 1.152-4(e)(1) (2015).

187 Ellen D. Cook, *Final Regs. Clarify Which Divorced Parent Can Claim Child As Dependent*, 81 PRAC. TAX STRATEGIES 206 (Oct. 2008).

In some states,[188] the court does not have authority to award the dependency deduction to the non-custodial parent without the custodial parent's approval, giving the custodial parent additional leverage in the negotiations.

> ***Trap***: The custodial parent is normally the party responsible for filing and paying the "kiddie tax" of an applicable child.[189]

> ***Trap***: A parent may revoke the dependency declaration by notifying the ex-spouse and filing IRS form 8332.[190]

Divorce Trusts. Divorces are seldom amicable. As a result, conflicting perspectives and desires for control can create implacable disagreements. For example, a less wealthy spouse will be concerned that the wealthier spouse will renege on support payments or have future financial problems. The wealthier spouse may not want a former spouse to remarry and still receive benefits or the wealthier spouse may not want to benefit the heirs of the soon-to-be ex-spouse.

One solution may be the creation of a divorce trust. While divorce trusts are not regimented, there are the general terms of that will normally apply. For example:

- The trust could provide for payments equal to the settlement terms between the divorcing couple.
- The trust must generally be irrevocable to avoid adverse tax consequences and to provide the beneficiary spouse some assurance of payment.

While creative planning may offer new approaches, in most cases, these trusts will generally fall into one of the following approaches. Assume the husband holds the larger wealth.

Lifetime QTIP. The husband can create a lifetime Q-TIP trust for the wife, with the provision that the trust rolls over to a trust for his descendants at her death. The assets remain available to benefit the wife for life. At her death the basis in the assets step-up to their fair market value and her available estate exemption can reduce the family's overall estate tax. The husband makes a timely election to treat the trust as a Q-TIP trust[191] eliminating any gift tax on the transfer to the trust.

> ***Trap***: Code §682 provides that upon divorce, the donee spouse pays tax on distributed income from a trust that was a grantor trust as to the donor spouse.[192] For gift tax purposes, a qualified terminable interest property trust is a trust in which the donee spouse has a qualifying income interest for life and

188 C.f., Georgia: Blanchard v. Blanchard, 401 S.E.2d 714 (Ga., 1991).
189 I.R.C. § 1(g)(5) (2015).
190 Treasury Regulation § 1.152-5(e)(3) (2015).
191 I.R.C. § 2523(f)(4) (2015).
192 I.R.C. §682 (2015).

to which a gift tax QTIP election has been made.[193] An interest subject to termination upon a divorce will not qualify for the gift tax QTIP election.[194] Therefore, post-divorce income must continue to be distributed to the donee spouse. But for §682 this income would be includable in the gross income of the donor spouse pursuant to Code §672(e)(1)(A). Therefore, §682 overrides the grantor trust rules and taxes income to the divorced donee spouse. But Code §682 doesn't apply to shift income tax on accumulated capital gains from the donor spouse (or the trust) to the donee spouse post-divorce.[195] If the lifetime QTIP is a grantor trust as to principal, the donor spouse will continue to pay income tax on undistributed capital gains post-divorce during the lifetime of the donee spouse. [196]

Bypass Trust. But what if the donor spouse wants the trust to cease providing benefits to the soon-to-be ex-spouse before her death (e.g., after a stated number of years or the remarriage of the spouse or when she remarries)? In that case, the donor spouse will effectively be forced into using some form of a lifetime By-Pass trust because the rules governing QTIP Trusts would not permit such an early termination before the beneficiary/spouse's death. There are at least two major downsides to this decision. First, upon the termination of the trust benefits to the ex-spouse, there is no step-up in the basis for the trust assets. Second, the trust will be covered by the grantor spouse's transfer tax exemption rather than the former spouse's exemption. However, with the limited number of states with a death tax and the high federal transfer tax exemption, this issue will not be a pertinent part of most clients' decisions.

Reversionary Trust. The grantor of the trust may want to assets of the trust to revert to the grantor upon certain prescribed events (e.g., death or remarriage of the former spouse), particularly if there are no children from the marriage who could be named as remaindermen. If the trust provides that it reverts to the settler at its termination (i.e., the end of support obligations), then the trust will normally be includable in the settler's estate.[197] However, assuming the trust is satisfying deductible divorce obligation, there may be an offsetting estate deduction. With the larger federal transfer exemptions creating fewer taxable estates, reversionary trusts may become more acceptable from an estate tax perspective.

Trap: The transfer of assets to a trust for the benefit of an ex-spouse (as opposed to a direct transfer to an ex-spouse) can create taxable income to the transferor. For example:

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193 I.R.C. §2523(f)(2) (2015).

194 Treas. Reg. §2523(f)-1(c), 25.2523(e)-1(f) (2015).

195 PLR 200408015

196 For a more detailed discussion of this topic, see: Barry Nelson & Richard Franklin, I*nter Vivos QTIP Trusts Could Have Unanticipated Income Tax Results to Donor Post-Divorce*, LISI Estate Planning Newsletter #2244, (September 15, 2014).

197 See: I.R.C. § 2036 (2015).

- A transfer of an asset having a liability in excess of basis can create a current taxable income to the transferor.[198]
- A direct transfer of an installment sale note to a spouse or ex-spouse as a result of a divorce as not a taxable disposition.[199] However, if the transfer is in a trust for the spouse or former spouse, the disposition is taxable to the transferor.

Charitable Remainder Trust. One creative solution in divorce negotiations is to have the wealthier spouse create a charitable remainder trust ("CRT") that names the soon to be ex-spouse as lifetime beneficiary. The grantor of the trust obtains a current income tax deduction equal to not less than ten percent of the value of the contributed assets. The sale of an appreciated asset contributed to the trust would not create current taxable income to the trust or grantor. The grantor could retain a lifetime income interest from the trust after the death of the ex-spouse. Finally, the grantor spouse could retain the right to change the charitable remainderman during his life. The charities could include a Donor Advisor account with the grantor as decision maker or a private foundation created by the grantor.

The ex-spouse receives an income stream for life in lieu of direct ownership of assets. But for a financially challenged spouse, this might be a good choice for at least part of the benefits they receive as a result of the divorce.

Divorce and Charitable Remainder Trusts. Many married clients have created CRTs that have a lifetime payouts for the lives of the two spouses. Can the CRT be divided if they get divorced?[200] The IRS has approved such divisions.[201]

> ***Opportunity***: In lieu of a division of an existing CRT, the clients might provide that one of them renounces all of their rights to the CRT as a part of the negotiated divorce terms. This renunciation might create a charitable deduction to the disclaiming party because the present value of what the charity will receive may have increased.

Retirement Plans. In managing the divorce negotiations, advisors and clients should understand the differences in the tax treatment of various retirement plans. For example, if a distributions are made pursuant to a qualified domestic relations order (QDRO) from a qualified retirement plan to an alternative payee before the plan participant reaches age 59½, then the funds can be withdrawn, without having to pay

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198 See: I.R.C. § 1041(e) (2015). See the discussion in this article on liability in excess of basis.

199 I.R.C. § 453B(g) (2015). The Code section has a parenthetical exception to the exclusion from taxability that provides "*other than a transfer in trust*."

200 For a more detailed analysis of this issue, see Dewan, *PLR 200824022 and Rev. Rul. 2008-41 – CRTs Can Be Divided At Divorce Without Self-Dealing or Termination Tax Risk*, LISI Charitable Planning Newsletter # 134 (Jul. 14, 2008).

201 I.R.S. P.L.R. 200824022 (Jun. 13, 2008); Rev. Rul. 2008-41, 2008-2 C.B. 170.

an early withdrawal penalty of 10% of the withdrawal.[202] A similar exception does not apply to IRAs.[203]

> ***Trap***: In Hartley v. Commissioner,[204] the Tax Court ruled that when a family court required the plan participant to withdrawal funds from his ERISA retirement plan to pay for alimony, the 10% early withdrawal penalty applied because the payment was made to the plan participant not an alternative payee as required by I.R.C. § 72(t)(2)(C) and a QDRO was never prepared.
>
> ***Opportunity:*** Assume a husband is a participant in a defined benefit plan. Based upon his health and family history, the husband believes he will live longer than the mortality tables indicate. By retaining all of the defined benefit account and giving other assets to his wife, the husband might retain a greater financial benefit then actuarially calculated by the plan administrator.
>
> ***Opportunity***: If a retirement plan distributes employer securities, the value of the employer stock which is distributed may be taxed at the plan's basis in the stock rather than its current fair market value.[205] If the holding periods are met,[206] the subsequent sale of the stock receives capital gain benefit. If a retirement plan holds appreciated employer stock, the after-tax benefit of receiving employer stock from the plan should be part of the decision process on deciding which assets each spouse will receive.

ERISA generally provides that the retirement benefit of a qualified retirement plan cannot be assigned. [207] The statute provides an exception for assignments incident to a divorce.[208] In order to pass a portion of an ERISA retirement benefit to an ex-spouse, the divorce decree must satisfy the requirements of I.R.C. § 414(p).

> ***Trap***: In Hendon v. E.I. Dupont Nemours & Co.,[209] the Sixth Circuit Court of Appeals ruled that even when a divorce decree and martial dissolution agreement provided that a divorced spouse waived rights to a ERISA retirement plan, the ex-spouse was still entitled to the qualified plan assets upon the death of the plan participant. The Court ruled that the waiver was not in compliance with the requirements of ERISA.

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202 I.R.C. § 72(t)(2)(C) (2015); I.R.S. Notice 87-13, 1987-1 C.B. 432.

203 I.R.C. § 72(t)(3)(A) (2015).

204 104 T.C.M. (CCH) 553 (2012).

205 I.R.C. § 402(e)(4)(A) (2015) and I.R.S. Notice 98-24, 1998-17 I.R.B. 5.

206 See I.R.S. Notice 98-24, 1998-17 I.R.B. 5 for the rules governing applicable holding periods.

207 I.R.C. §401(a)(13) (2015).

208 The Pension Benefit Guaranty Corporation has issued a helpful booklet on divorce and Qualified Domestic Relations Orders. The booklet includes sample forms and a checklist. Copies can be found at www.pbgc.gov/publications/

209 No. 96-6233, 1998 WL 199824 (6th Cir. Apr. 13, 1998).

I.R.C. § 457 deferred compensation plans for governmental and non-profit employees are also subject to the qualified domestic relation orders.[210] Federal law does not require a qualified domestic relations order for a divorced-based IRA transfer.[211]

Creditor Issues. Financial problems are often a root cause of divorce. As a result there may be numerous creditor related issues in the divorce process.

> ***Caution***: If property transfers as a consequence of the divorce were deemed to be made in order to hinder, delay or defraud creditors, then the transfer could be rescinded as a "fraudulent transfer."

> ***Opportunity***: If there is the possibility of bankruptcy for an ex-spouse, then the non-bankrupting spouse is well advised to obtain the advice of bankruptcy counsel before the settlement is finalized. While a property settlement may be deemed a preference or fraudulent transfer, it is less likely that a support obligation to a spouse and children would be overturned. Moreover, payments for alimony, maintenance and support are not dischargeable in bankruptcy.[212] Therefore, one method of protecting a divorcing spouse of a financially distressed party may be to treat the payment as alimony and support—albeit at a potential tax cost to the recipient ex-spouse.[213]

> ***Trap***: Many clients mistakenly believe that because the divorce decree or settlement requires one spouse to pay marital debts, creditors cannot seek recovery from the other spouse. Because the creditor is not a party to the contest, it is normally not restricted in its rights. For example, assume a couple had co-signed a line of credit note, and the divorce decree assigned the liability to the husband. If the husband declares bankruptcy after the divorce, the ex-wife might still be responsible for the debt.[214]

> ***Opportunity***: ERISA Plans are exempt from the claims of most creditors.[215] Original IRA owners[216] have a federal bankruptcy exemption of up to $1.0 million, plus the full value of IRAs which received rollovers of ERISA plans.[217] A number of states[218] also provide creditor protection for IRAs. As a

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210 See I.R.C. § 414(p) (2015).

211 26 USCA § 408(d)(6) (2015).

212 *See* 11 U.S.C. § 523(a)(5), 727, 1141(d)(2), 1228(c)(2), 1328(a)(2) (2012).

213 i.e., the recipient of the alimony is taxable. I.R.C. §§ 61(a)(8), 71(a) (2015).

214 For more information on this issue see: Kathryn Henkel, ESTATE PLANNING AND WEALTH PRESERVATION: STRATEGIES AND SOLUTIONS § 53.17 (1994).

215 29 U.S.C. § 1056(d)(1); 26 U.S.C. § 403(b); Patterson v. Shumate, 504 US 753 (1992).

216 Inherited IRAs do not have similar protections. See the later discussion of US Supreme Court decision of Clark v. Rameker.

217 11 U.S.C. § 522(n).

result, divorcing clients in financial difficulty should consider do their best to retain their own retirement assets upon a divorce and try to obtain rights to their spouse's retirement assets.

Life Insurance. As a part of divorce settlements divorce decrees may require that one or both spouses maintain life insurance on the spouse's life for the benefit of an ex-spouse and/or children.

If the insured former spouse wants to deduct the insurance premiums as alimony, the insured should consider having the ex-spouse be both owner and irrevocable beneficiary of the policy.[219] However, many divorced clients have a rather adverse reaction to an ex-spouse benefiting from their death.

> ***Trap***: If the policy has a significant cash value and the couple is no longer married when the transfer to the ex-spouse is made, the transfer may be taxable gift for gift tax purposes.[220] Moreover, if the insured dies within three years, the death benefit could be pulled back into the insured's estate.[221]

> ***Trap***: In Smoot v. Smoot, life insurance proceeds paid to a former wife from a policy owned by the decedent were taxable in the estate.[222] As a result the former wife was required to contribute to the estate taxes due on the taxable estate.[223] The case illustrates two problems with divorce related life insurance First, the ex-spouse will not be happy about the diminution of any insurance proceeds by the applicable state or federal estate taxes. Second, because the insurance death payment is made directly to the former spouse, the executor of the estate may have a hard time getting funds out of the former spouse to cover their portion of the estate taxes.

> ***Drafting***: Divorce agreements should clearly state that the former spouse is responsible for any applicable portion of any state or federal estate taxes on the insurance proceeds. Moreover, the insured's Will should specifically provide that the insurance recipient is required to pay any applicable taxes in order to avoid having the taxes reduce the residuary estate.

> ***Opportunity***: If the former spouse is owner of the policy, the ex-spouse will direct the ultimate disposition of the death proceeds. Instead, the insured could

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218 See for example: 11 U.S.C. § 541(c)(2) (2012); GA. CODE ANN. § 18-4-22 (2015); *see also* Meehan v. Wallace, 102 F.3d 1209 (11th Cir. 1997) (applying the Georgia law).; See the IRA State Exemption Chart at http://moranknobel.com/retirement.htm

219 *See* Rev. Rul. 70-218, 1970-1 C.B. 19.

220 Although the large federal gift exemption would practically render this issue moot for most clients.

221 I.R.C. § 2035 (2015).

222 *Smoot v. Smoot*, No. 2:13-cv-00040 (S.D. Ga. Mar. 31, 2015)

223 *See* I.R.C. § 2206 (2015).

place a policy in an irrevocable life insurance trust (an "ILIT") and give the ex-spouse a beneficial interest until the spouse has died, married or co-habitated, at which time the benefits of the trust could pass free of transfer taxes[224] to other heirs (e.g., the children from the first marriage). If the policy is owned by an ILIT, the insured will lose the alimony deduction for the payment of insurance premiums, but as the creator of the trust, the insured can also direct the ultimate disposition of the death proceeds. If the ILIT is properly created, the policy is also excluded from the insured's taxable estate.

Trap: If the divorce decree provides that the insurance policy will revert to the insured upon the satisfaction of the divorce obligations it was designed to fund, then this reversionary interest[225] may result in the husband having to include the policy in his taxable estate, even when the spouse is the irrevocable beneficiary.[226] However, the decedent's estate may qualify for an estate tax deduction for the amount of the proceeds.[227] In many cases it will be better to have the settlement agreement provide for transfer of the policy into a trust for the benefit of any joint descendants.

