

# Morgan Stanley

PRIVATE WEALTH MANAGEMENT

## Life After Divorce: Planning Your New Future

Divorce is almost never easy. It can impact your life in complex and unexpected ways, particularly when it comes to your finances. The more you know and the better you understand your options, the more prepared you will be to make sound decisions. That will help you take control of your financial life and prepare the way for greater security and flexibility in the future.

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# Financial Separation

If you are not yet officially divorced, understanding the process and knowing the rules can reduce stress and make life easier. It can also help you protect your interests.

The legal landscape of divorce is well-mapped, and while there are intricate points of law that may have a bearing on your situation, you really only need to understand a few core concepts at the outset, especially when you have adequate counsel. What should you do in advance? How will property likely be divided? What advisors do you need? Divorce is seldom easy, but you can prepare for it—and when you do, it can go more smoothly and predictably than you may anticipate.

## WEATHERING DIVORCE

### Who Gets What?

The divorce process involves a financial separation as well as an emotional one. Which assets will you own following the divorce, and which will be owned by your former spouse?

In an uncontested and/or mediated divorce, the two of you may be able to divide your assets on your own, and then have that agreement memorialized by your attorneys. If future ownership is in dispute, however, a court may have to decide. How the judge will make that decision will depend largely on guidelines set out in state law. While specifics vary significantly from state to state, you should be aware of some key concepts, including marital and nonmarital property and equitable distribution.

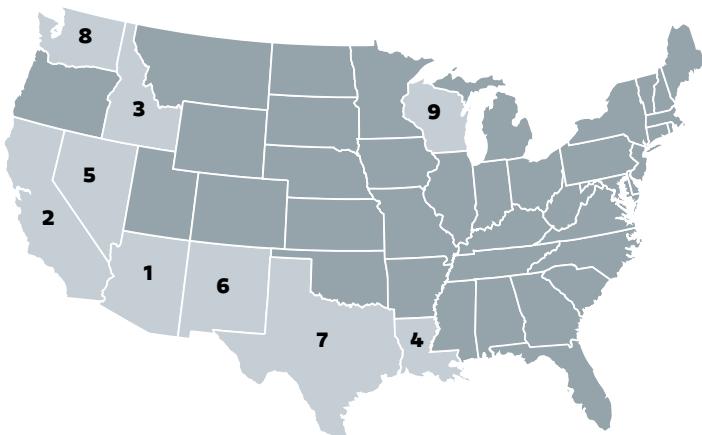
#### MARITAL VERSUS INDIVIDUAL/NONMARITAL PROPERTY.

Marital property includes virtually all property that you and your spouse acquired during the marriage: real estate, investments, bank accounts, art collections, cars, boats and so on. Almost anything owned by you and your spouse will be included except property that was:

- Given to one of you or that you inherited
- Acquired before marriage
- Acquired using property that was a gift, inherited or already owned before the marriage
- Excluded by a prenuptial or postnuptial agreement

You should discuss the issue of marital property carefully with your attorney, because it can become very complex depending on how nonmarital assets were combined and used during the marriage. What's more, appreciation of nonmarital property during your marriage may be considered marital

### COMMUNITY PROPERTY STATES



For illustrative purposes only

1	Arizona	4	Louisiana	7	Texas
2	California	5	Nevada	8	Washington
3	Idaho	6	New Mexico	9	Wisconsin

property under the theory of equitable appreciation in some jurisdictions.

#### DIVIDING MARITAL PROPERTY.

Most states will rely on the concept of *equitable distribution* in dividing marital property. The goal is to achieve a division that is fair based on a range of considerations, including the contribution of each spouse to acquiring and maintaining the marital property, the length of the marriage, needs related to child custody and the financial needs, circumstances and future prospects of each spouse. In a contentious divorce, it is important to have a knowledgeable divorce lawyer to ensure that all relevant factors are included in your case.

Another system that exists for dividing marital property is the "community property" approach, which is used in nine states. In these states, property is divided evenly between the spouses, regardless of how it came into the marriage or the projected financial needs of either spouse. Clearly, the classification of community property versus nonmarital property takes on

special importance in the division of assets. ■

### What About the House?

Deciding whether to keep or sell the house you've lived in and may have raised children in can be one of the most complex decisions you face. Few questions present such a tightly woven blend of emotional and financial issues.

**TO SELL OR NOT TO SELL?** Keep in mind that decisions involving your home or homes should not focus solely on value. You should also consider liquidity, cash flow and the cost of maintaining the asset once you own it. That can be a significant financial burden that may preclude other opportunities or needs. Alimony and child support may help, but they are likely to be time-limited. What will be best for your long-term interests? That's probably not an easy question to answer. An accountant may be useful when determining basis, value and taxation of assets. ■

## Don't Go It Alone

Going through a divorce can feel like a lonely process, which is all the more reason not to go it alone. Assembling a strong, experienced team of confidential professional and personal advisors—your personal board of directors—can provide critical guidance and support, helping you make more informed decisions while you approach the future with greater confidence. Consider building a team that includes:

**YOUR OWN LAWYER.** Yes, it is possible to get through a divorce without a lawyer, but usually it's not wise. Your lawyer takes on the responsibility of safeguarding your best interests and can deal objectively, unemotionally and forcefully with the many complex issues that typically arise. Plus, an experienced lawyer can offer you valuable perspective on the tough decisions you will have to make.

