



Anticipating Divorce

by David J. Drucker | 05-19-05

Is it ethical and professional for us to prepare financial plans without considering the fact that 50% will be hogwash due to divorce?

The question was posed by advisor Richard Hall of Albuquerque, N.M. Owner of B&H Wealth Management, Hall earned his Certified Divorce Financial Analyst credential several years ago and now sees divorce planning in a very different light. "The question is, how do we raise the possibility of divorce with clients? I think not to do so is unethical and smacks of incompetence," Hall says.

He raises two important issues. First, does prudent planning require the financial advisor to anticipate and plan for events that may never happen? Second, if the answer is "yes," at least for divorce, then how do we raise the question? Like other life planning issues, the subject of divorce--particularly if a client couple appears happily married--may encounter great resistance and even animosity if raised.

"There are many things that can befall a couple or individual that I know might happen that could change the plan," says Mary Gibson, a San Juan Bautista, Calif., financial advisor, "but it would be impossible to list them all and to know if they will happen to the people I have sitting in my office. Think about a child coming home after college to stay, grandparents having to take care of grandchildren, or an unexpected windfall."

And she's right. We can't plan for everything that might possibly happen to a client. But many advisors agree--due to the relatively higher probability of divorce than other unknowable future events--that something must be done. The question is, well, how to raise the question?

Hall finds the easiest way to raise the question is during the data-gathering process.

"When reviewing assets, I ask if any are separate assets, and I explain what these are and when and why the subject is important, gently feeding into what's really on my mind. I might say to the client, 'In our planning, we will address the two risks of death and disability and what you can do to protect yourself. However, those of us in the profession who take seriously our responsibility to our clients are in a quandary about how to incorporate the greatest risk to achieving your financial goals--one that affects 50% of all couples, the big pink elephant in the room. That, of course, is divorce. Is this something you would like me to try and incorporate into your plan in some way?'"

Russ Wild of Global Portfolios in Allentown, Pa., does something similar: "Being divorced myself, and having had the experience wreak major havoc on my own financial plans, I make it a habit when taking on new clients of asking husbands and wives whether their marriage is solid. I feel it is my responsibility to ask that question and to repeat the question every few years. I haven't had anyone take offense yet. But how honest are their answers? Only time will tell."

But while these approaches may work for Hall and Wild, they won't fit for all advisors. Some clients will take offense at the mere suggestion there could be a problem with their marriage. Of course, they may be precisely the ones heading for trouble. Says Linda Leitz, an advisor with Pinnacle Financial Concepts in

Colorado Springs, Colo., "A planner friend of mine saw the primary wage-earner among one of his client couples doing things--apparently unintentionally--that could potentially devastate his wife if a divorce were to occur. This planner mentioned these activities to his client, who completely flew off the handle at the mere suggestion he might be doing something unethical. Several years later, this husband and wife divorced. The husband had been putting assets in his separate name, although he did split them equitably with his wife when the time came."

A gentler approach to raising the subject, says Ted Feight of Creative Financial Design in Lansing, Mich., is to "discuss with new clients what happens when inherited assets and/or assets earned prior to the marriage are co-mingled." Of course, this issue is particularly important if the clients reside in a community property state. "In California, where I practice," says Jean Sinclair of San Diego-based Avenue Advisors, "I nearly always explain to clients the benefits and risks of community property versus joint titling and commingling of assets, irrespective of what I believe to be the state of the relationship."

In fact, many advisors see a need to approach the divorce discussion indirectly. Says Curt Fey, an advisor in Pittsford, N.Y., "I consider the possibility of divorce without mentioning it. I urge couples, usually unsuccessfully, to have prenuptial agreements. I suggest for couples with significantly different assets to have post-nuptial agreements. And I require married clients to both come to meetings."

What happens if you aren't proactive on this issue? Often, not what you would have wanted for your client. Delia Fernandez learned after bringing on a new client couple that they were probably already headed down the road to divorce. "My biggest frustration was that I had innocently allocated their assets, mostly in company 401(k)s, as one portfolio versus individual portfolios. That is, where one of them had the best large-cap growth fund, we left that allocation in their 401(k), and where the other had the best bond offering, that person got all the bond allocation. This was in the mid-1990s, so by trying to maximize long-term returns for the two of them, I had inadvertently minimized short-term returns for one of them."

These kinds of lessons can make much more clear to us what we should be doing to anticipate our client's divorces. Many advisors, including Fernandez, now say that, whenever possible, we should apply the same investment template to each spouse's assets; we should look at the couple's balance sheet both as a couple and as individuals; and we should make sure each spouse has a credit record that could stand on its own.

And, as noted earlier, "if one or both members of the couple could be in line for an inheritance, that offers the chance to discuss separate property versus joint/community property, which can 'tease out' some emotional issues that can guide you in better understanding your client," according to Fernandez. At the very least, she says, she is always running a divorce "what-if" scenario in her head when she reviews a couple's situation: "It's like playing three-dimensional chess. I'm always thinking ahead to the move that's not on today's agenda."

Even if you don't play mental chess, you might consider protecting yourself with contract language. Says Ben Jennings of Navigator Financial Planning in Lakewood, Wash., "In my client service agreement, I have a paragraph dealing with 'multiple clients,' and when reviewing this with prospective clients, I consistently point out that, unless they tell me differently, I assume I am planning for the marital community. I note that I could recommend things for one spouse that could be detrimental to the other. I let them know that, if they are heading toward divorce, my planning is probably based on inappropriate assumptions. I then ask them if it's okay to proceed on that assumption or if they have any questions about that."

Perhaps the most novel solution to the problem of how to anticipate and plan for a divorce that has yet to happen is that of Ed Sherman, an attorney and owner of Santa Cruz, Calif.-based publisher Nolo Press-Occidental. Sherman designed his "couples contract" to put a safety net under the clients' relationship. "The couples contract," he says, "is much less intrusive and divisive and very positive compared to lawyer-drafted contracts, which are tightly focused on legalistic issues of power and control over assets and income. The couples contract has a completely different purpose. It asks the question: What's the most useful and constructive thing a couple can accomplish in a written agreement?"

Essentially, Sherman's contract expresses each party's desire to make a loving commitment to a lasting relationship. It introduces concepts that can help solve relationship problems if any arise. And, perhaps most appealing, it makes sure the clients' relationship never ends up in court. It can also ensure that the couple's marriage remains governed by the laws of the state where they were first married even though they may have since moved to another state with different laws.

"A lot of people move to another state and don't know laws have changed," Sherman says. "For example, laws pertaining to who owns and controls income and assets, what debtors can and can't make claims against, what happens on death. With the couples contract, we can keep these agreements under the laws of the state the clients moved from."

Does the couples contract prevent divorce? No, but it makes the whole process much easier to manage and it may be just the catalyst needed to raise the issue when talking to one's new client.