Trap: Assume a former spouse obtained a policy on the former spouse. Does the insured ex-spouse have an obligation to cooperate with the former spouse to retain the policy? In a Kansas Supreme Court decision,[228] the court ruled that a husband had no obligation to help the ex-spouse maintain a life insurance on his life. The case largely turned on Kansas Statutes Annotated § 40-453(a), which provides that an insurable interest ceases when an insured requests the insurer to terminate or non-renew the policy applicable to such person's life. The Court noted: "*we hold a court order requiring a child support obligor to cooperate with a child support obligee's efforts to obtain insurance on the life of an obligor is against public policy, as expressed by the Kansas Legislature in K.S.A. 40-453(a). . . .*"

Drafting: In drafting the divorce settlement agreement, specifically provide that any ex-spouse who is insured by the other spouse must cooperate in maintaining the coverage. The responsibilities for paying for the insurance should also be spelled out.

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224 On transfers of an existing life insurance policy to the ILIT, the insured/owner must survive the transfer by three years for the policy to be outside the insured/owner's taxable estate.

225 I.R.C. § 2042(2) (2015).

226 Rev. Rul. 76-113, 1976-1 C.B. 276; Estate of Kahanic v. Comm'r, 103 T.C.M. (CCH) 1434 (2012); Louis A. Mezzullo, *Using Life Insurance to Satisfy Support Obligations in a Divorce*, 38 EST., GIFTS & TR. J. 329 (November 2013).

227 Rev. Rul. 76-113. 1976-1 C.B. 276; *see also* I.R.C. § 2053(a)(4) (2015).

228 *In re* Marriage of Hall, 286 P.3d 210 (Kan. 2012); *see also* Howard M. Zaritsky, Marriage of Hall*: Ex-Husband Cannot Be Made to Cooperate with Ex-Wife's Attempt to Maintain Life Insurance Policy on His Life*, EST. PLAN. NEWS. (LISI), no. 2012, Oct. 15, 2012.

Revocation of Rights in Existing Trusts. Many clients have created existing irrevocable trusts (e.g., an ILIT) in which a soon to be ex-spouse is a Trustee, beneficiary and/or holder of rights over the trust (e.g., a limited power of appointment).

> ***Drafting***: The settlement agreement or the irrevocable trust terms should provide that the former spouse irrevocably renounces all of the spouse's rights, powers and other benefits in any existing trusts upon divorce or legal separation.

Gifting and Divorce. The couple's transfer tax exemptions and annual exclusions should be viewed as a tradable asset. Remember when net operating losses used to be sold? Advisors should look at the available transfer tax benefits of each spouse in the same light when a divorce occurs. The unused transfer tax exemption of a less wealthy spouse can be a valuable asset to the wealthier spouse.

> ***Opportunity***: A husband wants to begin transferring equity in his family business to children from a prior marriage. He has a prenuptial agreement that restricts the rights of the current spouse. The appraiser has provided a discount in value of 40% for the minority interest he will transfer in the business. If the spouses elect gift-splitting, the donor spouse can effectively transfer his and his spouse's unified credit amount (with an applicable valuation adjustment of 40%) to a generation-skipping trust and could save up to $3,620,000 in estate taxes.[229] In effect agreeing to the utilization of the poorer spouse's exemption without any actual transfer by that spouse. There are multiple ways to make the trade-off including:
>
> - The wealthier spouse could modify his Will to provide a more generous trust for the benefit of the soon-to-be former wife, or
> - The wealthier spouse could create an ILIT or non-insurance trust with other assets that provides a life interest to the ex-spouse, but which passes the trust assets to the wealthier spouse's family at the ex-spouse's death (or other triggering event such as a remarriage), or
> - The wealthier spouse might provide a larger property settlement to a soon-to-be ex-wife. "*In return for saving me $3.6 million in transfer taxes, I will agree to increase the property settlement by $2.0 million.*"
>
> ***Opportunity***: Both spouses have been married before and both are wealthy. One spouse has 10 potential donees, and the other has 20 potential donees. Each of them can double the non-taxable annual exclusion of the other, without any adverse impact to either spouse's estate planning, while saving both families significant estate taxes.

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229 i.e., $5,430,000 (spouse's 2015 gift exemption), discounted at 40% ($9,050,000 in transferred value), multiplied by the top estate tax rate of 40%.

__Drafting__: Make sure there is a document in which each spouse agrees to sign a gift tax return for the year in which they consent to gift-splitting.

__Opportunity__: In an amicable divorce, clients should also review the possibility of using their transfer tax exemptions more effectively. For example, assume a husband and wife could each create Bypass/Exemption trusts naming the other as beneficiary. These irrevocable trusts could grow tax-free and protect the ex-spouse/beneficiary from creditor claims. Clients should make sure that the terms of the trusts do not "mirror" each other to avoid the reciprocal trust doctrine.[230] If the doctrine applies, both trusts will be ignored for transfer tax purposes.

Tuition Payments. A settlement agreement may require that the wealthier spouse fund the college education of family members of the less wealthy spouse. Clients should be careful to make the payments in a manner which does not produce a taxable gift. For example:

- Instead of reimbursing an ex-spouse for the cost of a descendant's tuition, the payment could be made directly to the institution, using the gift tax exclusion.[231] Other education related payments to the descendant could be covered by the $14,000 annual exclusion.
- As a part a divorce decree, the couple might also consider the pre-funding of college costs for descendants (especially younger descendants) using Section 529 Plans. Section 529 permits donors to pre-pay up to five years of annual exclusion gifts to fund a Section 529 plan.[232]
- The IRS has agreed that a grandmother's advance payment of her grandchildren's tuition at a private secondary school were excluded from her gift tax pursuant to I.R.C. § 2503(e).[233] However, the advance tuition payment cannot be refunded if the beneficiary fails to attend the school. This ruling offers an opportunity for wealthy divorcing spouses to potentially pre-fund a family member's education and reduce their respective estates.

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230 *See* Cheryl L. Hader, *Planning to Avoid the Reciprocal Trust Doctrine*, 26 EST.PLAN. 358 (Oct. 1999); Paul E. Van Horn, *Reciprocal Trusts Revisited*, 19 PRAC. TAX LAW. 39 (Summer 2005).

231 I.R.C. § 2503(e) (2015).

232 I.R.C. § 529(c)(2)(B) (2015).

233 *See* I.R.S. Priv. Ltr. Rul. 9941013 (July 9, 1999); *see also* I.R.S. Priv. Ltr. Rul. 0602002 (Jan. 13, 2006).

Alimony, Child Support, Property Transfers & Unexpected Tax Issues

Albert Einstein's Nobel Prize money went to his ex-wife as part of his divorce settlement.[234]

Alimony. Properly structured, alimony payments are considered gross income to the recipient[235] and are deductible to the payor.[236] In order for a payment to qualify as alimony, all of the following must occur:[237]

- The payment must be made in cash.
- The payment must be made pursuant to a divorce or written separation agreement.[238] Payments made to a spouse before a divorce or separation agreement is signed may not qualify as alimony payments.[239]
- Payments made on behalf of the recipient spouse to a third party must be evidenced by a timely executed document.
- The payor's obligation to make the payment terminates at the recipient's death. I.R.C. §71(b)(1)(D) provides that 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 treated as deductible alimony.[240]
- If divorced or legally separated, the couple must live in separate households,
- The couple do not file a joint return (i.e., if they are legally separated).
- The divorce or separation agreement does not provide that the payments are not considered alimony.

Drafting: While the alimony rules seem fairly straightforward, this is one area where drafting documents without proper tax advice can have unfortunate consequences. For example, in Croteau v. Commissioner,[241] a taxpayer drafted his own settlement agreement using someone else's agreement as a format. Because of improper language, the Tax Court ruled that $34,000 in "alimony" payments were instead a non-deductible property settlement. Not only did the husband lose a $34,000 annual deduction, the Court also permitted an accuracy-related penalty to be assessed.

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234 *Mileva Einstein-Maric*, BIOGRAPHY, http://www.biography.com/people/mileva-einstein-maric-282676 (last visited June 5, 2015).

235 I.R.C. §§ 61(a)(8), 71(a) (2015).

236 I.R.C. § 215(a) (2015).

237 I.R.C. § 71(b) (2015).

238 *See* Milborn v. Comm'r, 109 T.C.M. (CCH) 1056 (2015) (discussing the definition of a "written separation agreement").

239 *Id.*

240 Okerson v. Comm'r, 123 T.C. 258 (2004).

241 75 T.C.M. (CCH) 1550 (1998); *see How Not to Get an Alimony Deduction - Draft Your Own Settlement Agreement*, 88 J. TAX'N 184 (Mar. 1998).

Trap: If the alimony payments are reduced or terminated during the first three calendar years after the first payment of alimony or separate maintenance fees, the paying spouse may be required to recapture some of the previously obtained alimony deductions.[242] The IRS provides a worksheet for computing the amount of the recaptured deduction.[243]

Trap: The Tax Court has ruled[244] that the termination of alimony upon "*the graduation from high school of the youngest child*" resulted in the denial of an alimony deduction. The Tax Court ruled that I.R.C. § 71(c)(2) provides that the amount of any payment that is subject to "contingencies involving child" must be considered payment made for the support of the child. The Code specifically lists "child leaving school" as an example of such a contingency.

Trap: The Tax Court has ruled[245] that when a divorced parent cannot pay alimony and child support, the payments will first be applied to child support, effectively reducing the tax deduction for the spouse making the payment.

Trap: Normally workers compensation claims are excluded from income.[246]The IRS recently issued a private letter ruling[247] which indicates that payments of a former spouse's workers compensation to an ex-spouse pursuant to a qualified domestic relations order was not excluded from income. Effectively, the payment to the ex-spouse converted the payments from non-taxable to taxable.

Normally, the payor ex-spouse does not have to withhold taxes on the alimony payments. It is the responsibility of the recipient ex-spouse to make sure sufficient taxes have been withheld or estimated taxes have been paid. If the recipient ex-spouse is a nonresident alien, a withholding tax may be imposed on the alimony payments.[248] However, review any tax treaty between the U.S. and the recipient's country of residence because it may override the requirements for withholding.

Alimony which remains uncollected at the recipient's death is considered income in respect of a decedent[249] and can result in the imposition of both state and federal estate and income taxes.

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242 I.R.C. § 71(f) (2015).

243 *See* U.S. DEP'T OF TREASURY, INTERNAL REVENUE SERV., PUBLICATION 504, DIVORCED OR SEPARATE INDIVIDUALS, Worksheet 1 (2014).

244 Johnson v. Comm'r, 107 T.C.M. (CCH) 1358 (2014).

245 Becker v. Comm'r, T.C. Summ. Op. 2015-2.

246 I.R.C. § 104(a)(1) (2015).

247 PLR 201521009.

248 I.R.C. § 1441(a) (2015).

249 I.R.C. § 691 (2015); *See* Kitch v. Comm'r, 103 F.3d 104 (10th Cir. 1996).

Caution: Taxpayers should expect a greater IRS focus on proper reporting of alimony payments. On March 31, 2014, the Treasury Inspector General for Tax Administration issued a report entitled "*Significant Discrepancies Exist Between Alimony Deductions Claimed by Payers and Income Reported by Recipients*."[250] The 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.

Child Support. Payments designated as child support are not deducible by the payor and do not constitute taxable income to the recipient parent.[251] A payment is deemed for child support if any one of the following occurs:

- The divorce agreement designates it as child support,
- The payment reduces at times tied to a child's pivotal birthdays (e.g., age 18),
- The payment reduces when an event occurs to the child (e.g., marriage), or
- The payment reduces at a time clearly associated with a child related event.

A related issue to child support is deciding which parent receives the dependency exemption for the child. See the prior discussion.

Property Transfers. Most property transfers that are "incident to divorce" are not taxable to either spouse.[252] However, there are some situations in which the I.R.C. imposes income taxes, including:

- If a property settlement is made with a non-resident alien, Section 1041 does not apply, and the transfer may be a taxable event.[253]
- A direct transfer of property to a divorcing spouse is not taxable even when the liabilities secured by the property exceed the transferor's basis in the property. However, if the transfer of the same property is made to a trust for the benefit of the divorcing spouse, the difference between the secured liability and the transferor's basis in the property may be taxable to the transferor.[254]See the discussion in the next section.
- Accrued interest on Series E and EE US Savings Bonds must be recognized by the transferor of the bonds, even when the transfer is a part of the divorce.[255]
- Many divorcing spouses make settlement payments over a number of years. Any interest on an installment obligation will be taxable to the recipient spouse.[256]

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250 Copy available at: http://www.treasury.gov/tigta/auditreports/2014reports/201440022fr.html

251 I.R.C. §§ 71(c), 215(b) (2015).

252 I.R.C. §1041 (2015).

253 I.R.C. §1041(d) (2015).

254 I.R.C. §1041(a),(e) (2015).

255 Rev. Rul. 87-112, 1987-2 C.B. 207.

256 *See* Gibbs v. Comm'r, 73 T.C.M. (CCH) 2669 (1997); Seymour v. Comm'r, 109 T.C. 279 (1997).

Opportunity: The IRS has ruled that the transfer of non-qualified stock options and deferred compensation to a spouse incidental to a divorce did not result in any taxable income to the employed spouse who made the transfer.[257] In addition, the transferee spouse was taxable on the options and deferred compensation only when the spouse received the benefits.

257 Rev. Rul. 2002-22, 2002-19 I.R.B. 849 (May 8, 2002).

Income Taxes, Tax Basis, Marriage and Divorce

Ronald Reagan is the only person to be elected as US President after having had a divorce

Carry-Over Basis in Divorce. Pursuant to I.R.C. §1041 if property is transferred to a spouse or an ex-spouse as a consequence of a divorce, the transfer does not generally create taxable income and the recipient spouse gets the full carry-over basis of the transferor. Unlike gratuitous transfers to non-spouses, the recipient's tax basis is not impacted if the tax basis is higher than the fair market value of the transferred asset.[258]

> ***Trap***: Obtaining a carryover in basis is not always a good thing. For example, in Godlewski v. Commissioner,[259] a husband transferred cash to his wife in return for her transferring their residence to him. When the husband sold the house, he treated his cash payment to the wife as additional tax basis in the residence. The Tax Court ruled that there was no basis adjustment.

Liability in Excess of Basis. In general, a pre-death transfer of property secured by a debt that exceeds the tax basis creates a taxable event to the transferor. I.R.C. section 1041(e) provides an exception to this rule and a potential trap to the ex-spouse that receives the property. If property is transferred directly (but not in trust) to a spouse or ex-spouse and the property has a liability in excess of its basis, no recognition occurs on the transfer and the recipient spouse takes the transferor spouse's basis.[260] But, if the recipient spouse later transfers the asset, the amount by which the secured debt exceeds the tax basis can be taxable to the recipient spouse.

> ***Example*****:** Assume a divorcing wife owns a tract of land that has a fair market value of $2.1 million, a basis of $200,000 and secured debt of $1.5 million. The husband receives the property as a part of the divorce and immediately sells it, thinking that he gets to keep the $600,000 in equity. When his CPA asks him about the tax basis in the transaction, the husband responds with "*what's tax basis?*" The recognized gain is $1.9 million. Assuming a state and federal effective income tax rate of 30%, the taxes on the sale are $570,000, leaving the client with $30,000 after payment of the mortgage. Instead of getting $600,000, the husband nets $30,000 before payment of commissions. Assuming a 6% sales commission, the husband would actually be out of pocket for the sale (e.g., the 6% sales commission would be $126,000, netting a total loss of $96,000).

> ***Opportunity***: But assume the above client's husband was terminally ill and they are not getting divorced. The client gifts the property directly to the husband, who

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258 I.R.C. § 1015 (2015).

259 90 TC 200 (1988).

260 For a more detailed analysis of this issue, see BORIS BITTKER & LAWRENCE LOKKEN, FEDERAL TAXATION OF INCOME, ESTATES AND GIFTS, ¶ 44.6 (2015); I.R.S. P.L.R. 9615026 (Apr. 12, 1996); I.R.S. P.L.R. 8644012 (Jul. 31, 1986); Treas. Reg. § 1.041-1T(d) Q&A 12 (2015).

specifically passes the real property to a trust for the benefit of the couple's children. Not giving any beneficial interest in the trust to the donor/wife avoids any possible application of section 1014(e).[261] The gift to the husband does not create a taxable event to the wife, even though the liability on the asset exceeded its basis. When the husband passes away, the tax basis increases to $2.1 million. Assume the property is immediately sold. The trust should have no recognized gain from the sale, netting an after-tax profit of $600,000 (less mortgage payoff, closing costs and commissions).