**YOUR OWN ACCOUNTANT.** Your tax filing status changes significantly as the result of a divorce. An accountant can advise you on matters such as income and capital gains taxes, gifts of marital

property, incidence of gift splitting during the marriage as well as any residual tax issues that may linger from your marriage.

### YOUR OWN PRIVATE WEALTH ADVISOR.

You and your spouse may have worked with a Private Wealth Advisor to help plan and manage assets during your marriage. Now you need a Private Wealth Advisor who can focus solely on you and your needs and plans—on a completely confidential basis. Your Private Wealth Advisor can help you understand the assets you own and your liquidity and cash flow issues as well as strategies for reaching long-term objectives such as educating a child or planning for retirement.

### YOUR OWN PERSONAL COUNSELOR.

Divorce is a legal, financial and emotional process. You may have encountered issues that you are less than comfortable discussing with a financial or legal advisor. That's where a therapist, clergyperson or other personal counselor can become invaluable, helping you deal with the complex, private and very human side of divorce. ■



## THE FAMILY BUSINESS

If you or your spouse owns a business, or if you started one together, it may be your marriage's most valuable asset. If it is a primary source of income for you and your spouse, it may not make financial sense to sell or liquidate it. Valuing your business in these circumstances is complex and likely to involve appraisals, income projections and significant analysis on the part of your respective accountants. Determining the most appropriate course of action will, in all likelihood, require extensive negotiation. However, operating agreements may include dissolution remedies. A review of all documents can be well worth it.

## INFORMATION IS POWER

When you have comprehensive, accurate information, your attorney can represent you more effectively, and you will be able to shape your own financial life more quickly. Try to assemble this information as early in the process as possible:

- Bank accounts or Cash Management accounts
- Financial statements
- Tax returns for the prior three years
- Investment/brokerage accounts and mutual funds
- Retirement (IRA, 401(k), etc.) and pension plans (both yours and your former spouse's)
- Social Security benefits statements
- Employee benefits coverage (health, dental, short-term disability and long-term disability for you and your former spouse)
- Military benefits
- Credit card statements
- Mortgage statements (including first and second mortgages and home equity line(s) of credit)
- Car, boat and other loans
- Loans you or your spouse may have guaranteed
- Prior taxable and nontaxable gifts to others
- Pending loan applications
- Lease agreements
- Purchase and sale agreements
- Employment agreements
- Partnership agreements
- Estate planning documents
- Will
- Living will
- Powers of attorney
- Trust documents (for trusts established by you or your spouse, and for trusts of which you are a beneficiary)
- Durable medical powers of attorney
- Life insurance
- Homeowner's insurance
- Umbrella liability
- Car insurance
- Long-term care
- Appraisals for art, collectibles, jewelry and other high-value items
- Donor-Advised Fund statements and/or family foundation documents

## What can you do right now?

1

**REVIEW YOUR CREDIT REPORT**

2

**ESTABLISH CREDIT  
IN YOUR NAME**

3

**OPEN YOUR OWN  
BANK ACCOUNT**

4

**CHANGE THE BENEFICIARIES  
ON KEY DOCUMENTS**

5

**CREATE A NEW,  
PRIVATE EMAIL ACCOUNT**

6

**SET UP YOUR OWN  
MAILING ADDRESS**

## Taking Control

You're in charge now, and you can take significant steps to build a secure financial life. One of the most important tasks is to review your credit score and take measures to build your credit as a financially independent person.

In all likelihood, your credit history is likely to be intertwined with that of your former spouse. As you work to separate your financial lives, it is important to establish and/or expand your own borrowing capacity. Credit can help you accomplish many goals now that you are independent, and it can be an important source of confidence and flexibility.

Credit is only one aspect of your personal financial life that deserves your immediate attention. The sooner you establish your own financial identity, the more comfortable you will be as you move forward. It's all part of being in control of a new financial life.

## WEATHERING DIVORCE

### Declaring Credit Independence

Using credit wisely and maintaining your good credit are important concerns at any time—but paying attention to credit is never more important than during and after your divorce.

Distractions and financial pressures can multiply during divorce, along with the likelihood of making late payments or missing them altogether. Managing your credit may be something new to you if your former spouse handled your family's finances, but it is a critical skill to develop when you are on your own.

**CHECK YOUR CREDIT REPORT.** A good credit report translates into financial flexibility. Equally important, credit scores are used by many types of organizations for purposes that extend beyond credit. For example, insurance companies and prospective employers may request authorization to review your credit reports as a qualifier for employment or coverage.

Note the word “reports.” There are three primary credit reporting agencies that monitor your credit: Equifax, Experian and TransUnion. You are entitled to request a free credit report from each of these agencies once a year. Because each company scores your credit and reports it slightly differently, it is important to check all three. Fortunately, that is not as complex or time consuming as it sounds. One easy and free way to start is to visit this government-approved website: [www.annualcreditreport.com](http://www.annualcreditreport.com).

