Morgan Stanley

PRIVATE WEALTH MANAGEMENT

DIVORCE

Among the many emotional and practical difficulties you must address as a divorcing couple are the needs to re-establish separate bank and investment accounts, change your estate plans and insurance policies, and divide your assets and liabilities. A broad range of factors may influence how, and how easily, all of this can be done, including:

NUMBER AND AGES OF CHILDREN

TITLING OF ASSETS

THE ABILITY OF THE COUPLE TO ACHIEVE CONSENSUS

STATE OF RESIDENCE

RELATIVE SALARY AND SAVINGS

OWNERSHIP OF A BUSINESS

TERMS OF PRENUPTIAL AGREEMENT

ADJUSTING YOUR BUDGET

Even in the presence of significant wealth, you may very well have to make some adjustments in your household budget and possibly accept some level of compromise in your lifestyle. Whether or not this is the case, you should always sit down and calculate an accurate, post-divorce household budget. This can be a valuable negotiating tool and, if a court is involved, it can help the judge evaluate alimony and child support needs.

At its most basic level, a budget should add up your sources of monthly income and delineate your regular expenses. The more time you spend preparing your budget, the less likely you are to overlook sources of income and expenses. So, be thorough and refer to at least the past year's bank, brokerage and credit card statements to help jog your memory. You may also want to use an online household budgeting application to assist in the process, or enlist the aid of your accountant and other advisors.

REBUILDING YOUR RETIREMENT SAVINGS

Even if you are many years away from retirement, the assets that may be held in your spouse's IRA, 401(k) or other retirement plans may represent a significant marital asset. As such, you may be entitled to some portion of these accounts, which can become the cornerstone of your own retirement savings strategy. Depending on how long you have been married, you also may be entitled to up to one-half of your former spouse's Social Security retirement benefits when you retire. This Social Security 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 Social Security "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.

SIX STEPS YOU CAN TAKE PRIOR TO YOUR DIVORCE:

1. Open accounts in your own name including your own credit card, checking and savings accounts.
2. Have your paycheck deposited directly into your checking account.
3. Contact creditors to explain your situation and, if appropriate, to ask to stop any future charges by your spouse.
4. Be aware that late payments or liens related to jointly owned assets may remain a legal obligation to you as a co-owner of the property.
5. Check your credit report by using either a commercial Internet site or a free federal government site.
6. Open an interim account to manage interim family expenses during the period between separation and divorce.

CREDIT ISSUES

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.

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

ESTABLISH AN INDEPENDENT CREDIT PROFILE

One of the first things you can do to establish an independent credit profile is to open your own bank and investment accounts. Your Private Wealth Advisor may also 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.

STARTING OVER

When coping with the emotional stresses of divorce, it may be difficult to focus on the important practical considerations of creating separate households and independent financial lives. Make sure that you have the proper support and advice needed to achieve a fair division of assets, so you do not create long-term difficulties out of your short-term concerns. Hire a competent divorce attorney, utilize the services of your Private Wealth Advisor and Accountant, and make sure you understand the full implications of any agreements you make. A divorce can represent a fresh start, so do what you can to get off to a good one.

[1] Source: Find Law. Available at: https://family.findlaw.com/child-support/child-support-basics.html. June 2023..

[2] Source: American Academy of Child & Adolescent Psychiatry. Available at: https://www.aacap.org/AACAP/Families_and_Youth/Facts_for_Families/FFF-Guide/Children-and-Divorce-001.aspx. Accessed November 2023.

PWM7879221
CRC 4251744 03/25 CS 1599197-5515859 03/25

THE LEGAL AVENUES TO DIVORCE

There are three approaches to the divorce process, each of which involves different levels of legal involvement and costs:

COLLABORATION: You and your spouse agree not to litigate. Instead, you attend sessions with your attorneys, and sometimes with mental health professionals and financial planners, to work out an agreement as a team. This approach involves minimal court involvement.