Tax Carry-forwards. The unused tax loss carry-forwards of a decedent are not carried over to the estate or to heirs.[262] Instead, they simply vanish. There are at least three ways that expiring losses could be used. First, the client (or persons holding a general power of attorney) could take actions to use any expiring losses (e.g., accelerating taxable income to offset a net operating loss ("NOL")). Second, a spouse who files a joint return for the year in which the decedent spouse dies might take pre-mortem actions to create personal taxable income to offset the soon-to-expire losses. Third, a surviving spouse can take post-mortem steps to increase surviving spouse's taxable income that is reflected on the final joint tax return.[263]

Example: Assume the deceased Husband left a $400,000 NOL from his failing business. In the year of the Husband's death, the Wife could convert $400,000 of her IRA to a Roth IRA to take advantage of the expiring NOL.

Caution: To determine the actual tax benefits, always do the math before implementing the strategy.

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261 John J. Scroggin, *Understanding Section 1014(e) and Tax Basis Planning,* EST. PLAN. NEWSLETTER (LISI), no. 2191, Feb. 6, 2014; HOWARD M. ZARITSKY, TAX PLANNING FOR FAMILY WEALTH TRANSFERS ¶ 8.07[5] (5th ed. 2015); Mark R. Siegel, *IRC Section 1014(e) and Gifted Property Reconveyed in Trust,* 27 AKRON TAX J. 33 (2012).

262 See Rev. Rul. 74-175, 1974-1 CB 52.

263 I.R.C. § 6013(a) (2015).

Transfer Taxes

In Ancient Rome, Augustus (63 B.C.–A.D. 14) passed laws compelling people to marry and penalized those who remained single[264]

A number of unique gift, estate and generation-skipping tax issues surround marriage, divorce and legal separation. Some of these issues include:

Spouse not a U.S. Citizen. If the donee is not a U.S. citizen, a gift tax marital deduction is not allowed. Moreover, gifts cannot be made to a Qualified Domestic Trust as allowed for estates. Instead, the annual exclusion for gifts to non-U.S. citizen spouses is increased to $100,000.[265] The exclusion amount number is inflation-adjusted and has increased to $147,000, effective for 2015.[266]

> ***Opportunity***: Where a client is married to a non-US citizen, the transfer of $147,000+ each year to the spouse may provide significant tax savings. However, if the spouse is a U.S. resident, then the assets may still be taxable when the spouse dies. Moreover, the spouse's home country may also impose a death tax on the assets at the spouse's death.

Property Transfers and Gift Taxes. Property settlements must be reviewed in light of the possible imposition of a gift tax. I.R.C. § 2523 provides for an unlimited marital deduction for transfers between spouses. However, transfers after divorce do not fall into the section 2523 exception because the marital deduction is only available if the gift "*is to a donee who at the time of the gift is the donor's spouse.*"[267]

I.R.C. § 2516 provides some gift tax protection for property settlements consummated after a divorce is finalized. Transfers for the settlement of property rights or for child support are exempt from gift tax if:

- The parties enter into a written agreement. The agreement does not need to be approved by any court.
- The transfers are payments of cash or property in settlement of spousal martial rights and a "reasonable allowance" of support rights of an "issue of the marriage" who are minors.[268] Transfers for other purposes (e.g., requiring a spouse to fund education costs of a stepson[269]) are not excluded from gift tax

264 Mary R. Lefkowitz & Maureen B. Fant, *Women's Life in Greece & Rome: Legal Status in the Roman World*, THE STOA CONSORTIUM, http://www.stoa.org/diotima/anthology/wlgr/wlgr-romanlegal120.shtml (last visited June 1, 2015).

265 I.R.C. § 2523(i) (2015).

266 Rev. Proc. 2014-61, 2014-47 I.R.B. 860.

267 I.R.C. § 2523(a) (2015). See also: Treas. Reg. § 25.2523(a)-1(a) (2015).

268 Thus, support payments for children who have reached majority (e.g., while in college) are not protected by I.R.C. § 2516.

269 However, it is not clear whether payments for tuition costs for a stepchild might be treated as non-taxable gifts under I.R.C. § 2503(e). The placement of such language in a settlement agreement might mean that the payment was not a gift, but rather was consideration for the release of marital

computations pursuant to I.R.C. § 2516.

- The agreement must be entered into within a period that begins two years before the divorce and ends one year after the divorce. The IRS may require the modifications of the agreement also occur within these time frames.[270] Note that a marital agreement which was entered into more than two years before the divorce would not qualify as the required agreement. In addition, if one of the parties voluntarily increases the benefits to an ex-spouse after the period has run, I.R.C. § 2516 does not apply and the change may be treated as a taxable gift.

Drafting: I.R.C. § 2516 does not require that the divorce decree mention the settlement agreement. The parties can enter into it independently of the decree, allowing clients to keep their property settlements out of the public records.

Caution: The regulations require the filing of a gift tax return for gifts made pursuant to I.R.C. § 2516. The regulations[271] provide: "*In any case where a husband and wife enter into a written agreement of the type contemplated by section 2516 and the final decree of divorce is not granted on or before the due date for the filing of a gift tax return for the calendar year ….. in which the agreement became effective…, then, except to the extent Section 25.6019-1 provides otherwise, the transfer must be disclosed by the transferor upon a gift tax return filed for the calendar year (or calendar quarter) in which the agreement becomes effective, and a copy of the agreement must be attached to the return. In addition, a certified copy of the final divorce decree shall be furnished the internal revenue officer with whom the return was filed not later than 60 days after the divorce is granted.*"

There are numerous situations in which the client cannot qualify for the protection of I.R.C. § 2516. However, courts have developed a series of exceptions to the imposition of a gift tax on transfers made after the marriage has dissolved. For example, in Harris v. Commissioner,[272] the U.S. Supreme Court ruled that divorce related transfers which were founded upon a court decree were involuntary and therefore do not constitute voluntary taxable transfers. Treasury Regulations also provide that any obligation imposed by law is a deductible debt of the estate.[273]

Drafting: Planners need to ensure that the property transfer provisions of the divorce decree are specifically incorporated into the divorce court's ruling. If the decree merely declares the marriage terminated, but does not approve the property transfer, then the IRS could argue that Harris is not applicable.

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rights.

270 *See* Rev. Rul. 79-118, 1979-1 CB 315.
271 Treas. Reg. § 25.6019-3(b) (2015).(emphasis added)
272 340 U.S. 106 (1950),
273 *See* Treas. Reg. § 20.2053-4 (2015).

Modifications of the original settlement agreement should also be approved by the court.

Property Transfers and Estate Taxes. Divorce attorneys are often not particularly good at examining the estate tax implications of the divorce decrees. I.R.C. § 2056 provides for an unlimited marital deduction for death transfers to a spouse, but does not provide any marital deduction for transfers to an ex-spouse. It is important to make sure the divorce documents create an enforceable debt against the estate to create an estate tax deduction, rather than creating a taxable transfer.

I.R.C. § 2053(a)(3) provides for the deduction of the decedent's personal obligations to the extent incurred for adequate consideration. If the decedent's obligations are founded upon a court decree, then Harris would apply and the post-death obligations would be deductible. However, if the court did not have the power to require the property transfers (e.g., transfers to fund a step-child's education), then Harris will not apply and the post-death transfers may not be deductible for estate tax purposes.

Gift-Splitting. The law permits a spouse to elect to be treated as the donor of a gift, even when the other spouse is the sole transferor.[274] In order for the "gift-splitting" to apply, the donor must file a gift tax return, on which the spouse consents to the treatment of the gifts as made one-half by the spouse.[275] Gift-splitting for any year applies to all gifts and cannot be made on a gift-by-gift basis - except if a divorce occurs in the year of the gift-split, post-divorce gifts would not be gift-split. If neither spouse has filed a gift tax return for the applicable year, the gift-splitting consent may be filed late, generally without any adverse tax impact.[276] If a married couple agrees to "gift-splitting," each is treated as though they made the gift for generation-skipping tax purposes also.[277] The couple must be married on the date the gift is made if they intend to elect gift-splitting and neither can marry someone else before the end of the year.[278]

Trap: If gift-splitting is elected, the spouses have joint and several liability for any gift tax which may be due.[279] Because of this rule, consenting spouses should be very careful to assure that the value of the gifts are accurate. The consenting spouse may also want to obtain an indemnity from the gifting spouse.

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274 I.R.C. § 2513 (2015).

275 Treas. Reg. § 25-2513-2(a) (2015). The return must be filed by the donor spouse, even if a gift tax return was not otherwise required (e.g., only annual exclusion gifts were made).

276 I.R.C. § 2513(b) (2015); Rev. Rul. 80-224, 1980-2 CB 281.

277 I.R.C. § 2652(a)(2) (2015).

278 I.R.C. § 2513(a)(1) (2015).

279 I.R.C. § 2513(d); Treas. Reg. § 25-2513-2(a) (2015).

Court Orders. Many states have laws permitting guardians, generally with court approval, to adopt an estate plan for an incapacitated resident.[280]

> ***Trap***: In Technical Advice Memo 9731003, the IRS ruled that court-ordered annual exclusion gifts to the family of an incapacitated taxpayer, the gifts would remain in the taxpayer's taxable estate. The IRS noted that under applicable state law the gifts could have been rescinded by the taxpayer if she recovered capacity (even though she had irreversible Alzheimer's).

280 For more detailed analysis of this issue, see Elizabeth G. Clark, *Substituted Judgment: Medical and Financial Decisions by Guardians*, 24 EST. PLAN. J. 66 (Feb. 1997).

Existing Estate Planning Documents and Marriage

As of 2012, Iowa and Illinois have the lowest divorce rates in the nation[281]

Prior Planning Documents. If marriage is anticipated, the client should discuss with an estate planning attorney the benefit of executing a new Will in contemplation of the marriage. The rights of the new spouse (see the prior the discussion) and the impact of the marriage on each spouse's existing estate planning (especially on how it impacts their respective heirs) should be considered as a part of the pre-marriage process. Leaving the decision to the inflexibility of statutory law is not advisable, particularly in second and third marriages.

How a marriage affects existing estate planning documents varies widely from state to state, with all sorts of exceptions and limitations. A few examples, may give a sense of the issues.

- In Oregon[282] marriage can revoke all previous Wills which were not drafted in contemplation of marriage. In Kansas, the Will is only revoked if a child is born of the marriage. [283]

  Trap: If the Will is revoked and there is no pre-nuptial agreement that waives such rights, the surviving spouse may have spousal elective share claims and intestate share claims against the estate.

- In Texas and Kentucky,[284] the marriage has no impact on the Will and if the Will does not mention the new spouse, they have no right of inheritance under the Will.

- Generally, in community property states, a spouse is entitled to half of the community property assets, but the other spouse has a right to convey their half of the community property assets and their separate assets as they see fit.

- In most states,[285] the Will is not revoked, but the new surviving spouse may be entitled to an intestate share of the decedent's estate (referred to as "pretermitted spouse statues"). Particularly in marriages in which there are children from a prior marriage, the pretermitted rights of the second or third spouse can create dispositions that neither spouse intended.

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281 CTR. FOR DISEASE CONTROL, NATIONAL VITAL STATISTICS SYSTEM, DIVORCE RATES BY STATE (2011), *available at* http://www.cdc.gov/nchs/data/dvs/divorce_rates_90_95_99-11.pdf.

282 ORE. REV. STAT. § 112.305 (2015), which provides that the existence of a pre-nuptial agreement can result in the Will not being revoked at marriage.

283 KAN. STAT. ANN. § 59-610 (2015) provides: "*If after making a will the testator marries and has a child, by birth or adoption, the will is thereby revoked.*" (emphasis added)

284 KRS 394.090. However, the spouse may still have a spousal elective share.

285 C.f.: Georgia: GA. CODE ANN. § 53-4-48(c) (2015); Massachusetts: MASS. GEN. LAWS §2-301 (2015); New York: NY EPT Law § 5-1.3 (2015).

Intestacy. If the couple does not have enforceable Wills at the time of the marriage, major conflicts among the family groups.

> ***Trap***: Assume a couple in their second marriage had no children and no Wills. Both are injured in a car accident. The wealthier wife dies at the scene and the husband dies the next morning. Under the intestacy laws of most states, the husband inherits 100% of the wealthier spouse's assets for the few hours of his remaining life. His family would then inherit his share and the wife's family would receive none of the intestate estate.

> ***Trap***: Even if the couple had a pre-nuptial, conflicts could easily arise in the above example. The only intestate heirs of the husband are his family who have a financial incentive (i.e., 100% of the wife's assets) to argue that the pre-nuptial agreement did not govern intestate rights which could not accrue until after the marriage.[286]

Waivers. Newly married clients should consider waiving any spousal rights that are created by the marriage (e.g., ERISA retirement rights, spousal elective share). Both spouses should be given "fair disclosure" and be represented by separate counsel. See the prior discussion.

Decision Makers. Client need to thoroughly evaluate whether to change the decision makers in their documents.

> ***Trap:*** Clients in second and third marriages (particularly those with adult children from prior relationships) need to be cautious of naming their adult children and/or new spouses as decision makers or co-decision makers. Such appointments are often a recipe for conflict, dead-locked decisions and litigation.

> ***Trap***: Some attorneys will recommend that a spouse can serve as sole Trustee of a trust, if distribution decisions are subject to an ascertainable standard. If there are children from a prior relationship, there is a strong probability that they will disagree with the step-parent's lifestyle expectations and resulting expenditures from the trust.

Medical Directives. Some states provide that upon marriage a Medical Directive is automatically revoked except with regard to the spouse. For example, Georgia law[287] provides: "*Unless an advance directive for health care expressly provides otherwise, if*

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286 A similar argument was used with ERISA retirement plan spousal benefits, because ERISA rights did not accrue until after the marriage and a future spouse cannot renounce a right he or she did not have at the time of the renunciation. See the discussion supra note 161.

287 GA. CODE ANN. § 31-32-6(b) (2015).

after executing an advance directive for health care, the declarant marries, such marriage shall revoke the designation of a person other than the declarant's spouse as the declarant's health care agent…"

Clients should discuss with their counsel whether new Medical Directives should be executed upon their marriage, particularly when there are adult children from a prior relationship.

General Powers of Attorney. Incapacity planning should be a major discussion for clients entering into a second or third marriage.

Drafting: Among the terms the clients should consider are:

- In some states, appointment of a guardian revokes or limits the agent holding the GPOA (e.g., Florida,[288] Texas,[289] Virginia,[290] and Washington[291]). To assure that a conflict does not develop between the power holder and a potential adverse guardian (e.g., a second spouse), provide in the document that the power holder is also intended to be the guardian over the client's property if one is ever appointed.
- Even if the state statute provides that the GPOA survives incapacity of the principal (i.e., it is "durable"), place survival language in the document so that there is no question of enforceability in those states which require durable language in GPOAs (i.e., the client moves to a new state).
- To assure that the death of the named power holder does not force the grantor's family into guardianship, name one or more successor power holders (e.g., do not have spouses as the sole power holders for each other).
- Particularly in second and third marriages, advisors should point out the inherent conflicts of appointing the spouse or children from former marriages as the Agent and/or named Guardian in their documents. Moreover, if such appointments are made, clients should consider how the rights granted under the documents may be limited (e.g., "*if I am incapacitated and my spouse is serving as my Agent, my spouse will not have the authority to change my state of domicile if such a change would create substantial new rights or benefits to my assets to the spouse, unless all of my children agree in writing with such a change of domicile*.")

Caution: A 2015 article in the New York Times[292] noted that it has become "routine" for nursing homes to attempt to gain guardianship over residents and to use that power

288 FLA. STAT. § 709.2109(1)(c) (2015).
289 TEX. CODE ANN. § 485 (2015).
290 VA. CODE ANN. § 64.2-1606 (2015).
291 WASH. REV. CODE § 11.94.010(1) (2015).
292 Nina Bernstein, *To Collect Debts, Nursing Homes Are Seizing Control over Patients*, N.Y. TIMES, Jan. 26, 2015, http://www.nytimes.com/2015/01/26/nyregion/to-collect-debts-nursing-home-seizing-control-over-patients.html.

to pay bills to the nursing home. Moreover, other family members may attempt to gain control of an incapacitated person if they disagree with the actions of the person holding the GPOA. Always name the agents listed in a General Power of Attorney as the document maker's Guardians to avoid this potential problem.

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Resources:

- Eric A. Manterfield, *Estate Planning for Couples Entering Second Marriages—Part 1*, 41 EST. PLAN. J. 3 (Dec. 2014) and *Part 2*, 42 EST. PLAN J. 23 (Jan. 2015).
- Joseph R. Pozzuolo, et al., *Remarriage Situations Can Raise Special Estate Planning Considerations*, 82 PRAC. TAX STRAT. 220 (APR. 2009).