Your credit report will be based on a number of factors, the most important being your payment history. If you and your spouse were both listed on an account, payment history for that joint account will influence your individual

credit score. That will continue to be true for as long as your name is associated with an account. You have the right to correct errors on your credit report, and it is important that you do so as quickly as possible—but you won’t know about the errors unless you request the report.

**PROTECT YOUR CREDIT.** Joint credit is usually not appropriate after divorce, since there is a risk that your credit rating can be damaged by the actions of your former spouse. One way to protect yourself is to close joint credit cards and other joint accounts. Remember, even after your divorce, if you signed the original credit application, you can be held responsible.

Here are the rules regarding joint accounts, as summarized by the Federal Trade Commission:

By law, a creditor cannot close a joint account because of a change in marital status but can do so at the request of either spouse. A creditor, however, does not have to change joint accounts to individual accounts. The creditor can require you to reapply for credit on an individual basis and then, based on your new application, extend or deny you credit. In the case of a mortgage or home equity loan, a lender is likely to require refinancing to remove a spouse from the obligation.

The creditor can require you to reapply for credit on an individual basis and then, based on your new application, extend or deny you credit.

**ESTABLISH YOUR OWN CREDIT.** If you work with a Private Wealth Advisor, he or she may be able to help you establish credit as part of that relationship. If your credit reports are strong, you may want to apply for credit cards and store accounts in your own name. A secured loan, such as an auto loan, is often a faster and easier way to establish an independent credit history than an unsecured account. ■

### Who Are Your Beneficiaries?

Chances are, when you were married, you named your spouse as primary beneficiary in your will as well as the beneficiary of your life insurance policies and retirement accounts.

Your spouse is probably also named in your other estate-planning documents, your IRA and insurance beneficiary designations, your medical directive and your power of attorney. It is a good idea to create a list of all of the relevant documents so you have current

## FACTORS INFLUENCING YOUR CREDIT SCORE

1

Your payment history, including individual and joint credit cards and accounts

2

The amounts you owe and how much credit you use

3

The number of recently opened accounts and recent requests for credit reports

4

Types of credit you use—for example, secured versus unsecured

information about who you have designated in each of these documents. While you may want to change these designations quickly, it is imperative that you get advice from your lawyer before doing so. Some states do not allow for changes during the divorce proceedings; and others won't recognize changes made just prior to the divorce. In certain cases, sanctions may be attached to changes that are made before a divorce is concluded. In fact, some changes require the consent of your former spouse even after the divorce becomes final.

The two documents you can and should change as soon as possible are your medical directive and your power of attorney. Otherwise, your soon-to-be ex will continue to be able to make medical or financial decisions for you in the event you are not able to do so. ■

### Borrowing From Your 401(k)

While not all 401(k) plans allow loans, a majority do. If you have a 401(k) plan through your employer, you may be able to borrow from it. It depends upon the provisions of your employer's plan—if it does allow loans.

In general, if your plan permits loans, you take a withdrawal and promise to repay it, with interest, over a fixed period of time. The plan and the Internal Revenue Code limit the amount of the loan(s) you can take; your plan administrator can provide you with more details. If you continue to repay the loan, withholding taxes and penalties will not apply.

Keep in mind, though, that if you have an outstanding loan balance at the time you end your employment, and if you do not or cannot make repayment arrangements, the loan is considered to be in default and the unpaid balance is considered to be a taxable distribution. ■

## UNDERSTANDING YOUR CREDIT SCORE

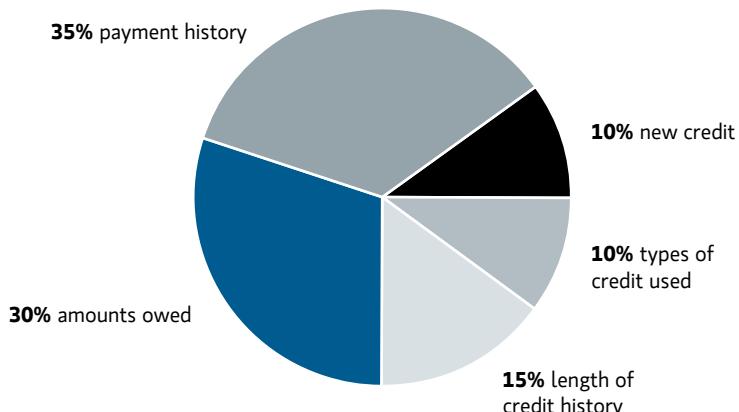
Understanding your credit rating is more complex than it used to be, now that there are two systems: the original FICO system, which provides purely numerical ratings; and the newer VantageScore system, which computes a different set of numbers and translates the score into a letter grade.

FICO, the better known and still more frequently used of the two systems, is an acronym for the Fair Isaac Corporation, which developed the credit scoring concept. The VantageScore system was developed by an independent corporation established by the three credit reporting companies: TransUnion, Experian and Equifax.

