

Be careful with divorce finances or you may get burned

Part 1 of 2

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Johnny Carson once said that the difference between divorce and legal separation is that a legal separation gives a husband time to hide his money. They say that true humor has to have an element of truth in it and Johnny was definitely speaking from experience!

It's a lot easier to fall in love than to untangle a marriage, especially from a financial perspective. One of the biggest mistakes I find people make is to forgo getting solid financial advice in an effort to save money. This can be very hazardous to your bank account, not to mention everything else you own! Below is a list of some areas for divorcing couples to consider – absolutely free! Use it as a guide for asking questions at your next advisor appointment.

Alimony and child support are *not* created equally!

Alimony is deductible to the payor and taxable to the receiver, child support is neither. But there are rules attached to both that you need to know. To qualify as alimony, certain requirements must be met (I'll cover child support in next month's article):

- The payment must be received by a spouse under a divorce or separation instrument.
- You and your ex-spouse must live apart (I know, it's hard to believe, but it happens!)
- Your documents should stipulate that payments terminate upon death of the recipient.
- Do not refer to dependents in determining alimony terms.
- You cannot "front-load" the alimony (discuss this with your financial advisor)
- Payments must be by cash or check, not in property or use of property
- Payments to a third party on behalf of your spouse under the terms of your divorce or separation instrument, however, can be alimony, if they otherwise qualify
- Be sure to keep written records of support paid (and received). In the event of a dispute, these records will be indispensable.

How's your health (insurance)?

If you are covered through your husband's job, you may be able to include continued coverage in settlement negotiations. If that is not an option, you can continue group coverage for up to 36 months under COBRA if your ex-husband works for a COBRA-qualifying business. The law states that your cost cannot exceed 102% of the employer's cost for the insurance. Learn more by calling the Department of Labor at 866/444.3272.

Property settlements

Property divisions can have disastrous consequences if you don't plan. Here are a couple of examples:

- Your residence: Because up to \$500,000 of the gain may be non-taxable upon the sale of your house, the person who keeps it may have a tax advantage.
- Retirement accounts: Boy, is this a sore spot with divorcing couples! Often a person is entitled to as much as 50% of the ex-spouse's pension, IRA, etc. It is *imperative* to get solid advice to handle the division advantageously. An ill-timed withdrawal could reduce your benefits by up to 50% or more! If you have the option between a fully taxable or a non-taxable account (Roth, for example), go for the non-taxable account.

There are many more property settlement areas and rules to consider – please be sure to see your financial advisor!

"Phantom" assets

Some assets aren't obvious. For example, I have seen spouses overpay tax estimates by significant amounts to conceal money. Therefore, it's a good idea to determine how any tax refunds will be split. Notes receivable, such as from a closely held business, are another example of assets

that aren't readily visible.

Unless otherwise agreed to, any tax overpayment is allocated according to the amount of tax paid by each spouse. The allocation of itemized deductions, especially if significant, should be accounted for as well.

The name game

- Be sure to remove your ex-spouse's name from your accounts (credit card, mortgage and auto loan) immediately. I also recommend, where feasible, to refinance any loans titled jointly.
- Before a divorce is finalized, it's especially important for both sides to review each other's recent credit history. Debt trouble surfacing during a breakup can cause big problems later.
- If you took your husband's surname during marriage and are now changing back to your maiden name, be sure to notify the Social Security Administration. Failure to do so can result in denial of tax benefits by the IRS – and a lot of headaches to get it straightened out.
- Don't forget to change beneficiaries in trusts, wills, investment accounts, IRAs, powers of attorney, pension plans, and life insurance policies. Otherwise, your ex-spouse may have a really good reason to dance on your grave!

Help from the IRS

IRS Publication 504 is full of information that can answer many of your questions. Even CPAs and CERTIFIED FINANCIAL PLANNERS™ use it as a reference guide!

I'm at my 900 word limit and have just scratched the surface of what you need to know. One universal truth to remember is that the emotions associated with a divorce do not generally encourage rational thinking, no matter how intelligent or accomplished you are. That's why it is so very important to hire an experienced financial advisor who will keep your best interests intact when your world is falling to pieces. Next month, we'll take a look at topics affecting taxes, with a focus on the complicated rules relating to children – support, tax credits, and more.

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