Existing Estate Planning Documents and Divorce

According to Swedish researcher Yvonne Aberg, divorce is contagious. She found that as the proportion of divorced office workers increased, the chance of divorce by the remaining married office workers also increased. The more single people in the office, the greater the divorce rate.[293]

Revocation of Benefits Upon Divorce. In most states, a divorce automatically terminates the rights of an ex-spouse under a Will that preceded the divorce. For example, in Georgia, *"[a]ll provisions of a will made prior to a testator's final divorce or the annulment of the testator's marriage in which no provision is made in contemplation of such event shall take effect as if the former spouse had predeceased the testator . . ."* [294] Note that the Will is still valid, but the ex-spouse is deemed to have predeceased the testator.

> ***Trap***: There is a potential unintended consequence in states which adopt the above approach. Assume there are children of the marriage and the Will provides that the surviving spouse will serve as a Trustee or Co-Trustee for the children's beneficial interests upon the death of the testator. The couple gets divorced and then the husband dies. As a result of the above presumption, the former wife is treated as predeceased "*for all provisions of a will*," The wording would indicate that the former wife could not serve as a Trustee for the couple's children.
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> ***Trap***: In many states, the wife is considered to have predeceased the former spouse, but the relatives of the former spouse who are listed in the Will still have a right of inheritance. Some states also treat the former spouse's relatives as having predeceased.[295]
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> ***Trap***: The disinheritance of an ex-spouse may only occur when the divorce is finalized. Even if a new Will is drafted to disinherit the soon-to-be ex-spouse during the divorce process, in most states, the spouse still has legal rights against the decedent's estate (e.g., a spousal elective share or community property right) until the divorce is finalized.

New Dispositive Documents. If divorce is anticipated, the client should promptly

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293 Sue Shellenbarger, *Co-Workers Can Wreck a Marriage: At the Office, Divorce Is Contagious*, WALL ST. J., (Nov. 13, 2003, 8:53 AM), http://www.wsj.com/articles/SB106868624044945OO.

294 GA. CODE ANN. § 53-4-49 (2015).

295 C.f., Texas (TEX PB. CODE ANN. § 69(b)), provides: *"If, after making a will, the testator's marriage is dissolved, whether by divorce, annulment, or a declaration that the marriage is void, all provisions in the will, including all fiduciary appointments, shall be read as if the former spouse* *and each relative of the former spouse who is not a relative of the testator* *failed to survive the testator, unless the will expressly provides otherwise."* (emphasis added)

discuss with an estate planner the benefit of executing a new Will in contemplation of the divorce. The impact of the divorce on the client's existing estate planning should be considered an integral part of the divorce process and should precede the finalization of the divorce process. Leaving the decision to the inflexibility of statutory law is not generally an acceptable approach.

> ***Drafting***: If a divorce or separation has occurred and the resulting agreement places financial obligations on the client, any new Will should reflect the terms of the settlement agreement. Drafters should be careful to provide that any bequests to an ex-spouse are in lieu of the decedent's legal divorce obligations. For example, assume the divorce decree provides that a payment of $100,000 be made to an ex-spouse in ten years. The Will says *"If my ex-spouse is alive in ten years, I convey to her $100,000."* As a result, the ex-spouse may receive a double benefit of both the bequest and divorce settlement rights.

Incapacity Documents. Many clients have drafted powers of attorney to provide for the handling of medical and property issues upon incapacity. In many cases, the clients do not focus on revising these important documents during or even after divorce. Having an ex-spouse or a divorcing spouse in charge of your medical and property decisions is probably not advisable.

If the spouse is the only named agent and is automatically removed by applicable state law, there could be no one empowered to serve as agent for the Medical Directive or Power of Attorney. Clients should be strongly encouraged upon the first appearance of divorce to update their powers of attorney and name successor decision makers.

The effective date of the revocation for incapacity documents varies from state to state For example:

- In Florida,[296] an agent's authority under a Power of Attorney terminates when "*an action is filed for dissolution or annulment of the agent's marriage to the principal or their legal separation*, *unless the Power of Attorney otherwise provides*" and dissolution or annulment of the marriage of the principal revokes the designation of the principals former spouse as a surrogate.
- Georgia law[297] provides: *"... if, after executing an advance directive for health care, the declarant's marriage is dissolved or annulled, such dissolution or annulment shall revoke the designation of the declarant's former spouse as the declarant's health care agent."*

> ***Drafting***: Clients should consider whether to provide that their Medical Directives and Powers of Attorney are terminated immediately upon the filing of a divorce complaint, rather than having the termination be effective as of the

296 FLA. STAT. § 709.2109(2)(b) (2015) (emphasis added)
297 GA. CODE ANN. § 31-32-6(b) (2015). (emphasis added)

date of the final divorce decree. Most clients would prefer not to have an ex-spouse decide what pain medicine they should receive.

Divorce & Beneficiary Changes. Many divorcing clients are under the mistaken impression that their divorce settlement agreement and/or divorce decree eliminate all spousal claims to their retirement benefits or other non-probate beneficiary designations.[298] This same problem can occur with outdated beneficiary designations for life insurance policies.[299]

Trap: Unfortunately, the failure to change the beneficiary designations after the marriage is dissolved may result in the ex-spouse still being entitled to the retirement account upon the death of the plan owner.[300] For example, in Schultz v. Schultz,[301] an Iowa court ruled that when a divorce decree did not include any waiver of a spouse's IRA account and the former spouse never removed the ex-spouse as a named IRA beneficiary, the ex-spouse was entitled to the IRA assets upon the death of the IRA account owner, even when the account owner had remarried.

Trap: In Merchant v. Corder,[302] 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.

Caution: The IRS has announced[303] that qualified retirement plans which provide that a legal separation automatically terminates a participant's designation of his or her spouse as beneficiary may violate the ERISA spousal death benefit rules. The announcement noted that *"Retirement plans may continue to provide that if participants get a divorce, their designation of their former spouse as plan beneficiary is automatically revoked."* Note that it is the terms of the retirement plan that were in question and when spousal rights are revoked.

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298 See the excellent article by Leslie A. Shaner, *When Clients Fail to Change Beneficiary Designations*, FAM. L. MAG. (Dec. 10, 2013), http://www.familylawyermagazine.com/articles/beneficiary-designations. *See also* UNIF. PROB. CODE § 2-804 (UNIF. LAW COMM'N 2014).

299 EDWARD G. (WOODY) CONNETTE, ET AL., LAWYERS MUTUAL, DEAD BUT NOT DONE: THE OUTDATED DESIGNATION OF BENEFICIARY, *available at* http://files.lm2014.gethifi.com/Dead_not_Done.pdf (last visited June 1, 2015).

300 *Supra* Shaner, note 298.

301 591 N.W.2d 212 (Iowa 1999).

302 No. 98-2128, 1999 WL 486590 (4th Cir. July 12, 1999).

303 INTERNAL REVENUE SERV., EMPLOYEE PLANS NEWS, 2013-3.

Resource: Albert Feuer, *Determining the Death Beneficiary Under an ERISA Plan and the Rights of Such A Beneficiary*, 54 Tax Management Memorandum 323 (August 2013).

Proactive Planning for Clients and their Heirs

In 1820 Missouri imposed a tax on all Bachelors between the ages of 21 and 50.[304]

Divorce is a demographic fact which is often ignored in the estate planning process. Every plan needs to address the possibility that the client or an heir will face a future divorce. While the discussion may be awkward for the client and advisors, it is an unpleasant prospect which should be strongly addressed.

Many parents recognize that their children's marriages are not stable. Because 49% of marriages end in divorce, a couple with four children (on average) can expect two divorces within their family. In contemplation of this, clients should consider inheritance vehicles which restrict the ability of a divorced spouse to obtain part of the family assets. Among the approaches which should be considered are:

Limiting Control. The single most important aspect of any asset is its control. This is especially true in the context of the divorce of an heir. For example, the last thing that most family businesses need is a former son-in-law attempting to gain some control over the family business. In many cases, a client's spouse or the spouses of his or her heirs hold interest in a family business or may obtain an interest in a family business as a result of divorce or death of the family member. Buy–sell agreements[305] should contemplate this possibility and provide a mechanism that allows other family members to buy-out the divorcing spouse on reasonable terms. If the terms are designed to penalize an ex-spouse, they may be considered unenforceable. Included in those terms should be a long-term payout to minimize the cash flow problems for the business. Such terms may also reduce the risk that the spouse would want to receive business interests in the divorce.

Spendthrift Trusts. Spendthrift trusts have long been a part of the estate planner's tools. In recent years, as clients increasingly express concerns about asset protection and/or spendthrift children, these trusts have become a major part of the estate planning business. Basically, a spendthrift trust is any trust which provides for two major restrictions. First, it restricts the ability of any trust beneficiary to assign or otherwise transfer his or her interest in the trust. In most states, a beneficiary may freely assign a trust right (e.g., as collateral for loans or for other personal purposes). Second, a spendthrift trust restricts the right of creditors of a beneficiary to demand trust distributions of income or principal in order to satisfy the obligations of the beneficiary. Such trusts also eliminate the ability of spouses to put pressure on an heir to put assets into a joint name. Virtually every trust should contain a spendthrift provision. It's simply good planning.

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304 WILLIAM E. FOLEY, THE GENESIS OF MISSOURI: FROM WILDERNESS OUTPOST TO STATEHOOD 287 (2014).

305 See HOWARD M. ZARITSKY, TAX PLANNING FOR FAMILY WEALTH TRANSFERS ¶ 9.05 (5th ed. 2015).

But there are other cases which should provide some caution. For example:

- The permissible limits of spendthrift trust vary widely from state to state. In some states creditors are still free to garnish actual distributions to the beneficiary but are unable to force Trustee to make distributions in order to garnish them.
- In Dwight v. Dwight,[306] a Massachusetts Appeals Court ruled that a spendthrift trust created by a divorced husband's father could be treated as an increase of the divorced husband's income, allowing the ex-spouse to claim a portion of it as alimony. A narrow reading of the case would seem to indicate that the decision was at least partially based upon the existence of an ascertainable standard for the husband's benefit. Had distributions been in the "sole, absolute and unfettered discretion" of an independent trustee, the ruling might have been different.

  Drafting: Include in any prenuptial or post-nuptial agreement a waiver of any direct or indirect rights or powers over any trust benefits of the other spouse in the event of divorce.

  Drafting: Given the high incidence of divorce, lawyers should counsel their clients about the possible alimony and property claims that heirs' divorcing spouses may be able to make and draft the client's estate planning documents in ways designed to minimize those risks. For example:
  - Using discretionary trusts with independent trustees in lieu of mandatory payouts or ascertainable standards,
  - Making specific statements that it is the client's intent that income and property of the trust are not accessible to an heir's ex-spouse and
  - Adopting spendthrift trust language.

  Caution: In states which do not permit self-settled spendthrift trusts, the use of trusts (e.g., Charitable Remainder Trusts and Grantor Retained Annuity Trusts), created by a grantor and which provide current distribution rights and benefits to the grantor (and with the grantor often serving as a Trustee) may open the grantor's beneficial rights in the trust to the claims of creditors.[307]

Garnishment of Distributions. Even though a trust may limit the claims of a divorcing spouse against the assets of the trust, the divorcing spouse might still be able to make a claim against actual distributions made to the beneficiary/ex-spouse. For example, a Georgia statute provides that, except when the beneficiary of a spendthrift trust is suffering under significant physical or mental disability that impairs the beneficiary's

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306 756 N.E.2d 17 (Mass. App. Ct. 2001).

307 *See*: In Re Mack, 69 B.R. 392 (2001).

ability to provide for their care, an alimony or child support claim can be made against "*a distribution to a beneficiary*."[308] Note that the Georgia statute does not allow a former spouse to require that the trustee(s) make a distribution from a spendthrift trust.

Discretionary Trusts. As discussed above, when clients are concerned about the financial and marital problems of an heir, they would be well advised to adopt provisions in their trusts which grant trustees the broad discretion to decide when to make distributions to or for the benefit of a beneficiary. The effective result is that the beneficiary has no vested or attachable rights in the trust for a creditor to make claim against.[309]

> ***Drafting***: If the client adopts such provisions, it may be important to provide some additional safeguards for both trustees and beneficiaries, such as giving beneficiaries the right to remove trustees and indemnifying trustees for their good faith acts. It may also be advisable to place responsive trustees in charge of such heir's trust, so that if the marriage is dissolved, additional benefits (i.e., greater principal distributions) may pass to the heir.

> ***Drafting***: A key element of a Spendthrift/Discretionary Trust is limiting the rights of a trustee/beneficiary to make decisions on distributions to the beneficiary's own benefit.[310] Either the beneficiary should not be a trustee or they can be a Co-Trustee, with specific language limiting the beneficiary's right to participate in distributions for an heir's own benefit or to satisfy any legal obligations that they might have (e.g., child support).

Jointly Held Accounts. Many couples hold significant assets in joint name (e.g., a brokerage account). As a deemed marital gift, the spouse may have a right to 50% of the account in the event of divorce, even though the spouse may have made no contributions to the joint account. The solution? Encourage clients who have sizeable assets before marriage or who receive sizable inheritances to keep the funds segregated from marital assets in their personal accounts.

Irrevocable Trusts. Virtually all irrevocable trusts should be drafted (and maybe even some revocable trusts), in contemplation of the possibility that one or more of the beneficiaries may get divorced. For example, assume a client creates an irrevocable life insurance trust. The spouse is named as a beneficiary and co-trustee and is given significant power, such as the right to remove other trustees and a limited power of appointment to reconfigure the trust for the benefit of the couple's joint heirs. The documents should contemplate the possibility that the insured grantor and the beneficiary/spouse are later divorced. The document could provide that all rights and powers of the spouse, including her right to serve as co-trustee, immediately terminate

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308 GA. CODE ANN. § 53-12-28 (2015).
309 *See*: First Northwestern Trust Co. v. IRS, 622 F.2d 387 (1990).
310 C.f., In the Matter of: Warren and Brenda Bierman, 1998 Bankr. LEXIS 2012.

upon either legal separation or divorce. Few clients want an ex-spouse to benefit financially from their death or be able to control the inheritance of their assets.

Similar issues involve planning for surviving spouses. For example, assume a widow remarries and then dies. There could be claims against the deceased spouse's assets by the second husband. Spousal elective share statutes may permit the new husband to claim support from the deceased wife's estate, or assets may have been directly or indirectly (e.g., payoff of the mortgage on a home that was jointly held) placed in joint name, with the surviving new husband taking survivorship rights. The use of spendthrift Bypass and QTIP trusts in the deceased husband's estate can reduce these potential claims.

Other Issues

The average married couple with small children spends just four minutes a day alone together[311]

Common Law Marriages. A minority of states allow their residents to enter into marriages without obtaining a marriage license. As of January 1, 2015, these states include: Alabama,[312] Colorado,[313] Iowa,[314] Kansas,[315] Montana,[316] New Hampshire,[317] Oklahoma,[318] Rhode Island,[319] South Carolina,[320] Texas[321] and Utah.[322]

In addition, a number of other states have statutorily eliminated common law marriages which occur after certain dates.[323] These states and the effective dates are:[324] Florida (Jan. 1, 1968),[325] Georgia (Jan. 1, 1997),[326] Indiana (Jan. 1, 1958),[327] Mississippi (April 6, 1956), Michigan (January 1, 1957), Ohio (Oct. 10, 1991),[328] Pennsylvania (Jan. 1, 2005),[329] and South Dakota (July 1, 1959).

In most states, a common law marriage only occurs if certain requirements are met. Just living together (even if the cohabitation spans decades) does not create a common law marriage. The general requirements include:

- the parties have the legal right to marry under state law,
- the couple intends to be married,
- the couple hold themselves out to the public as being married, and

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311 SARÍ HARRAR & RITA DEMARIA. THE 7 STAGES OF MARRIAGE: LAUGHTER, INTIMACY, AND PASSION (2007).

312 Waller v. Waller, 567 So. 2d 869 (Ala. Civ. App. 1990); Hudson v. Hudson, 404 So. 2d 82 (Ala.Civ.App. 1981); Ala. Att'y Gen. Op. 1992-041.

313 COLO. STAT. §14-2-109.5 (2015).

314 IOWA CODE §595.1(A) (2015)

315 KAN. STAT. ANN. § 23-2502, 23-2714 (2015).

316 MONT. STAT. §40-1-403 (2015).

317 N.H. REV. STAT. ANN. § 457:39 (2015)

318 OKLA. STAT. TIT. 43, § 7-A (2015) provides that marriage is only recognized by the fulfillment of statutory formalities. However, case law indicates that the state may recognize common law marriages.