Because the two scoring systems are different, it is important to know which set of numbers (or numbers and letters) your lender is using to evaluate your credit.

### What's in Your FICO Score

*FICO scores are calculated from information contained in your credit report and grouped into five categories as shown in the chart below. The percentages reflect how important each of the categories is in determining your FICO score. (Source: <http://www.myfico.com/crediteducation/whatsinyourscore.aspx>)*



### What Your Score Means

Generally, the higher your credit score, the lower the risk you are likely to represent in the eyes of a lender. This table will give you an approximate idea of how your FICO score and VantageScore match up.

FICO	VANTAGESCORE		
Excellent	760–850	A	900–990
Very good	700–759	B	800–899
Good	660–699	C	700–799
Below average	620–659	D	600–699
Poor	580–629	F	501–599
Very poor	500–579		

(below 640 is considered "subprime")

For illustrative purposes only

**Know where your money comes  
from—and where it goes.**

Alimony  
Child Support  
Earnings and Bonus  
Investment Income  
Interest  
Trust Income

For illustrative purposes only

Budget





## Making It Work

The good news is you have more control over your finances than ever before. The less-good news is you may need to develop some new financial skills and habits.

Divorce can be disorienting, financially as well as emotionally. You may be moving from a world of two incomes to one. You and your former spouse will almost certainly be moving from supporting one household to paying for two. Your divorce decree is going to spell out things like alimony and child support, if they are relevant, but you still are going to be piecing together an unfamiliar financial puzzle.

For your own peace of mind, you will probably need to develop some new financial habits and disciplines. Budgeting may not have been a problem during your married life if cash flows were adequate or even ample. You may not have had to worry about the record keeping that goes along with paying income and property taxes, and maintaining the right levels of the right insurance could be something you thought little about.

Your accountant and Private Wealth Advisor can help you develop sound approaches for day-to-day management. Still, the reality is you are likely to play a more important role in your own financial life than ever before.

## WEATHERING DIVORCE

### Building a Budget

Knowing where you stand financially, especially when it comes to your cash flow, starts with a budget.

Even if you did not have a formal budget during your marriage, it may still be useful to create a predivorce budget now. If you are in the midst of the divorce process, an accurate prebudget can be a valuable negotiating tool and, if a court is involved,

it can help the judge evaluate alimony and child support needs. In addition, with predivorce and postdivorce budgets, you can compare income and outflows and begin to gauge any changes that divorce could make in your lifestyle.

At its most basic level, a budget adds up your sources of monthly income and then subtracts your monthly expenses. At a comprehensive level, however, a budget

can have dozens of line items. That may sound complex, but the more time you spend preparing your budget, the less likely you are to overlook sources of income. Fortunately, there are several excellent computer programs that can help you organize a budget and track variations from month to month. These programs can also help you organize the data you will need to file your tax returns (see below). ■

### WHAT'S IN A BUDGET?

It is easy to overlook items when putting together a comprehensive budget. Make sure you analyze each of these categories carefully.

<b>EARNED INCOME</b>		
<b>ALIMONY</b>	<b>TRANSPORTATION</b> Car Loan or Lease Gas	<b>BUSINESS AND PROFESSIONAL</b>
<b>INVESTMENT INCOME</b>		
<b>CHILD SUPPORT</b>	<b>MEDICAL</b> Physician Dentist/Orthodontist Elder Care/Parental Support Counseling	<b>TAX RELATED</b> Quarterly Estimated Payments Withholding Year-End Payments
<b>RENTAL/REAL ESTATE INCOME</b>		
<b>BANK INTEREST</b>		
<b>HOME</b> Mortgage or Rent Condo/Co-op Fees Home Loans Maintenance (landscaping, pool, snow plowing) Property Taxes	<b>CHILD EXPENSES</b> Sports/Music Lessons and Equipment Child Care/Nannies Gifts and Celebrations Camp Allowance	<b>INSURANCE</b> Life Home Auto Medical/Health Disability Long-Term Care Jewelry/Art/Collectibles
<b>UTILITIES</b> Telephone (both landlines and cell) Cable Internet Electricity Gas Water Garbage	<b>ENTERTAINMENT</b> Club Dues Restaurants Boat/Yacht Maintenance Vacations Electronics Movies Outings	<b>PHILANTHROPY</b> Charitable Contributions Board Give-Get Commitments Fundraising Events Foundation Expenses

For illustrative purposes only

## The Reality of Alimony

As with most things related to divorce, alimony laws vary from state to state. Fundamentally, however, alimony—also known as “spousal support”—is a monthly payment that one former spouse is required to make to the other as part of the divorce settlement. There are four types:

- Temporary support is paid during a separation before the divorce is final. It is likely to change, or cease altogether, depending on the final agreement.
- Rehabilitative support is also temporary in that it is designed to last until you become self-supporting.
- Permanent support lasts until the death of either former spouse, or until you remarry or begin living with another person. (Keep in mind that permanent alimony can be increased or decreased by a court, and that there has been recent discussion of reducing alimony when the paying spouse reaches retirement age.)
- Reimbursement is designed to repay you for specific expenses you helped pay during the marriage, such as the cost of medical or law school for your spouse.