MEDIATION: You and your spouse negotiate directly in the presence of a third-party mediator. You then consult with your attorneys outside of these sessions before you sign a final, legally binding agreement. Court involvement is also minimal with this approach.

LITIGATION: You and your spouse are represented by separate attorneys who negotiate on your behalf and represent your interests in divorce court. Requiring extensive court and attorney involvement, this is generally the most expensive way to get a divorce. This approach may be necessary if you and your spouse cannot agree to terms on a collaborative or mediated basis.

COORDINATING YOUR ADVISORY TEAM

If the same legal and financial advisors have represented you and your spouse, you may need to assemble a new team to provide critical guidance and support. Consider building a team that includes the following professionals:

DIVORCE ATTORNEY

While it is possible to get through a divorce without a lawyer, it is generally not wise, particularly when significant marital assets are involved. 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.

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—as well as any residual tax issues that may linger from your marriage.

PRIVATE WEALTH ADVISOR

You need a professional who can focus solely on you and your needs and plans—on a completely confidential basis. Your Private Wealth Advisor can work with you and your attorney to divide assets in a joint portfolio to minimize tax liabilities. He or she can then help you develop strategies to address your needs for short-term liquidity and long-term objectives, such as educating a child or planning for retirement.

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.

DIVIDING PROPERTY

Planning your financial life after a divorce begins with an analysis of your predivorce financial situation and holdings. This includes how much you have earned as a couple over the past five years and how much debt you have. You should also determine how much money you have in all of your financial accounts; understand how the money is allocated among stocks, bonds and cash; and know who owns each account if they are in separate names. You will also need to determine how much it costs on an annual basis to maintain your lifestyle: monthly bills, homes, vacations and other expenses.

WHAT IS MARITAL 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:

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

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

HOW IS MARITAL PROPERTY TYPICALLY DIVIDED?

Most states will rely on the concept of equitable distribution in dividing marital property. The goal is 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.

Community property states include:

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

DIVORCE AND 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—but in the case of a successful business, the effort can be well worth it. Keep in mind that actions you take with respect to your business, whether you sell it or otherwise change the ownership structure, can have significant tax consequences.

DOCUMENTS TO GATHER

- [ ] Prenuptial agreement
- [ ] Bank account statements
- [ ] Brokerage account and mutual fund statements
- [ ] Tax returns for the prior three years
- [ ] Retirement (IRA, 401(k), etc.) and pension plan statements (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 credit)
- [ ] Car, boat and other loans
- [ ] Loans you or your spouse may have guaranteed
- [ ] 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
- [ ] Insurance coverage
- [ ] Life insurance
- [ ] Homeowner's insurance
- [ ] Umbrella liability
- [ ] Car insurance
- [ ] Long-term care insurance

UNDERSTANDING 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 payments are neither deductible nor taxable to either spouse.

UNDERSTANDING CHILD SUPPORT[1]

Child support payments are made by parents to support a child or children of whom they do not have full custody. The amount and duration of these payments are stipulated in a divorce agreement and are neither deductible nor taxable to either spouse. Most commonly, payments are made to the custodial parent, though there are cases where payments are made to others who have custody of the child or children (a grandparent, for example).

The amount of child support can vary greatly depending on your state of residence. Each state is required by federal law to establish guidelines to calculate a range of child support based on the parents' respective incomes and expenses. Some states allow their judges considerable discretion within that range and others do not. Among the factors that are typically considered in calculating child support are:

- The needs of the child, including health insurance, education, day care and special needs.
- The income and needs of the custodial parent.
- The paying parent's ability to pay.
- The child's standard of living before divorce or separation.

While courts will generally attempt to maintain the pre divorce standard of living for children, this is more of a goal than a guarantee. Courts understand the difficulty of maintaining two households on the income that formerly supported one, and make determinations that lead to a more frugal standard of living.

DISCUSSING DIVORCE WITH YOUR CHILDREN

The American Academy of Child & Adolescent Psychiatry has these suggestions for talking about your divorce with your children:[2]

- 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.