319 Demelo v. Zompa, 844 A.2d 174 (R.I. 2004)

320 S.C. CODE ANN. § 20-1-360 (2015).

321 TEX. FAM. CODE. ANN. § 1.101, 2.401–.402 (2015).

322 UTAH CODE ANN. § 30-1-4.5 (2015)

323 The following states have never permitted common law marriages: Arkansas, Connecticut, Delaware, Louisiana, Maryland, North Carolina, Oregon, Tennessee, Vermont, Virginia, Washington, West Virginia, and Wyoming.

324 This list only includes states making changes after the 1950s. For example, Massachusetts eliminated common law marriages in 1646 and North Dakota made the elimination in 1890.

325 FLA. STAT. § 741.211 (2015).

326 GA. CODE ANN. § 19-3-1.1 (2015).

327 IND. CODE §31-11-8-5 (2015).

328 OHIO REV. CODE ANN. § 3105.12 (2015)

329 23 PA. CONS. STAT. § 1103 (2015).

- the couple lives together for some period of time and has sexual relations.

A common law marriage has all of the legal rights of a formalized marriage, and if recognized in the state of residency of the couple, it is generally deemed a legal marriage even if the couple moves to another state which does not permit common law marriages.

Abandoned Spouse. Even if a legal separation is not in place, a married but "abandoned spouse" will not be considered married for tax purposes if the following criteria are meet:[330]

- the individual files a separate return,
- the individual maintains a household which constitutes for more than one-half of the taxable year the principal place of abode of a child with respect to whom such individual is entitled to a deduction for the taxable year under section 151 (or would be so entitled but for section 152(e)),
- such individual furnishes over one-half of the cost of maintaining such household during the taxable year, and
- during the last 6 months of the taxable year, such individual's spouse is not a member of such household.

Legal Separation. A legal separation is like putting your marriage on hold. Warren Buffett separated from his wife in 1977 and stayed separated from her until she died in 2004. He married his long term live-in girlfriend in 2006.

> ***Opportunity***: In some cases, obtaining a legal separation instead of a divorce makes sense. For example:
>
> - To receive rights that require a minimum number of years of marriage (e.g., to obtain survivor social security benefits you must have been married 10 years). Having a legal separation may allow you to meet that condition.
> - A legally separated spouse may be entitled to obtain medical insurance from the spouse's employer.
> - For religious purposes, a legal separation may be more acceptable.

> ***Caution***: For most federal tax purposes (and most state tax purposes), a person who is "*legally separated from his spouse under a decree of divorce or of separate maintenance shall not be considered as married*."[331]

Year-End Marital Status. The income tax status of a taxpayer is determined as of the end of the tax year or upon the death of either spouse.[332] If the couple are divorced,

330 I.R.C. § 7703(b) (2015).
331 I.R.C. § 7703(a)(2) (2015).
332 I.R.C. § 7703 (2015) (2015).

legally separated or the “abandoned spouse” rule[333] applies, then the couple cannot file joint income tax returns.

> ***Opportunity***: If the tax savings are significant, a settlement agreement could be entered into before year-end, with the divorce decree being effective after the end of the year.[334] A client may have a lower income tax cost from filing as married rather than single. As a part of any amicable divorce (and perhaps as a negotiating position in less amicable divorces), the income tax savings of remaining legally married until the end of the year should be examined.
>
> ***Opportunity:*** If the delay can be arranged, the higher income taxpayer should consider accelerating income into the current tax year and delaying deductions until the following year. While projections must be run, such a move might lower the overall taxes.
>
> ***Trap:*** There are also disadvantages to filing a joint return, including:
>
> - Alimony deductions are not available. If the wealthier spouse is in a higher state and federal income tax bracket (potentially over 50% in 2015) and the other spouse is in a lower tax bracket (potentially 10%), the payment of alimony can provide a significant tax savings to both spouses.
> - If a spouse signs the return, he or she has joint and several liability for the return. However, if the spouses decide to do this, then they may want to file a “separate liability election,”[335] which states that neither has liability for the other’s tax reporting or taxes.
> - If both spouses have significant income, the “marriage penalty” and the loss of tax benefits at higher levels of income may actually mean that filing a joint return creates a higher level of overall income taxation. Always run the projections.

Defining Family. The Internal Revenue Code defines family members and related parties in at least 16 different ways. The tax definitions of a family member or related party can get interesting. For example:

- In-Laws. I.R.C. §4946 provides that "*For purposes of subsection (a)(1), the family of any individual shall include only his spouse, ancestors, children, grandchildren, great grandchildren, and the spouses of children, grandchildren, and great grandchildren*." This ironically means that you are a member of your spouse's parents' family, but they are not a member of your family. Try explaining that to your in-laws.

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333 I.R.C. § 7703(b) (2015).

334 In such a case, the divorce decree should discuss how any income tax refunds are allocated. In the absence of such language, the IRS has created a methodology for such allocations based upon each party’s relative tax liability. *See* Rev. Rul. 85-70, 1985-1 C.B. 361; Rev. Rul. 85-72, 1985-1 C.B. 347; Rev. Rul. 80-7, 1980-1 C.B. 296; Rev. Rul. 74-611, 1974-2 C.B. 399.

335 *See* I.R.C. § 6015(c)(3)(C) (2015).

- Related Party. Code §672(c) provides that: "*For purposes of this subpart, the term* "*related or subordinate party*" *means any non-adverse party... who is the grantor's spouse if living with the grantor*." (emphasis added). So if your spouse lives across the country or moves across the street, the application of the definition changes?
- Subservient. Code §672(c) provides that: "*for purposes of subsection (f) and sections 674 and 675, a related or subordinate party shall be presumed to be subservient to the grantor in respect of the exercise or non-exercise of the powers conferred on him unless such party is shown not to be subservient by a preponderance of the evidence.*" (emphasis added) Just how much evidence do you need to properly demonstrate that your spouse is not sufficiently "subservient"? Do years of marriage count?
- Qualifying Relative. The definition of a "*qualifying relative*" in Code §152(d)(2)(H) can include someone who is not related to you by blood or marriage.
- Spouses. Code §7701(a)(17) reads: "*As used in sections 682 and 2516, if the husband and wife therein referred to are divorced, wherever appropriate to the meaning of such sections, the term 'wife' shall be read 'former wife' and the term 'husband' shall be read 'former husband'; and, if the payments described in such sections are made by or on behalf of the wife or former wife to the husband or former husband instead of vice versa, wherever appropriate to the meaning of such sections, the term 'husband' shall be read 'wife' and the term 'wife' shall be read 'husband.'*" Crystal clear-right?
- Child. The useable definition of a "child" varies widely due to the particular benefit Congress was trying to create. Differences particularly have to do with age. Children under age 19 count in defining earned income tax credit benefits, those under 17 qualify for the child credit, and only those under 13 are eligible for the child and dependent care credit. Meanwhile, a "child" for purposes of the "kiddie" tax age stops at age 24 for full time students.

The U.S. Supreme Court has ruled that an Illinois law that provided for an absolute bar of inheritance from a father for a child born out of wedlock was unconstitutional.[336]

Adopting your Significant Other. Divorce can throw a wrench into planning expectations, particularly the pre-divorce creation of inflexibly drafted irrevocable trusts.

> ***Opportunity***: However, there can be creative opportunities. For example, in Goodman v. Goodman a Florida resident and 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

336 Trimble v. Gordon, 430 U.S. 762 (1977).

adoption on a procedural basis (i.e., lack of notice to the other trust beneficiaries), but did not rule on the core issue of whether the adoption was legal and entitled the girl friend to benefit from the trust. It is not clear what, if anything, Mr. Goodman did next, but his options may be limited.

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.[337]

Dependency Deduction. Most people assume that the dependency deduction[338] is limited to family members, but this is not the case. A non-blood member of the household can be a dependent. The definition of a "qualifying relative" in I.R.C. §152(d)(2)(H) includes "*[a]n individual . . . who, for the taxable year of the taxpayer, has the same principal place of abode as the taxpayer and is a member of the taxpayer's household*." The person must be a member of the taxpayer's household for the entire year, with partial year residency disqualifying the deduction.[339]

> ***Opportunity***: Effectively, this allows a step-parent to obtain a dependency deduction for a stepchild.

Interestingly, while the head of the household may qualify for a dependency deduction for someone who is not a blood relation or a relation by marriage, they will not qualify for head of household income tax filing.[340]

Innocent Spouse Relief. Many a divorced spouse has been surprised to discover their former loved one was not altogether honest about paying taxes. Unfortunately, if a joint return was signed, the IRS may be calling upon the "innocent" spouse to pay the couple's income taxes, penalties and interest.

An "innocent spouse" may be able to file to avoid a claim based upon the actions of the other spouse. In 1998, Congress greatly broadened the rules protecting innocent

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337 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 (Apr. 16, 2013); *Matter Robert Paul P.*, 63 N.Y. 2d 233, 236 (1984); Adult Adoption Law in the United States, available at http://adoptingback.com/adopting-back/united-states-adult-adoption-law/.

338 I.R.C. § 151 (2015). While referred to as an "exemption," the I.R.C. makes it clear that it is deduction used in computing taxable income.

339 Treas. Reg. § 1.152-1(b) (2015).

340 *See* Rev. Rul. 84-89, 1984-1 C.B. 5.

spouses.[341] Final regulations have been issued under the new rules.[342]

Even when the spouse is declared an innocent spouse for liability purposes, the IRS can claim that property transfers from the tax-burdened ex-spouse should be subject to rescission and, therefore, subject to the unpaid tax liability. While most property transfers between spouses are treated as "disqualified" transfers (and subject to seizure for the payment of taxes of the transferor spouse), transfers under divorce or separation agreements are generally presumed to be valid. In such cases, the IRS bears the burden of showing that the payment was disqualified. This may be one situation in which the less the transferee spouse knows of the tax problems of the transferor spouse, the better.

Resources:

- U.S. DEP'T OF TREASURY, INTERNAL REVENUE SERV., PUBLICATION 971, INNOCENT SPOUSE RELIEF (2015);
- U.S. DEP'T OF TREASURY, INTERNAL REVENUE SERV., FORM 8857, INNOCENT SPOUSE RELIEF (2014);
- U.S. DEP'T OF TREASURY, INTERNAL REVENUE SERV., FORM 8958, ALLOCATION OF TAX AMOUNTS BETWEEN CERTAIN INDIVIDUALS IN COMMUNITY PROPERTY STATES (2014);
- INNOCENT SPOUSE RELIEF, 645-2nd TAX MGMT (BNA).

Non-Citizen Spouse. The rules governing the marriage, divorce, immigration, and taxation of non-resident and resident aliens who are married to US citizens can be quote complex, involving both US and foreign based tax issues, tax treaties, conflicts between jurisdictions and various reporting requirements. While these rules are beyond the scope of this article, the following materials may be helpful.

Resources:

- Tax Management Portfolios (BNA):
  - Immigration and Expatriation Law for the Estate Planner, No. 806-2nd
  - Transfers to Noncitizen Spouses, No. 842-2nd
  - Non-Citizens - Estate, Gift and Generation-Skipping Taxation, No. 837-3rd
  - U.S. Estate and Gift Tax Treaties, 851-2nd
- Jane R Livingstone, *Marriage, Immigration, and Taxes*, Practical Tax Strategies, Sept. 2011.

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341 *See* Internal Revenue Service Restructuring and Reform Act of 1998 §§ 3201–3202, I.R.C. § 6015 (2015). For more detailed information see U.S. DEP'T OF TREASURY, INTERNAL REVENUE SERV., PUBLICATION 971, INNOCENT SPOUSE RELIEF; Paul G. Schloemer, *Innocent Spouse Rules Provide Challenges And Opportunities,* 87 PRAC. TAX STRATEGIES 69 (Aug. 2011).

342 Treas. Reg. §§ 1.6015-0 to -9 (2015).

- Diana S.C. Zeydel and Grace Chung, *Estate Planning for Noncitizens and Nonresident Aliens: What Were Those Rules Again?* Journal of Taxation, Jan. 2007.

Deducting Legal Fees. Normally, the cost of personal, non-tax related legal advice is not a deductible expense. Thus, most legal expenses incurred in a divorce are not deductible.[343] However, if the legal costs are incurred by the taxpayer in order to obtain or force payment of taxable alimony (or an increase in taxable alimony) the costs may be deductible.[344] Tax advice obtained in the course of the divorce may also be deductible.[345]

However, the legal fees of the spouse paying the alimony, or attempting to reduce the amount of alimony are not generally deductible.[346] Moreover, if the spouse paying the alimony is also paying the legal fees of the ex-spouse, the fees will not be deductible.

> ***Opportunity***: It may make sense to have the ex-spouse be responsible for his or her own legal fees and increase the alimony payment (a deduction for the paying ex-spouse) to cover the additional cost. If such an approach is taken, the agreement should provide that the obligation to make the alimony/legal fee payment terminates at the recipient spouse's death.[347]

Payment of legal fees to determine child support and property settlements are not generally deductible, because they are treated as personal, non-income related expenses. The cost of preparing prenuptial agreements would probably fall into the same category of personal, non-deductible expenses.

The divorce attorney should be encouraged to allocate appropriate portions of the legal costs to deduction-related alimony and tax issues.[348] Unfortunately, there are no specific rules governing such allocations and if the allocation is too aggressively bent to providing deductions to the client, the IRS or the courts may impose their own opinion of a more reasonable allocation. Accurate and detailed time records will be a pivotal part of any final determination.

> ***Caution***: Even if the client gets the tax deduction, other tax limits can reduce the tax benefit. Deductible legal fees are shown as a miscellaneous itemized deduction on the taxpayer's Schedule A. Only the expenses in excess of 2% of the taxpayer's adjusted gross income are deductible,[349] and these may also be

343 *See* U.S. v Gilmore, 372 U.S. 39 (1963).
344 *See* I.R.C. § 212(1) (2015); Treas. Reg. § 1.262-1(b)(7) (2015).
345 *See* I.R.C. § 212(2); and Treas. Reg. § 1.212-1(l) (2015).
346 Hunter v. U.S., 219 F.2d 69 (2nd Cir. 1955).
347 I.R.C. § 71(b)(1)(D) (2015); Hampers v. Comm'r, 109 T.C.M. (CCH) 1138 (2015).
348 *See* Rev. Rul. 72-545, 1972-2 C.B. 179.
349 *See* I.R.C. § 67 (2015).

reduced by the itemized deductions for high income taxpayers.[350]

Inherited IRAs & Bankruptcy. In the Clark v. Rameker decision,[351] the U.S. Supreme Court unanimously ruled that an inherited IRA did not have the bankruptcy protection of an ERISA retirement account or a taxpayer's own IRA. The ruling did not provide that a spousal inherited IRA had a different treatment. State statutes may offer some partial protections for IRAs and other retirement benefits, particularly if a bankruptcy filing has not occurred.[352]

> ***Trap:*** If a creditor seizes funds from an inherited IRA to cover the owner's debts, the owner remains responsible for the income taxes resulting from the withdrawal.
>
> ***Opportunity***: To provide some asset protection and create a gate-keeper between the asset and the beneficiary, clients should consider using qualified trusts as designated beneficiaries of retirement accounts and IRAs.[353] Particularly in second marriages, the use of a qualified trust can also assure that any remaining IRA assets upon the surviving spouse death are distributed to the original owner's family members.
>
> ***Trap***: If the surviving spouse is insolvent or has pending creditors, a spousal rollover by a surviving spouse/debtor might be a fraudulent conversion of non-exempt assets (inherited IRA) to an exempt asset (spouse's own IRA)?[354]
>
> ***Resources***:
> - Mary Vandenack, *Reconsidering the Design of Trusts Used As IRA and Qualified Account Beneficiaries Post-Clark*, ASSET PROTECTION PLAN. NEWSLETTER (LISI), no. 252, July 7, 2014.
> - Ed Morrow, *Clark v. Rameker: Supreme Court Holds that Inherited IRAs Are Not Protected in Bankruptcy, Are Spousal Inherited IRAs and Even Rollover IRAs Threatened As Well?* ASSET PROTECTION PLAN. NEWSLETTER (LISI), no. 248, June 16, 2014.

Social Security. If clients legally change their names as the result of a divorce or marriage, they should notify the Social Security Administration (SSA) and obtain a new Social Security card under their new name. When the application is filed for the new card, SSA will process the change and relay the change to the IRS.

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350 *See* I.R.C. § 68 (2015).

351 134 S. Ct. 2242 (2014).