Courts award alimony based on a number of factors, including how long you were married, your predivorce lifestyle (which makes a predivorce budget important), the disparity in earnings between spouses and the health of the receiving spouse. ■

**ALIMONY:** Spousal support payments are not tax deductible to the paying spouse and are not included in taxable income to the recipient spouse (different rules apply to pre-2019 divorce or separation agreements).

**CHILD SUPPORT:** Payments defined in the divorce agreement that are intended to support a child or children and are not tax deductible to the paying spouse and are not included in taxable income to the recipient spouse.

For more information, visit [www.irs.gov](http://www.irs.gov) and download IRS Publication 504.

## Tax Time

With divorce comes significant and complex changes to your income tax filing status and your tax return. It is very important that you discuss these changes with your own tax advisor or accountant.

Perhaps the most important tax subject, and certainly something central to your budget, is the cash flow provided by alimony and child support. Under a 2017 change to the tax laws, for post-2018 divorce or separation agreements, the amounts you receive as alimony are not taxable income to you and are not deductible for the payor spouse. That is similar to the tax treatment of child support payments. The impact of the tax treatment of these two types of payments can become a contentious topic in divorce, making it particularly important to get good advice before you finalize any agreement.

Additional issues you may encounter include:

- When it is appropriate and advantageous to consider filing a joint tax return with your spouse or former spouse.<sup>1</sup>
- Whether you can take advantage of filing as a head of household because a dependent lives with you.
- Claiming a child or children as dependents on your tax return. (In general, you must be the custodial parent, which may also allow you to claim certain deductions or credits as well.)
- Tax credits for child care and work-related expenses if your child is younger than 13.
- Deductions for a child's medical expenses. ■

<sup>1</sup> Generally, the divorcing couple's marital status on the last day of the year determines how they will file their income tax returns.

## INSIDE INSURANCE

### HEALTH INSURANCE

If you have been covered under your spouse's employer-provided plan, you have the right to continue coverage for a set period for a monthly fee following your divorce. This coverage, frequently referred to as COBRA, can be expensive and hence a topic of negotiation. Be sure to pay close attention to any related deadlines. Coverage for your children can be maintained under a qualified medical child support order (QMCOSO), which may require your former spouse to continue coverage under the employer plan.

### LIFE INSURANCE

If you are receiving child support payments—or your former spouse has agreed to pay or share future education costs—life insurance naming you as beneficiary can help make certain these obligations are met if your former spouse dies.

### DISABILITY INSURANCE

Disability income insurance can help make sure your former spouse can continue to meet financial obligations to you and your children. In addition, if you work, you may want to purchase a policy that helps protect your personal income.

### AUTO INSURANCE

It may make economic sense to continue to insure vehicles belonging to you and your former spouse under the same policy. If you do, make sure that all information—like registered owners and new addresses—is updated with the insurer. Note that costs are likely to increase.

### HOME INSURANCE

If you will take full ownership of your home after the divorce, be sure to remove your former spouse from the policy. The same applies for any insurance riders you have to cover high-value art, jewelry and collectibles.

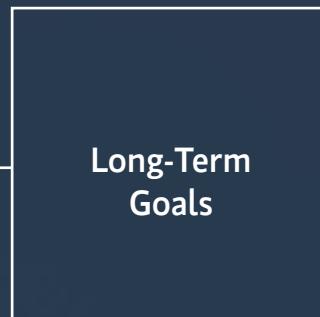
## The Long View

Achieving your long-term goals, whether they are educating a child or retiring comfortably, depends more than ever on you.

While you were married, it may have been easier to focus on retirement plans or college costs. These may have felt like shared goals, and you may have been on a more comfortable financial footing. Divorce can complicate the future, but with good advice and sound planning, you can make things happen—and you can do it your way.

As a single person, you can arrange to have your money managed in the way that makes the most sense for you—for your objectives, comfort level with risk and time horizon—because it's your money. You can also take advantage of plans that offer tax-deferred, or even tax-free, investment earnings potential as you pursue retirement goals for yourself and education goals for your children. While you now have more responsibility, you have also gained more flexibility and control—advantages that can serve you well as you focus on the long view.

**Someday, your long-term goals  
will become immediate needs.**



Utilize Tax-Advantaged  
College Savings Programs

Adjust Wealth  
Transfer Plans

Divide Retirement  
Assets

Establish Your Own  
Retirement Plan

Look at Long-Term  
Care Insurance

### Retiring With Your Fair Share

When you are in the middle of the divorce process, retirement may not be high on your list of things to think about. Still, if you ignore it—specifically, the assets that may be held in your spouse's retirement plan—you could be doing a major disservice to yourself and your future financial security.

Retirement plan assets are usually regarded as marital property, which means that there is an expectation they will be divided between the divorcing spouses. These assets typically include 401(k) plans, individual retirement accounts (IRAs), defined benefit pension plans and even deferred compensation and long-term executive compensation packages. Determining the actual amount due to you can be a complex process involving federal law (for 401(k) plans) and state law (for IRAs). Pension plan assets, the benefits of which may not be paid for years down the road, are particularly difficult to divide. All this underscores the point that you, your attorney and other advisors should look carefully at these assets, because after your divorce is finalized it will be too late.

**TRANSFERRING ASSETS.** Complex tax laws and strict distribution requirements surround retirement plans. Moving assets from your spouse's retirement plan or IRA into your own account—usually a rollover IRA set up for that purpose—takes planning and paperwork. Generally, for a 401(k) or pension plan, you will have to provide the administrator of your spouse's plan with a qualified domestic relations order (QDRO) that has been approved by a judge and customized according

to the rules of the retirement plan. Your lawyers will have to perform some up-front work to make sure your QDRO follows the plan guidelines.

The typical QDRO identifies the participant from whose account the assets will be taken and names you as the recipient, as well as specifies the dollar amount and number of payments, the reason for the QDRO and the account to which the funds will be paid. If you receive the funds directly, you may be subject to tax withholding, an issue you may be able to avoid by making a direct transfer into an IRA. However, you will have a one-time opportunity to withdraw funds for immediate use without paying the usual 10% early withdrawal tax.

Please note that in order to divide an IRA in a tax free manner the marital property agreement must be incorporated into a court order, which is generally the divorce decree. ■

### A Social Security Secret

You may not be aware that you are entitled to up to one-half of your former spouse's Social Security retirement benefits when you retire. This rule applies when:

- Your marriage lasted more than 10 years
- You are at least 62 years old and have not yet remarried

You can receive these "derivative benefits" even if your former spouse has not retired. If your former spouse is retired and receiving benefits, neither of your benefit amounts will be reduced. If you have more than one former spouse but were married

longer than 10 years both times, the benefit will be based on whichever earnings record pays you the higher benefit.

Be sure to compare any benefit you might receive on your own with the derivative benefit amount, because you will only receive one Social Security check. ■

### Children and College Costs

If you have children, your divorce agreement should include specific provisions related to education expenses. Otherwise, you may find yourself backed into a corner at a later date, forced to tap assets you had earmarked for retirement or other purposes.

If you remarry, you may also find that your new spouse's assets and income become a factor in any legal dispute with your former spouse over college costs.

**MAKING THE GRADE.** 529 college savings programs provide a tax-advantaged opportunity to set aside college expenses.

If you and your former spouse already had established one, you will probably want to divide these assets in the divorce settlement. If you do, you can

You will probably want to divide these assets in the divorce settlement.

use the assets as you see fit—ideally, to pay tax-free qualified education costs. You may also want to have the divorce agreement specify that your former spouse use the assets for the same purpose.

**STARTING A NEW PLAN.** If you are unfamiliar with 529 plans, here is the major benefit: Although you fund the plan with after-tax dollars, investment earnings in 529 plans are not subject to federal tax, and in most cases, state tax, so long as you use withdrawals for eligible educational expenses, such as tuition and room and board. In many states, you may also qualify for a state tax deduction for 529 plan contributions. These rules apply no matter how high your income. These rules apply no matter how high your income.

Each state has its own 529 plan, and some states have multiple plans.

Each plan is overseen by an administrator—like Fidelity, Vanguard or another firm—that manages investments. Two types of plans are available: prepaid plans, which effectively lock in the price of certain annual costs, such as tuition; and investment plans, which give you more flexibility in how funds can be invested and used.

#### **NONEDUCATION WITHDRAWALS.**

You can withdraw funds to meet other expenses if you need to, but any gains will be taxed at ordinary income rates, and there may be an additional 10% tax on those gains. Tax-free and penalty-free withdrawals are allowed without imposition of the additional 10% tax if your child is awarded a scholarship, becomes disabled, does not live to eligibility, and in certain other circumstances. ■



#### **CONSIDER LONG-TERM CARE INSURANCE**

These policies are designed to help cover costs if you are unable to care for yourself because of age or illness. It's important to apply as early as possible, because this coverage usually costs more as you get older. Another factor to keep in mind: Women are generally expected to live longer than men, which means they are likely to require care for a longer period—which usually means higher premiums.

### **529 PLAN FACTS**

**1**

Money saved in 529 accounts can be used to pay for tuition, room and board, books, computers and other required supplies.

**2**

When used for these purposes, withdrawals are typically tax-free.

**3**

The account owner retains control of account assets and can change the beneficiary at any time, in many cases tax-free.

**4**

Should one child decide not to go to college, the money can be used to help finance the education of another family member.

## Children, Divorce and Money

Divorce almost always involves money, and it often involves children. What happens when these two topics intersect?

Divorce can affect children in many ways, reflecting differences in age, personality and coping skills. As a parent, you may try to protect, comfort, manage and control, depending on the circumstances or issues.

One issue in particular deserves special attention when it comes to children, yet often remains below the surface: money. Even in the best of times, it can be difficult for parents to discuss finances with their children, often shortchanging an important facet of their education. Given the uncertainty and exhaustion that can accompany divorce, it may seem easier to let tough discussions about money slide.