352 Ed Morrow, *50 State Exemption Chart on IRAs, Non-ERISA 403(b) Plans & Roth Variants*, ASSET PROTECTION PLAN. NEWS. (LISI), no. 256, Aug. 7, 2014.

353 See the prior discussion of qualified IRA Trusts.

354 Moreover, could the 10 year look back rule of §548(e) of the Bankruptcy Code apply because the rollover could be treated as a transfer to a "Self-settled Trust or Similar Device"?

Clients cannot apply for a new Social Security card online. They must take or mail the application and supporting documentation to the local Social Security office. There is no charge for a new Social Security card.[355]

> ***Caution***: To avoid confusion on their income tax filings, clients should wait to file their returns until after the SSA process has been completed.

CONCLUSION:

Clients who are getting married need to understand the rights that their new spouse will automatically obtain when "I do," "I will" are spoken, particularly when there are children from prior relationships.

Clients also need to understand that while divorce may not be inevitable, it certainly has a strong probability of impacting any family. Discussing the difficult planning and drafting issues surrounding divorce may not be comfortable for the client or for the advisor, but it is essential if a client and the client's family are to be properly protected.

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355 For more information see: SOCIAL SECURITY ADMINISTRATION, www.ssa.gov (last visited June 4, 2015).

Additional Resources for Advisors

- *List of Helpful Resources*
- *Practical Remarriage Checklist*
- *Practical Post-Divorce Checklist*
- *Personal Property Disposition form for Married Clients*
- *Personal Property Disposition form for Single Clients*

List of Helpful Resources

Research Sources:

- BORIS BITTKER & LAWRENCE LOKKEN, FEDERAL TAXATION OF INCOME, ESTATES AND GIFTS ¶ 44.6 (2015) (discussing transfers between spouses and former spouses).
- Tax Management Portfolios (BNA):
  - Divorce and Separation, No. 515-2nd
  - Marital Agreements, No. 849-2nd
  - Spouse's Elective Share, No. 841-1st
  - Family, Kinship, Descent, and Distribution, 858-1st
- U.S. DEP'T OF TREASURY, INTERNAL REVENUE SERV., PUBLICATION 504, DIVORCED OR SEPARATED INDIVIDUALS (2015).
- JEFFREY A. LANDERS, DIVORCE: THINK FINANCIALLY, NOT EMOTIONALLY – WHAT WOMEN NEED TO KNOW ABOUT SECURING THEIR FINANCIAL FUTURE BEFORE, DURING, AND AFTER DIVORCE (2012).
- NATALIE B. CHOATE, LIFE AND DEATH PLANNING FOR RETIREMENT BENEFITS (2011).

Website Calculators: There are some interesting marriage and divorce related sites on the Web, including:

- http://www.divorce360.com/content/divorcecalculator.aspx - calculate your chance of getting divorced
- http://www.alllaw.com/calculators/ChildSupport & http://dadsdivorce.com/resources/child-support-calculator/ - for child support calculations
- http://alimonycalculator.us/ - to calculate estimated alimony payments
- http://www.ssa.gov/oact/quickcalc/ - to calculate your Social Security benefits
- http://taxpolicycenter.org/taxfacts/marriagepenaltycalculator.cfm and http://marriagetaxcalculator.com/ - to calculate the amount of your marriage penalty

Other Websites:

- Medicare and Medicaid Guide, an internet resource available www.wklawbusiness.com

Checklists:

- Go to www.scrogginlaw.com for practical checklists:
  - *Practical Post-Divorce Checklist*
  - *Practical Remarriage Checklist*
  - *Personal Property Disposition forms for Married Clients*
- BNA Portfolio 849-2nd: Marital Agreements, Worksheet 8 Client Letter — *Post-Execution Checklist to Carry out Terms of Agreement*

PARTIAL CHECKLIST OF ACTIONS TO CONSIDER UPON A RE-MARRIAGE

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There are a multitude of practical and legal issues which surround any remarriage. This list is intended to provide a partial list of issues that you should address before and after a remarriage. Your remarriage involves far more than just the signing a marriage license and a spouse immediately obtains multiple rights when you marry. While the checklist can apply to couples in their first marriage, its primary focus is on those getting remarried after either a prior divorce or after becoming a widower or widow.

____Examine with your Attorney the Issues on the Impact of Remarriage & Determine what needs to be Changed. For example:

- Spousal Medical Benefits
- Social Security Benefits (you can lose spousal survivor benefits by re-marrying before age 60)
- ERISA Retirement Plans (spouses can have an automatic right to your ERISA account, unless waived)
- Employment Pension Plans (e.g., do you elect joint life payouts or only a payout for one life)
- Employment Benefit Plans (e.g., life insurance for spouses, HSAs)
- Military and Veteran Benefits
- Spousal Support Laws
- Naming your new spouse as Joint Insured under auto, home, property, casualty and umbrella polices
- Spousal rights at Death, particularly if you do not have a valid Will
- Increased Taxes, particularly income taxes (e.g., the "marriage penalty")
- Rights of Spouse if you Reside in a Community Property State
- Statutory Right of Spouse to be your Decision Maker at your Death or Incapacity
- Medicaid Qualification
- Decide whether to execute a Pre-Nuptial Agreement dealing with the above issues
- Determine if there are open Issues from any prior marriage (e.g., see the Practical Checklist for Divorce at www.scrogginlaw.com)

____Decide whether to adopt a written Family Mission Statement on issues in a new marriage. For example:

- How expenses are shared (e.g., who pays for a minor child's education and other needs)
- How to deal with credit and liability issues, especially incurring new debt
- Interaction with an ex-spouse by the new spouse
- Savings approaches
- Religious affiliations
- Inheritance rights between spouses and all of the children
- The raising, supervision and education of children; Discipline by the non-parent

For more information, do a Google search on "Family Mission Statement" and "Marriage Mission Statement."

____ Determine what Beneficiary changes are needed for (both primary and contingent):

- ERISA Qualified Plans (if the spouse is not a beneficiary, the spouse <u>must</u> sign a consent *<u>after</u> the marriage is finalized*)
- Employer Pension Plans (e.g., electing joint life payouts)
- IRAs

- Deferred Compensation Plans (e.g., review the documents for automatic rights to a spouse)
- Stock Option Plans
- Life Insurance Policies
- Accounts "Paid to the Order of" or "Paid at your Death" to a third party

____Decide is the spouses will waive any beneficial rights under state law, to the extent permitted under state law. Note that it may be necessary to sign waivers <u>after</u> the remarriage. Check on the required conditions of any waivers (e.g., "fair disclosure"). Spousal rights under state law can include:

- Spousal Elective Share
- If residing in a Community Property state, the shared ownership of certain assets
- Spousal Support Rights
- Homestead and Personal Property Allowances
- Personal Property Allowance
- ERISA Retirement Plan Benefits
- Intestate Claims (i.e., if there is no Will to govern dispositions)

___ Complete any Title Transfers, such as:

- Residence Ownership
- Other Real Estate Ownership
- Automobiles
- Brokerage Accounts
- Bank Accounts
- Life Insurance

___Decide about entering into any Joint Liabilities, for example:

- Credit Cards
- Lines of Credit
- Personal Guarantees (e.g., business commercial loans)
- Mortgages (may not be permitted by the loan terms)
- Utilities (i.e., will it be in both names?)

____ Decide on Joint Accounts (*and update direct deposits to these accounts*), for example:

- Banking (i.e., checking, savings, etc.)
- Brokerage Accounts
- Safety Deposit Boxes (but be careful, the spouse may have authority to remove assets)
- Create Automatic Withdrawals (*e.g. to spouse's account or benefit*)

____If you change your Name or Address provide notice of the Change. For example:

- Tax Filings (file IRS Form 8822 for address changes)
- Employer Payroll and Benefit Plans
- Creditor, Credit Card, Bank, Brokerage and other Financial Accounts
- Insurance Policies, particularly auto, property, casualty and umbrella
- Medical Coverage
- Driver's License
- Voter Registration
- Passport
- Military and Veterans Benefits

- Social Security Administration (go to www.ssa.gov for the form)

____**Redo All Estate Planning Documents** (preferably before the remarriage)

- Reexamine all Decision Makers (and any automatic appointment of a new Spouse)
- Examine Spousal Rights to your assets if you Pass Away
- Will (*especially if revoked by remarriage under state law or state law grants spousal rights*)
- Revocable Trust(s)
- Medical Directive or Healthcare Power of Attorney
- General Power of Attorney
- Prepare a Joint Personal Property Disposition List (see example at www.scrogginlaw.com)
- Decide whether to create an Irrevocable Insurance Trusts or Marital Trusts which names the Spouse as Beneficiary (but consider providing that divorce or legal separation terminates a spouse's rights)
- If you revise your estate planning documents before the marriage, consider making them "in contemplation of the marriage" and provide for what happens if the marriage is called off.
- Provide in your documents that bequests are in lieu of any statutory rights that your spouse may have under local law.

___**Make Changes in Personal or Employer-Based Insurance Coverage**

- Life Insurance – should you increase the coverage and/or change beneficiaries?
- Health Insurance – name your spouse under your coverage?
- Long Term Care Insurance – should you purchase it for your spouse?
- Disability Insurance
- Property & Casualty (e.g., auto, home, umbrella)

___ **Notify the Children's School of any Changes in Custody or Pickup**

___**Decide if the new Spouse should have access to:**

- Your safety deposit box
- Any home safes
- Your bank and other financial accounts
- Your mail (i.e., do you use a non-residential mailing address?)

PARTIAL CHECKLIST OF ACTIONS AS A RESULT OF DIVORCE

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There are a multitude of practical issues which surround any divorce. This list is intended to provide a least a partial list of some of the issues which clients should address before and after their divorce is final. The list is not intended to cover every issue, but can help clients understand that the divorce involves far more than just the signing of a divorce decree.

____ **Change Beneficiary Designations on**:
- ERISA Qualified Plans (*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 your Death to the Ex-Spouse

___ **Complete Any Title Transfers on Assets** (*preferably before the divorce is finalized*),
- Residence Ownership
- Other Real Estate Ownership
- Automobiles
- Stock or Equity Rights in a Business or Investment (*get the original certificates*)
- Brokerage Accounts
- Life Insurance (e.g., ex-spouse owns policy)

___ **Terminate Joint Liabilities**, for example:
- Credit Cards
- Lines of Credit
- Personal Guarantees of Ex-Spouse's Liabilities (e.g., business interest)
- Mortgages (may not be permitted by the terms)
- Utilities

___ **Terminate Joint Accounts** (*and change direct deposits to accounts*)
- Banking (i.e., checking, savings, etc.)
- Brokerage
- Safety Deposit Boxes
- Terminate Automatic Withdrawals (*e.g. to ex-spouse's account or benefit*)

___ **Remove Permitted Access or Signing Authority by an Ex-Spouse,** for example
- Personal Banking *(i.e., checking, savings, etc.)*
- Business Payroll Service
- Business Checking Accounts
- Personal Brokerage Accounts

____ **File a Change of Address and/or Name Change for** (*Notice to Post Office and Notice to Each Party*), for example:
- Tax Filings (file IRS Form 8822 for address changes)
- Employer Payroll and Benefit Plans
- Creditor, Credit Card, Bank, Brokerage and other Financial Accounts

- Insurance Policies, particularly auto, property, casualty and umbrella
- Medical Coverage
- Driver's License
- Voter Registration
- Passport
- Military and Veterans Benefits
- Social Security Administration (go to www.ssa.gov for the form)

____ **Redo All Estate Planning Documents** (*to the extent an ex-spouse is named*)
- Will (*especially if revoked in any way by divorce under state law*)
- Revocable Trust(s)
- Medical Directive or Healthcare Power of Attorney
- General Power of Attorney
- Decide whether to Retain any Irrevocable Insurance Trusts which Name Spouse as Beneficiary
- If your Relatives have named your Ex-Spouse in their Documents, Alert them to the Need to make Changes

____ **Enter a Modification for any Employee Benefit Cafeteria Plan**

___ **Make Changes in Personal or Employer-Based Insurance Coverage that Names Ex-Spouse** *If permitted by the Divorce Decree* (*perhaps obtain a refund*)
- Life Insurance
- Health Insurance
- Long Term Care Insurance
- Disability Insurance
- Property & Casualty (e.g., auto, home, umbrella)

____ **Change Access Codes and Passwords**, for example:
- Web Based Access (e.g., bank, brokerage)
- Credit, Debit and ATM Cards
- Frequent Flyer Accounts
- Email Accounts
- Personal Safe

____ **Change the Locks and Location of any Hidden Keys** *(do not just take back keys)*
- Personal Home
- Studio Apartments
- Vacation Home
- Rental Properties
- Office
- Personal Safe
- Mailbox

____ **Obtain Signature of Ex-Spouse**
- Resigning an Officer or Director of any Business
- Signing over any Life Insurance, Long Term Care, Disability or Other Insurance Benefit
- To Permit any Continued Military or VA Benefits

- Relinquishment of any Rights to a Family Burial Plot

___ **Notify the School of any Minor Children of any Changes in Custody & Pickups**

___ **Create Any Required Funding Arrangements under the Divorce Decree**

Personal Property Ownership & Disposition List

(married couple)

Definitions:
"Asset" shall mean each particular tangible personal property listed below.
"Heir" shall mean the person named below who is intended to receive the Asset upon the death of the Owner.
"Owner" shall mean the person noted below who owns the particular listed Asset.
"Non-Owner" shall mean the person who signed this instrument, but is not listed at the owner of the particular listed Asset.
"Undersigned" shall mean each of the persons signing this instrument.

Agreement. The Undersigned(s) agree as follows:

1) That the ownership of their respective Assets is as shown below.
2) That except as disclosed in this statement:
    a) the ownership rests exclusively with the named Owner, and
    b) the Non-Owner does not have any collateral security, elective shares or any other rights in the Asset and hereby irrevocably waives any and all rights under any applicable law to each of the Assets.
3) That the Non-Owner will not challenge the ownership of any Asset, unless the Non-Owner has received a specific, signed statement from the Owner that the particular Asset has been transferred to the Non-Owner.
4) It is the desire of the Owner that any Executor or Personal Representative of the Owner's estate, in the exercise of such discretion as the fiduciary may have, convey the Asset to the Heir.

The Undersigned acknowledge that this instrument does not constitute a Last Will and Testament or similar dispositive document and may not legally convey the Asset under applicable state law. Consult with an estate planning attorney before using this instrument.

Detail Description of Asset *(add photo if possible)*	**Owner**	**Heir**
____________________________________	__________	_______________
____________________________________	__________	_______________
____________________________________	__________	_______________
____________________________________	__________	_______________
____________________________________	__________	_______________
____________________________________	__________	_______________
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____________________________________	__________	_______________
____________________________________	__________	_______________
____________________________________	__________	_______________

Effective this ___ day of _______, 201___ by the following Undersigned:

__________________________   ______________________________

Name: _________________   Name: _________________

This instrument was signed before the Notary Public the date first above written.

________________________   (Notary Seal)

Notary Public

Personal Property Ownership & Disposition List

(single)

Definitions:
"Asset" shall mean each particular tangible personal property listed below.
"Heir" shall mean the person named below who is intended to receive the Asset upon the death of the Owner.
"Undersigned" shall mean each of the persons signing this instrument.

Agreement. The Undersigned represents as follows:

- That except as disclosed in this statement:
  a) the ownership of the Assets listed below rests exclusively with the named Undersigned, and
  b) no other person has any collateral security or any other rights in the Asset.
- It is the desire of the Undersigned that any Executor or Personal Representative of the Undersigned's estate, in the exercise of such discretion as the fiduciary may have, convey the Asset to the Heir.

The Undersigned acknowledge that this instrument does not constitute a Last Will and Testament or similar dispositive document and may not legally convey the Asset under applicable state law. Consult with an estate planning attorney before using this instrument.

Detail Description of Asset *(add photo if possible)* **Heir**

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Effective this ___ day of _______, 201___ by the following Undersigned:

____
Name: ________________________

This instrument was signed before the Notary Public the date first above written.

_____________________ (Notary Seal)
Notary Public

Addendums from Federal Sources

- *5 Things Every Woman Should Know About Social Security*.
- HANDBOOK, SOCIAL SECURITY ADMINISTRATION § 406.
- *Spouses of Medicaid Long Term Care Recipients*.
- *Spousal Medicaid Improvisation Limits for 2015.*

www.socialsecurity.gov

5 Things Every Woman Should Know About Social Security[356]

There are many things a woman should know about Social Security. Here are five of the most important Social Security messages every woman should know.