According to Joline Godfrey, author of “Raising Financially Fit Kids,” that nonapproach can magnify insecurities while hampering the development of some key life skills. In this interview, conducted exclusively for Morgan Stanley, Joline discusses the importance of financial openness and education, particularly in the topsy-turvy environment of divorce.

**To find out what they're thinking, listen.**

“Are we going to be OK?”

Ages 5 to 8

“What’s going on? Did I do this?”

Ages 9 to 12

“I guess I can help out more.”

Ages 13 to 15

“It’s time to get on with my life.”

Ages 16 to 18

### Helping Your Kids Make Financial Sense of Divorce

At what age can kids begin to understand basic ideas about money?

**JOLINE GODFREY (JG):** In the womb—or sometimes it seems that way. There is good research suggesting that financial imprinting begins as early as 18 months. Everybody knows how effectively a three-year-old can manipulate a parent returning from a trip by asking, “Where’s my present?” That’s a form of bargaining.

#### So kids are more financially conscious than we realize?

**JG:** They are—but not necessarily in the right way or for the right reasons. Sometimes it’s just about competition or status. Kids have questions about money along with everything else, and they have more ways than ever to get answers. For instance, social media, which gives children access to more information than you can possibly imagine, carries some unintended consequences. One father told me a story about his nine-year-old son, who got up from the computer one night and said, “Look how much my house cost.” The boy had gone to an online real estate service and looked it

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—Joline Godfrey

up—along with the prices of his friends’ houses. It’s almost impossible to prepare for situations like that, but they happen all the time.

It can be daunting for a parent. The monster delusion is that if we don’t tell our kids about something, we are protecting them. So if we don’t talk to them about money, we are shielding them from all the messiness that goes with it. In reality though, it’s usually because we’re less than comfortable discussing it ourselves. In the process, we’re missing an opportunity to prepare kids for the world and give them some practical exposure to values we hold dear.

#### How do parental attitudes affect kids in a divorcing family?

**JG:** On the one hand, you often have immature parents who are acting like children themselves, and they use their own kids as pawns. When parents can’t get on the same page, [they] give conflicting signals and confuse the child, who doesn’t know what to do or what’s expected.

Then there are parents who may be deeply at odds between themselves, but they work to get on the same page with regard to their children. They have the maturity and ability to transcend their own hurt and anger at one another for the sake of their children. It’s as if they’ve said, “We have to rise above this and find some way to think about these children, even if we wanna kill each other.” Their kids have won the parent lottery when it comes to avoiding primitive behavior.

#### Are there practical things that divorced parents can do to protect their children and send messages that are constructive rather than destructive—particularly about money?

**JG:** It sounds cliché, but it’s very important to agree on a few operating principles for kids. You have to agree from the

beginning that, no matter what happens, you’re not going to use the kids. No bad-mouthing. No playing games. No “Ask your father” or “Ask your mother.” And those rules apply as much to money as to anything else.

It’s also important not to abdicate parental authority. There are parents who say, “I want to involve my children in all the decisions.” That forces kids to make choices and decisions before they have the maturity to do that—decisions that maybe even the parent isn’t mature enough to make comfortably. It’s not that children shouldn’t be involved or consulted, but passing the buck because you don’t want to do the hard work of taking a stand in your own life or as a parent is very destructive to kids. The reason they’re kids and you’re the parent is because you’re older. You are supposed to have some experience, to know things, and you really have to take responsibility for your choices and decisions on behalf of your children.

#### How does the context of divorce change the notion that you should have open, straightforward discussions with your children about money?

**JG:** It certainly complicates it. Often people are in a divorce because they have not been able to be their authentic selves. If you have not been able to be clear about who you are and what your needs are, it’s tough to step up and be clear and open in this area with your children. After all, had you been able to do it earlier with your spouse, it might have saved you from divorce.

The irony is that just at the point where couples are feeling most vulnerable and most depressed and least energetic, even more is expected of them. As a professional, I always feel I need to say over and over, “Look, you are going to be tired, and this is going to be really hard.” A parent is likely to be a beleaguered human being at this stage of his or her life, with a sense of “I’m alone. This is too hard. I can’t

do this." That is why having a personal team, a personal advisor and counselor, is so important—for empathy in the struggle. So you don't give up. Because this can be the hardest part of divorce.

### What is the right way to deal with kids who are feeling instability and insecurity, and starting to worry about money?

**JG:** Kids' responses can get pretty primitive, depending on their age. At five or six, they can start to worry about money, which can take the form of, "Are we going to be able to eat?" Your job as a parent is to say, "Yes, there are going to be some changes in the family, but Mom's here, and Dad's there, and it's going to be all right."

Kids who are a little older, say between nine and 12, are not only intuitively aware of what's going on, but they are also frightened by the changes in their bodies, their social lives, the pressure in school. So, again, it's essential not to abdicate. But you can't lie to them. If budgets and priorities are changing, you have to acknowledge that—but always in the context of, "We're going to be fine." There has to be clarity about what's coming down the pike, because kids who don't know will make it up.

With older kids, say 13 to 16 or 17, you can start expecting them to shoulder some responsibilities. Their world has changed,

and while they're not the new man or woman of the house, they can take on some responsibilities—because everyone has new responsibilities. This can become an invitation to growth, an opportunity to build character.