1. Nothing keeps you from getting own Social Security benefit

- If you've worked for at least 10 years and earned a minimum of 40 work credits, you are vested in the Social Security system.
- Once you reach age 62, you will be eligible for your own Social Security benefit whether you're married or not and whether your husband collects Social Security or not.
- Your retirement benefit is figured the same way a man's retirement benefit is figured. It's based on a percentage of your average monthly wage using a 35-year base of earnings. If you don't have 35 years of earnings, we must substitute "zero" years to reach the 35-year base.
- If you become disabled before your full retirement age, you might qualify for Social Security disability benefits if you've worked and paid Social Security taxes in five of the preceding ten years.
- If you also get a pension from a job where you didn't pay Social Security taxes (e.g., a civil service or teacher's pension), your Social Security benefit might be reduced.

2. There is no marriage penalty or limit to benefits paid a married couple

- If you are married and both you and your husband have worked, you will each be paid your own Social Security benefit.
- A working woman is not limited to one-half of her husband's Social Security. (That rate applies to women who never worked outside the home.)
- So, for example, if you are due a Social Security benefit of $1,200 per month and your husband is due a Social Security benefit of $1,400 per month, you will be paid
  $2,600 per month in retirement benefits.

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356 SOCIAL SECURITY ADMINISTRATION, http://www.ssa.gov/sf/FactSheets/WomenandSSrev1.pdf (last visited May 28, 2015).

3. If you're due two benefits, you get the one that pays the higher rate, not both

- Most women are potentially due two benefits: your own retirement benefit and wife's benefit on your husband's record.
- But you only get the one that pays the higher rate, not both.
- A wife is due between one-third and one-half of her husband's Social Security.
- Most working women who reach retirement age get their own Social Security benefit because it's more than one-third to one-half of the husband's rate.
- But if your husband dies before you, you can apply for the higher widow's rate. (See number 5 below).

4. If you're divorced and were married at least 10 years, you're eligible for some of your ex's Social Security

- Divorced women married at least 10 years are eligible for Social Security on the ex-husband's record if they are unmarried at the time they become eligible for Social Security.
- Some women sign divorce decrees relinquishing their rights to Social Security on their ex-husband's record. If you were married at least 10 years, those clauses in divorce decrees are worthless and are never enforced.
- Any benefits paid to a divorced spouse DO NOT reduce payments made to the ex or any payments due the ex's current spouse if he remarried.
- Generally, the same payment rules apply to divorced wives and widows as to current wives and widows. That means most divorced women collect their own Social Security while the ex is alive, but can apply for higher widow's rates when he dies.

5. When your husband (or ex dies), you're probably due a widow's benefit

- Widows are due between 71 percent (at age 60) and 100 percent (at full retirement age) of what the husband was getting before he died.
- But we must pay your own retirement benefit first, then supplement it with whatever extra benefits you are due as a widow, to take your Social Security benefit up to the widow's rate.
- We also can pay you a $255 one-time death benefit if you were living with your husband when he died.
- If you made more money than your husband, then he might be due a widower's benefit on your record if you die before he does.

Effect of Remarriage—Widow(er)'s Benefits[357]

406.1 ***Does The Remarriage Of A Widow(Er) Or Surviving Divorced Wife Or Husband Affect Widow(Er)'S Benefits?***

Your remarriage *after age 60* does not prevent you from becoming entitled to benefits on your prior deceased spouse's Social Security earnings record.

406.2 ***Does The Remarriage Of A Disabled Widow(Er) Or Surviving Divorced Wife Or Husband Affect Widow(Er)'S Benefits?***

Your remarriage does not prevent you from becoming entitled to benefits on your prior deceased spouse's Social Security earnings records as long as:

A. Your remarriage occurs after you turn 50; and
B. Your remarriage occurs after you become disabled.

NOTE: If you remarry *before you turn 50*, you will not be entitled to survivor's benefits, unless the marriage ends.
Entitlement is not affected if you enter into a same-sex marriage or union. The Social Security Administration does not recognize the marriage for benefit purposes.

406.3 ***How Does Remarriage Of A Widow(Er) Or A Surviving Divorced Wife Or Husband Before Age 60 Affect Widow(Er)'S Benefits?***

If you remarry before age 60, you will not be entitled to survivor's benefits, unless:

A. Your subsequent marriage ends, whether by death, divorce, or annulment; or
B. Your marriage occurred after age 50 and you were entitled to benefits as a disabled widow(er) or disabled surviving divorced spouse.

406.4 ***How Does The Termination Of A Remarriage Of A Widow(Er) Or Surviving Divorced Wife Or Husband Before Age 60 Affect Widow(Er)'S Benefits?***

If you remarry before you turn 60 and that marriage ends, you may become entitled or re-entitled to benefits on your prior deceased spouse's earnings record. Your benefits begin the first month in which the subsequent marriage ended if all entitlement requirements are met. If the remarriage was absolutely void or was annulled from the beginning, see §1853.

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357 HANDBOOK, SOCIAL SECURITY ADMINISTRATION § 406, *available at* https://www.socialsecurity.gov/OP_Home/handbook/handbook.04/handbook-0406.html (last visited June, 2, 2015).

U.S. Department of Health and Human Services

Spouses of Medicaid Long-Term Care Recipients

Thomson/MEDSTAT

April 2005

PDF Version

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This policy brief is one of five commissioned by the Department of Health and Human Services, Office of the Assistant Secretary for Planning and Evaluation on Medicaid eligibility policies for long-term care benefits. This brief outlines the Medicaid rules that affect community spouses of nursing home residents and widows or widowers of deceased nursing home residents. The remaining four briefs address: Medicaid Treatment of the Home; Medicaid Estate Recovery programs; Medicaid Liens; and A Case Study of the Massachusetts Medicaid Estate Recovery Program.

INTRODUCTION

When an individual enters a nursing home for the long term, the spouse remaining in the couple's home may fear financial devastation from paying the high cost of nursing home care. However, Medicaid rules have been designed to protect certain income and assets for the at-home spouse, without affecting the nursing home spouse's eligibility for publicly funded long-term care. While some may view the amounts that are protected as quite modest or even inadequate to sustain the at-home spouse's accustomed standard of living, they far exceed the income and asset levels that may be retained in the case of unmarried recipients of Medicaid long-term care services. Moreover, at-home spouses can employ a variety of financial planning strategies to preserve an even greater share of the marital assets, even after the Medicaid recipient's or spouse's death. While states are required to recover Medicaid long-term care expenses from the estates of deceased recipients, when there is a surviving spouse, the recipient's estate often escapes this outcome.

BASIC MEDICAID RULES GOVERNING INCOME AND ASSET LIMITS FOR MARRIED COUPLES

Medicaid eligibility is generally determined using the same income and asset provisions used for determination of eligibility for benefits from the Supplemental Security Income (SSI) program -- the Federal income maintenance program for poor elderly and disabled persons.[1] However, some states (the eleven so-called 209(b) States)[2, 3] employ more restrictive Medicaid eligibility criteria than are used in the SSI program, while certain other states may use more generous rules.[4] In addition, when one spouse applies for or receives Medicaid coverage of nursing home care while the other spouse remains in the community, the so-called "spousal impoverishment" rules[5] disregard a certain amount of income for the financial support of the at-home spouse.

Basic Medicaid income and asset eligibility rules for married couples:

1. All income and assets (his, hers and theirs) are combined, regardless of ownership, including things that are often the sole legal property of just one spouse -- for example, retirement savings accounts or pension checks.

2. If either spouse has an interest in property with a legal right to sell, claim or cash it out in some manner to obtain money for his or her personal use, then the fair market value of that property is counted to the extent of the spouse's legal right to convert it to cash.

3. The rules for couples living apart differ from those for couples living together, as the income of a community spouse is not considered to be available to an institutionalized spouse. Medicaid rules encourage married couples to choose nursing home rather than in-home care for an ill spouse in order to preserve additional income and marital assets for use by the community spouse.[6]

Recipients of Medicaid long-term care services in nursing homes are expected to use their income to pay a share of the cost of their nursing home care. Medicaid then pays the difference between the recipient's share of cost and the Medicaid payment rate. So-called "post-eligibility rules" (which apply to nursing home residents once they are determined to be eligible for Medicaid) are used to calculate how much of the institutionalized spouse's income must contribute toward his or her cost of care and how much may be protected for use by the community spouse.[7]

Married Medicaid nursing home residents may retain:

- A personal needs allowance of at least $30 (or more at state option)
- Unrestricted amounts for health insurance premiums or out-of-pocket medical expenses not covered by Medicaid
- At state option, a time-limited allowance to maintain the recipient's home if a physician determines that he or she is likely to return home within 6 months

- Income and/or assets sufficient to avoid impoverishment of the community spouse

In addition, ownership of certain assets does not affect the Medicaid eligibility of married couples.

Assets that are excluded when determining Medicaid eligibility of married couples:

- The first $3000 of assets if they live as a couple or $2000 each if they live apart
- The couple's home
- Limited amounts of household goods and personal property
- A vehicle
- Up to $1500 in funds designated for burial expenses, and contracts, spaces, or other irrevocable burial arrangements without limits for each spouse
- Life insurance with cash surrender value of less than $1500
- Certain income-producing property

Ownership of assets in excess of those listed above make an individual ineligible for Medicaid. However, the person may qualify at a later date after the excess is depleted, either by spending it down on medical bills or other necessary personal expenses, or by employing various financial planning strategies. Such strategies are more varied and numerous for married couples because they can take advantage of special provisions to protect additional resources for persons separated from their spouses by a long-term stay in a nursing home or other medical institution.

MEDICAID INCOME AND ASSET PROTECTION FOR THE COMMUNITY SPOUSE

Medicaid law was amended in 1988[8] in response to evidence that at-home spouses[9] -- typically elderly women with little or no income of their own -- faced poverty and a radical reduction in their standard of living before their spouses living in a nursing home could qualify for Medicaid. The so-called Medicaid "spousal impoverishment" provisions protect the community spouse when the institutional stay of the nursing home resident has lasted or is expected to last at least 30 consecutive days. This protection ceases if the institutionalized spouse is discharged and returns home or to another non-institutional setting. States must apply Medicaid spousal impoverishment rules "irrespective of state laws regarding community property or division of marital property."[10]

In some cases, states extend spousal impoverishment protections to the non-Medicaid spouses of recipients of Medicaid Home- and Community-Based Waiver services.[11] However, the law does

not extend these protections to couples in which both spouses receive Medicaid long-term care services.

PROTECTED MARITAL INCOME

Federal law prescribes income protection of a minimum maintenance needs allowance (MMNA) for the community spouse. Federal law prescribes that the MMNA should equal at least 150% of the federal poverty level for a couple ($1505 per month in 2004) and be adjusted every year by the general rate of inflation.[12] States have the option to use a higher minimum level -- $2319 per month. In 2000, 35 states used this higher figure.[13]

Medicaid rules provide three pathways for community spouses to obtain a higher MMNA. First, the allowance may be raised (though only as high as the Federal maximum allowance) for community spouses who show that they have exceptional housing costs, defined as more than 30% of the standard allowance. Second, they can receive a larger allowance if a state Medicaid hearing finds that exceptional circumstances might otherwise cause them extreme financial hardship. Third, they may seek a court order for additional support.[14]

A couple's total income is divided into his and hers by the "name on the check." This includes pension benefits, IRA payouts, or other income paid only to the account holder, and accessible by the spouse only if deposited in a joint account. Income the couple receives jointly is divided in half. The community spouse keeps all of his or her own income plus half of any shared income. If this total is less than the MMNA, then the institutionalized spouse must be allowed to supplement the community spouse's income in an amount that increases the community spouse's total income up to the applicable MMNA. If the income level of the community spouse is very low, he or she may receive all of the combined marital income. Conversely, a community spouse with a high total income may receive little or no supplementary income from the institutionalized spouse. In such a case, even if the income of the community spouse is considerable, the Medicaid program cannot require that any of it be applied toward the cost of the institutional spouse's care. Income remaining to the institutionalized spouse after he transfers the allowed amount to the community spouse is subject to the usual Medicaid post-eligibility share-of-cost requirements.[15]

PROTECTED MARITAL ASSETS

Medicaid rules that protect marital assets for the community spouse require that all the couple's countable assets are first added together, regardless of whose name appears on the title. From that total, Medicaid subtracts an amount to be retained by the community spouse, plus a small amount (usually $2000) for use by the institutionalized spouse. Any remaining assets must then be depleted in order to qualify the institutionalized spouse for Medicaid long-term care services. The couple may deplete these excess assets by spending them down on the cost of nursing home care or by using them in ways described later in this issue brief.

The process begins with a resource assessment in which a snapshot is taken of all countable assets owned by the couple at the time of admission of the ill spouse to the nursing home, even if the Medicaid application is not filed until later. The snapshot does not include assets normally excluded during Medicaid eligibility determination, such as the couple's home or personal effects. Either spouse has the right to request the assessment immediately upon admission to the nursing home or at any time thereafter. If the couple does not request an assessment, the State is required to perform an assessment at the time when the institutional spouse applies for Medicaid. Nursing homes must inform all new admissions about the availability and implications of the asset assessment, including those who have not expressed an interest in applying for Medicaid services upon admission. Couples who choose not to be assessed upon admission may encounter problems later on with collecting the necessary documentation to recreate a snapshot of what their countable assets were at the time of admission.

When the Medicaid application is filed, the State uses information obtained from the resource assessment to calculate the community spouse's share of the couple's total assets. The calculation begins by dividing the total assets in half and assigning one half to each spouse. The community spouse's half share of the total is then compared to the State's minimum and maximum spousal allowance amounts. If this half share is less than the minimum, he or she is allowed to keep more than a half share to boost that protected share up to the minimum level. If the half share of total assets is greater than the maximum allowance, then the share protected for the community spouse is limited to the maximum amount, and he or she retains less than half of the total assets. Once the spousal allowance is calculated, it is up to the couple to work out the allocation of specific assets.

Federal law determines the minimum and maximum protected resource amounts ($18,552 and $92,760, respectively, in 2004).[16] States have the option to raise the minimum to any level up to the Federal maximum. In 2000, 36 states opted to raise their minimum levels, most of them setting the minimum equal to the Federal maximum.[17]

The community spouse may be able to retain more than the maximum protected amount by: 1) obtaining a court order for more; 2) requesting a hearing to petition for an amount sufficient to generate income consistent with Medicaid income protection guidelines for spouses;[18] or 3) "just saying no"[19] -- i.e., by taking sole ownership of marital assets and refusing to make any of them available to pay for the institutionalized spouse's care. In this case, the institutional spouse may be unable to qualify from Medicaid because he or she is prevented from spending down the designated share of the marital assets. However, the State may make a determination of hardship in order to provide Medicaid benefits, or may pursue assets in possession of the community spouse under general state laws regarding marital support obligations.

FINANCIAL PLANNING STRATEGIES TO PRESERVE ADDITIONAL MARITAL ASSETS

General financial strategies used to shelter assets in order to qualify for Medicaid have been well documented.[20] They are legal and particularly amenable for use by married couples who wish to

preserve marital assets in amounts greater than those protected for use by the community spouse under the Medicaid spousal impoverishment rules.

The ethics of such strategies are beyond the scope of this issue brief. Arguably, married couples separated by long-term institutionalization of one spouse have more motives and opportunities for sheltering assets than do individuals without living spouses. Couples seek to avoid serious and potentially long-lasting financial harm to the community spouse, who is likely to outlive the institutionalized spouse. In addition, income support from the institutionalized spouse may decrease or even end at death. In contrast, the goal of individuals without spouses is more likely to preserve assets and improve the financial circumstances of able-bodied adult children or other heirs. Limited evidence suggests that asset transfers are more frequent among married couples than among individuals without living spouses,[21] and that opinions on the ethics of asset transfers by married couples are more numerous and complicated by subtle differences.[22]

By using up assets or converting them into another form of equal value that may not be counted when determining Medicaid eligibility, the institutionalized spouse, having retained fewer assets to spend down, may qualify for Medicaid long-term care assistance sooner. In this scenario, the long-term financial prospects of the community spouse may also be improved by eliminating certain future expenses.

TRANSFERRING ASSETS TO THE COMMUNITY SPOUSE

The general rule is that Medicaid coverage of nursing home and certain other medical care is denied for a period of time if an applicant or his or her spouse transfers asset and fails to receive full and fair market value in return.[23] This provision also includes transfer of the individual's home, an asset normally excluded in determining Medicaid eligibility. The State penalizes uncompensated or inadequately compensated asset transfers occurring as far back as 36 months before a Medicaid application is filed (60 months for assets transferred into a trust). The penalty begins when the transfer takes place -- a time that may precede the person's admission to a nursing home and/or filing of a Medicaid application. The penalty period is equivalent to the number of months of nursing home care that the transferred assets could have paid for at the private-pay rate.

Medicaid rules on asset transfers between spouses, or to a third party for the sole benefit of one spouse, are more complicated. They allow such transfers without penalty and without limits. Yet, if either spouse transfers assets to another party without receiving fair market return, the institutionalized spouse stands to lose Medicaid coverage of nursing home care.

USING ASSETS TO PAY PAST OR FUTURE BILLS

By using marital assets to pay bills prior to applying for Medicaid assistance, the community spouse can reduce demands on the assets he or she is allowed to keep under Medicaid spousal impoverishment rules. The couple may elect to pay off existing debts; to prepay real estate, insurance, or other large bills; or to prepay funeral expenses.

BUYING ASSETS THAT MEDICAID DOES NOT COUNT

As explained above, Medicaid eligibility rules do not count certain assets such as a home, a car, or personal effects. Therefore, a spouse might be advised to take money from countable savings to buy a more expensive home; repair or improve an existing home; or buy a new car, new household furnishings, or personal effects. Medicaid rules do not restrict conversions of countable assets into non-countable ones of equivalent value. Unlimited amounts of money can be spent on non-countable assets for the community spouse's use while getting Medicaid to pay for long-term nursing home care.

EXCHANGING ASSETS FOR SOMETHING OF EQUAL VALUE

Some strategies are designed to convert assets into income or an income equivalent for use by the community spouse. In order to avoid a Medicaid penalty or compromise coverage for the institutionalized spouse's long-term care needs, the community spouse must receive something of equal value in exchange for the transferred assets. Applying this concept to specific Medicaid cases may require considerable financial sophistication. It may be difficult both for states to be consistent in the way they address this issue and for elderly people and their financial advisors to accurately anticipate the Medicaid consequences of such asset exchanges. The confusion is exacerbated by numerous, varied and constantly evolving conversion strategies, which are also widely used in retirement planning for purposes unrelated to Medicaid long-term care.

Annuities are an increasingly popular conversion strategy. They are contractual arrangements in which an individual pays a lump sum, which may be from general savings or retirement accounts such as an IRA or 401(k), to receive a future stream of income in return. They are offered in a bewildering variety of forms by commercial financial entities, and often are associated with poorly understood consequences and costs to the consumer.[24] "Medicaid annuities" are heavily advertised on the Internet and presumably are designed to avoid potential Medicaid pitfalls.

Couples anticipating the need for long-term care for one spouse can protect unlimited assets by using them to buy an annuity that names the non-Medicaid spouse as beneficiary.[25] Although savings are immediately and substantially reduced, the community spouse's income is increased by a more modest but recurring amount. The at-home spouse can either spend that income or reinvest it, effectively recouping most of the assets used to purchase the annuity. Medicaid rules require the annuity's return to be commensurate with a reasonable, actuarially sound estimate of the life expectancy of the annuity beneficiary.[26] Annuities failing this test may result in a finding by the State that an uncompensated asset transfer has occurred, which triggers a penalty in the form of denial of Medicaid coverage of long-term care benefits for the institutionalized spouse. The duration of the penalty is based on the portion of the promised stream of income that is beyond the individual's predicted life expectancy.

Less common financial strategies for sheltering assets are life estates, family reverse mortgages, and care agreements. These arrangements are similar to annuities in that assets are exchanged for something of value in a non-commercial context (for example, agreements with family members or other private parties). The return may be in the form of income payments, use rights in the case of a life estate consisting of the home,[27] or care-giving services. The keys to avoiding denial or delay of Medicaid coverage are: 1) to have clear documentation to show that the exchange agreement was made before applying for Medicaid assistance; and 2) to describe how the Medicaid applicant or the spouse receives income or services of equivalent value from the party to whom the assets were transferred.[28]

MEDICAID RULES REGARDING WIDOWS OR WIDOWERS OF LONG-TERM CARE RECIPIENTS

Medicaid requires states to recover expenses for Medicaid financed long-term care services from the estates of persons who received these services after they reached age 55 or who, regardless of age, were determined by the state to be permanently institutionalized.[29] The major exception to this general rule is that estate recoveries are prohibited during the lifetime of a surviving spouse.[30] However, states have the authority to recover from the estate of the recipient's widow or widower, although many of them defer such recoveries or waive them altogether.[31] Further, states that do recover from the estate of a surviving spouse may elect to impose a lien on the home to protect the State's right to be informed and make a claim against the home upon his or her death. A Medicaid claim on behalf of the recipient may only be made on the estate of the surviving spouse if that estate includes countable assets. However, states may not interfere in any way with use or disposal of property, including the home, during the lifetime of the surviving spouse, who may freely spend it, sell it, or give it all away without concern for a Medicaid claim.[32] Of course, this freedom from Medicaid financial consequences ends if the surviving spouse also applies for Medicaid, at which point he or she becomes subject to Medicaid rules and penalties for transferring assets without receiving a fair market return.

CONCLUSION

Medicaid rules are designed to protect sufficient income and resources for the community spouse of a nursing home resident to avoid undue hardship, without compromising the institutionalized spouse's ability to qualify for Medicaid long-term care services. Sufficiency, institutional bias, and equity are three areas of concern to address in evaluating how well these rules accomplish their admirable goals.

On the matter of *sufficiency*, some would argue that the rules do not protect enough and that community spouses are well advised to exploit every legal financial strategy to shelter additional income and assets. Others argue that these opportunities should be limited so that Medicaid, a program for the poor, can target its funding toward people with even greater financial needs.

On the matter of *institutional bias*, spousal protections are primarily available only when one spouse enters a nursing home. This may encourage couples to choose nursing home care in lieu

of home- and community-based services, even though most couples would prefer to remain together in their own home. Although access to such services is more limited than access to nursing home care in many communities, the cost of care for the ill spouse in the community may be considerably less.

On the matter of *equity*, it is reasonable to ask why Medicaid gives special income and asset protections to some, but requires others (couples living together or persons without living spouses) to be impoverished before they can qualify for long-term care assistance. How these concerns will be addressed in the future, and at what cost, remains to be seen.

NOTES

1. SSI rules on income and assets are described in Title 20 of the Code of Federal Regulations at: http://www.access.gpo.gov/nara/cfr/waisidx_02/20cfr416_02.html. For income, see Subpart K, beginning at section 416.1100. See especially section 416.1160 on deeming of income support between spouses. For resources, see Subpart L, beginning at section 416.1201. Detailed rules are in the SSA Program Operations Manual System, Sections SI 008 and SI911 at: http://policy.ssa.gov/poms.nsf/poms?OpenView&Start=1&Count=50&Expand=5.4t.
2. *Groups Deemed to be Receiving SSI for Medicaid Purposes*. Technical Assistance Series for Medicaid Services to Elderly or People with Disabilities. Disabled and Elderly Health Programs Group. Center for Medicaid and State Operations. June 12, 2002. Disability and Aging TA Series #01 at: http://www.cms.hhs.gov/medicaid/eligibility/ssideem.pdf. Access state-specific information from the State Medicaid plan for each state at: http://www.cms.hhs.gov/medicaid/stateplans/.
3. They are Connecticut, Hawaii, Illinois, Indiana, Minnesota, Missouri, New Hampshire, North Dakota, Ohio, Oklahoma and Virginia, according to: Kassner, E. and Shirey, L. *Medicaid Financial Eligibility for Older People: State Variations in Access to Home and Community-Based Waiver and Nursing Home Services*. Report No. 2000-06. AARP Public Policy Institute. April 2000 at: http://research.aarp.org/health/2000_06_medicaid.pdf.
4. Section 1902(r)(2) of the Medicaid statute permits states to use less restrictive income and resource methodologies in determining Medicaid eligibility. Federal guidance is provided at: http://www.cms.hhs.gov/medicaid/eligibility/elig0501.pdf. Obtain state-specific information from individual state Medicaid plans at: http://www.cms.hhs.gov/medicaid/stateplans/.
5. Section 1924 of the Social Security Act; U.S. Code Reference 42 U.S.C. 1396r-5.
6. Kassner and Shirey. April 2000 at: http://research.aarp.org/health/2000_06_medicaid.pdf.
7. Regulations on the recipient's post-eligibility share of cost are in Title 42 of the Code of Federal Regulations, Chapter 435.700, Subparts H and I at: http://www.access.gpo.gov/nara/cfr/waisidx_02/42cfr435_02.html. Detailed guidance is found in Chapter 3 of the State Medicaid Manual at http://www.cms.hhs.gov/manuals/45_smm/sm_03_3_toc.asp. See Sections 3700-3714 for overall rules, Section 3628.2 for post-eligibility rules as they affect the medically needy eligibility category, and Section 3590 as they affect individuals in Home and Community-Based Waiver programs.
8. The Medicare Catastrophic Coverage Act (MCCA) of 1988 (P.L. 100-360) added Section 1924 to Title XIX of the Social Security Act at: http://www.ssa.gov/OP_Home/ssact/title19/1924.htm. Detailed Federal guidance is in Chapter 3 of the State Medicaid Manual at: http://www.cms.hhs.gov/manuals/45_smm/sm_03_3_toc.asp. See Sections 3260-3263, 3702, and 3710-3714.
9. "Spouse" is defined under the law of the state of residence.
10. Chapter 3 of the State Medicaid Manual, Part 3261.1.
11. Chapter 3 of the State Medicaid Manual, Part 3710.
12. The spousal allowance is increased by one third for every minor or adult dependent child, or certain other dependents who live with the community spouse. The amount of income the institutionalized spouse can transfer to such dependents is reduced by any income they have in their own right.

13. Stone, J.L. *Medicaid: Eligibility for the Aged and Disabled*. Report to Congress. Congressional Research Service. Library of Congress. updated July 5, 2002. See Table 7.
14. Chapter 3 of the State Medicaid Manual, Part 3713-4.
15. Note that "spousal impoverishment" rules on income apply post-eligibility but not in determining eligibility. As a result, income intended to be set aside for the community spouse is not set aside when determining the eligibility of the institutionalized spouse (See Section 3261.1 of the State Medicaid Manual). This may cause some institutionalized spouses to have too much income to qualify for Medicaid, though not enough to cover the cost of care and support of the community spouse. There is no data on whether or how often this hypothetical outcome actually occurs.
16. These are described at: http://www.srskansas.org/services/DivisionofAssets.htm.
17. Stone, J.L. *Medicaid: Eligibility for the Aged and Disabled*. Report to Congress. Congressional Research Service. Library of Congress. updated July 5, 2002. See Table 7.
18. States are permitted to use the so-called "income first" rule, which limits the amount of additional resources that the community spouse may petition for to an amount commensurate with current income, including income transferred from the institutionalized spouse. If the income of the institutionalized spouse disappears at death, assets owned by the community spouse alone may not be able to maintain his or her income at its previous level. This state policy option has been confirmed by the Supreme Court in *Wisconsin Department of Health and Human Services v. Blumer* at: http://supct.law.cornell.edu/supct/html/00-952.ZS.html. A synopsis of this decision is presented at: http://www.oyez.org/oyez/resource/case/1446/. For a discussion about determining the amount of assets necessary to produce a given amount of monthly income, see: http://www.elderlawanswers.com/resources/s7/r33487.asp.
19. A simple description of "just say no" or "spousal refusal" is at: http://www.elderlawanswers.com/resources/s8/r33572.asp#9. Note that the "just say no" strategy is only successful if the State does not pursue legal action against the community spouse to recover the assets.
20. For an overview of financial planning techniques used to bypass the standard Medicaid rules, see Burwell, B. and Crown, W.H. *Medicaid Estate Planning in the Aftermath of OBRA '93*. The Medstat Group. August 1995. For information on protecting the home from estate recovery, see Goldfarb, D. *The Homestead and Medicaid Planning* at: http://www.seniorlaw.com/homestead-medicaid.htm. Elder law information on Medicaid viewed in the broader context of estate planning is at: http://www.elderlawanswers.com/resources/s8/r33572.asp. Advice for both laypersons and attorneys is provided by Budish, A.D. (1995). *Avoiding the Medicaid Trap: How To Beat the Catastrophic Costs of Nursing- Home Care*. Henry Holt & Company. State-specific advice for attorneys and financial planners is widely available on the Internet.
21. Walker, L., Gruman, C. and Robison, J. (1998). Medicaid Estate Planning: Practices, and Perceptions of Medicaid Workers, Elder Law Attorneys, and Certified Financial Planners. *Gerontologist* 38(4): 405-411.
22. Curry, L., Gruman, C. and Robison, J. (2001). Medicaid Estate Planning: Perceptions of Morality and Necessity. *Gerontologist* 41(1): 34-42.
23. For general Medicaid rules on transfer of assets, see the State Medicaid Manual, Chapter 3, Part 3258. For asset transfers between spouses, see Parts 3252, 3258.10 and 3262.4.
24. Annuities are analyzed, with ample attention to consumer cautions and potential negatives consequences, at: http://www.efmoody.com/insurance/insuranceoverview.html.
25. A report by state Medicaid directors identifies annuities purchased for non-Medicaid spouses as a particular problem area. See Coates, A., Deily, M. et al. *The Role of Annuities in Medicaid Financial Planning: A Survey of State Medicaid Agencies*. Prepared by the Annuities Work Group of the Eligibility Technical Advisory Group of the National Association of State Medicaid Directors for the American Public Human Services Association. October 2003. at: http://nasmd.org/Annuities%20Workgroup%20Product_October%202003.pdf.
26. Federal Medicaid guidance on annuities is provided in Chapter 3 of the State Medicaid Manual, Part 3258.9.B at: http://www.cms.hhs.gov/manuals/45_smm/sm_03_3_3257_to_3259.8.asp#_3258.9.
27. Federal guidance on life estates is in Chapter 3 of the State Medicaid Manual, Part 3258.9.

28. Federal rules are wary about attributing cash value to care-giving services by family members that would be given out of affection and without expecting compensation, in the absence of Medicaid rules. The rules defer to states on what constitutes acceptable documentation. See Chapter 3 of the State Medicaid Manual, Part 3258.1.A.1.
29. Section 13612 of P.L. 103-66 imposed the Medicaid estate recovery mandate by amending Title XIX of the Social Security Act, accessible at: http://www.ssa.gov/OP_Home/ssact/title19/1917.htm. Detailed Federal guidance to states is in the State Medicaid Manual, Chapter 3, Section 3810 at: http://www.cms.hhs.gov/manuals/45_smm/sm_03_3_3800_to_3812.asp#_3810. Note that Medicaid recoveries take place within the context of state property and inheritance laws, and are influenced by options chosen by each state to define the scope of its Medicaid recoveries and implementation methods.
30. States are also prohibited from recovering if there is a surviving child who is under age 21, blind, or permanently disabled, and in certain cases where an adult child or sibling lives in the deceased recipient's home.
31. Only 9 of 34 states responding to one study reported always collecting from the estates of surviving spouses. See Table 6 of the report prepared for the AARP Public Policy Institute by Sabatino, C.P. and Wood, E. *Medicaid Estate Recovery: A Survey of State Programs and Practices*, September 1996.
32. This was confirmed in a recent court case. See *Nevada Department of Human Resources v. Estate of Ullmer* (120 Nev. Adv. Op. No. 16. April 1, 2004) at: http://www.leg.state.nv.us/scd/120NevAdvOpNo16.html.

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Policy Briefs on Medicaid Eligibility Policies for Long-Term Care Benefits

A total of six Policy Briefs are available from the Office of Disability, Aging and Long-Term Care on this subject:

- **Medicaid Estate Recovery** [http://aspe.hhs.gov/daltcp/reports/estaterec.htm] Posted May 2005
- **Medicaid Estate Recovery Collections** [http://aspe.hhs.gov/daltcp/reports/estreccol.htm] Posted February 2006
- **Medicaid Liens** [http://aspe.hhs.gov/daltcp/reports/liens.htm] Posted May 2005
- **Medicaid Liens and Estate Recovery in Massachusetts** [http://aspe.hhs.gov/daltcp/reports/MAliens.htm] Posted May 2005
- **Medicaid Treatment of the Home: Determining Eligibility and Repayment for Long-Term Care** [http://aspe.hhs.gov/daltcp/reports/hometreat.htm] Posted May 2005
- **Spouses of Medicaid Long-Term Care Recipients** [http://aspe.hhs.gov/daltcp/reports/spouses.htm] Posted May 2005