### Do you find that kids will act out about money in a divorce—make demands, test, push the limits?

**JG:** Not just children, but adults as well. It's people who can't sort out the difference between external change and internal change. It's understandable that a person will want to change things on the outside to get a new perspective or acknowledge some major shift in their lives. But it's important to figure out that you're not what you're wearing or that new car you just bought. Whether child or parent, it's important to be a little more reflective and think, "Okay, we're in a different place. What's important here? What decisions do we need to make?" In many ways, it's all about having solid values and then working to live them.

### What's the most important thing to remember about divorce and children?

**JG:** Again, this thought doesn't just apply to children but to parents as well. We human beings are pretty resilient. We have the strength to recover, to go on. Somehow, kids will adapt. As parents, our job is to make sure they have the emotional and financial skills to do it. ■



## DISCUSSING DIVORCE WITH CHILDREN

The American Academy of Child & Adolescent Psychiatry has these suggestions for talking about your divorce with your children:

- Do not keep it a secret or wait until the last minute.
- Tell your child/children together with your spouse.
- Keep things simple and straightforward.
- Tell them the divorce is not their fault.
- Admit that this will be sad and upsetting for everyone.
- Reassure your child/children that you both still love them and will always be their parents.
- Do not discuss each other's faults or problems with the child.

Source: American Academy of Child & Adolescent Psychiatry. As of April 2020. [https://www.aacap.org/AACAP/Families\\_and\\_Youth/Facts\\_for\\_Families/FFF-Guide/Children-and-Divorce-001.aspx](https://www.aacap.org/AACAP/Families_and_Youth/Facts_for_Families/FFF-Guide/Children-and-Divorce-001.aspx)

## 10 BASIC MONEY SKILLS

According to Joline Godfrey, these are the basic skills, learned between the ages of five and 18, that constitute a child's complete financial toolkit. When parents divorce, it becomes harder to impart these skills—but also more important than ever.

1. How to save
2. How to keep track of money
3. How to get paid what you are worth
4. How to spend wisely
5. How to talk about money
6. How to live within a budget
7. How to invest
8. How to exercise entrepreneurial spirit
9. How to handle credit
10. How to use money to change the world

## A Culture of Excellence

Over the years, you will make many financial decisions. One in particular is likely to have a lasting impact on your well-being and that of your family: the choice of a Private Wealth Advisor.

Thoughtful decision-making usually begins with a lot of questions. As you get answers and information, you can develop a framework for evaluating different choices and strategies. Little by little, you gain both the knowledge and the confidence to make decisions and create a wealth plan that helps you achieve your goals.

You will find your Morgan Stanley Private Wealth Advisor to be a knowledgeable source of objective information and ideas as you begin to assess how to best manage your wealth. Over the course of many years, our firm and Private Wealth Advisors have developed an in-depth understanding of virtually all the challenges, goals, preferences,

styles and strategies that distinguish wealthy investors. This experience is combined with access to a wide array of tools designed to help you maximize what you have and accomplish your specific goals—whether you are preparing for the cost of educating children, managing risk in your portfolio or finding ways to increase the impact of your charitable contributions.

Your Private Wealth Advisor is an advocate within our firm, your Private Wealth Advisor selects and aligns the many capabilities of Morgan Stanley for you, delivering resources to you in the way that is appropriate for how you invest and what you want to achieve. ■

## INVESTMENT MANAGEMENT

I have so many goals and priorities. How can one investment strategy balance them all?

## INTEGRATED PLANNING

Decisions about both assets and liabilities need to be made within the framework of important life goals. What steps are also the most tax efficient? How can a strategic approach to cash management and lending simplify my financial life and help maximize the value of what I own?

## ESTATE PLANNING

Making sure my estate goes to the people and organizations I care about is a priority. How do I transform my assets into a legacy?

## RISK MANAGEMENT

The ups and downs of the markets is one kind of risk—but so is not protecting my assets and my family. How do I protect what I care about most?

## EDUCATION FUNDING

Will I be able to pay for a good education for my children—and my grandchildren?

## PHILANTHROPIC PURSUITS

The charities I support are like extended family. How do I maximize the good I can accomplish?

## BUSINESS STRATEGIES

How do I manage my personal wealth with so much tied up in my company?

## LIQUIDITY

I can predict some expenses, but others, I know I can't. How can I plan to have the cash I need?

## RETIREMENT

When I retire, it will affect just about everything that matters: my lifestyle, my company, my family. Is there a way to plan for retirement that takes it all into account?

## WEATHERING DIVORCE

Weathering the financial effects of divorce takes knowledge, planning and objectivity. It is essential to focus on what works for you now and what will best prepare you for the future. Your Morgan Stanley Private Wealth Advisor will work with you to develop and implement a well-considered investment plan—one based on your unique financial goals and opportunities. As you assemble the team that will guide you through this demanding transition, your Private Wealth Advisor can play a key role, helping you approach your financial life with clarity and confidence.

Joline Godfrey is not affiliated with Morgan Stanley.

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