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The Impact of Divorce on Estate Planning And Wealth Management

Help clients protect their loved ones and their assets

Births, deaths, marriages and divorces reshape the definition of "family" for individuals on a constant basis. It's no wonder, then, that family law and estate planning often go hand in hand. Estate planners and divorce attorneys alike are often presented with "what if" questions that span both areas of law. Here, we explore a few common questions estate-planning professionals may have when guiding clients faced with these life transitions. The goal is to help clients make decisions that protect their loved ones and their assets.

Changing a Will

Can my client change their will while getting divorced? Should they? Although the last thing that many clients want to do once the divorce action has begun is to engage another attorney, it's actually a good idea for them to review their estate plan at this time.

If a client dies before the divorce is final, then technically that client is still married at the time of their death, so their soon-to-be former spouse is still their spouse. Public policy prohibits completely disinheriting a spouse, so a spouse who isn't named in the other's will may still be entitled to receive a portion of your client's estate. In community property states, a disinherited spouse generally receives half of the community property, automatically. In common law states, a spouse can claim what's known as the "right of election" to receive a portion of the deceased spouse's estate, generally about one-third of the estate. Depending on the state, this may or may not include "non-probate" assets like retirement accounts that can pass by beneficiary designation, and it may or may not take into account the surviving spouse's individual assets.

If your client dies without a will, intestacy statutes provide that their spouse would receive some or all of their estate, depending on the state where the client lives. For example, in New Jersey, the amount the spouse receives depends on whether the client is survived by any children or parents in addition to the spouse.[1] In Florida, the spouse receives the entire estate unless there are children from a prior relationship.[2]

Even if your client revises their will during the pendency of a divorce to disinherit their soon-to-be former spouse, this alone won't necessarily prevent the spouse from receiving assets from the client's estate that would have been subject to equitable distribution if the divorce had proceeded until conclusion. In this scenario, unless an agreement could be reached between the soon-to-be former spouse and the estate, a court would be charged with the task of determining the equitable share to which the soon-to-be former spouse is entitled.

Nevertheless, your client could change the appointment of their executor in their will before the divorce is final. Because there's no requirement that a married individual name the spouse as executor, your client is able to appoint someone else to serve in this capacity. Without a will, intestacy laws give priority to your client's spouse to serve as the administrator of their estate. Because the executor or administrator controls the administration of your client's estate, having someone other than your client's soon-to-be former spouse serve in this role

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would likely be desirable and is a reason to ensure that your client's will is up to date during the divorce proceeding.

Changing Beneficiary Designations

Can my client change their beneficiary designations while they're getting divorced? The short answer is that your client shouldn't. Some states require those filing a complaint for divorce to also file a document on which they list and provide the details relating to all insurance policies that were in place at the time of the filing of the divorce complaint.[3] In New Jersey, for example, this document also requires your client to disclose any modifications that have been made to these policies during the 90 days prior to filing the complaint. Therefore, if your client has a life insurance policy naming their spouse as the beneficiary, unless there's a consent order signed by both your client and their spouse that permits your client to make such a change, your client shouldn't make any modifications during the divorce. Even if a state doesn't require this initial affirmative disclosure, if recent changes are made to insurance policy beneficiary designations either shortly before the filing of a divorce or during the divorce process, courts have the equitable power to require that the changes are reversed.

Other beneficiary designations, such as those related to retirement accounts and investment plans, will typically require your soon-to-be former spouse to sign a form if they're removed as beneficiary while your client remains married. Further, retirement accounts and investment accounts that were accumulated during the marriage would still remain subject to equitable distribution regardless of the titling of such accounts.

Documents Changed After Divorce

What happens if my client doesn't change their estate-planning documents that name their ex-spouse after the divorce is final? Many jurisdictions provide that a divorce decree automatically revokes many rights of your client's ex-spouse in your client's estate, such as: (1) disposition under a will; (2) nomination as fiduciary, such as executor; and (3) right of survivorship of jointly owned assets.[4] This means that if your client had a will that leaves all of their assets to their spouse and names their spouse as executor, but your client gets divorced and dies without changing their will, your client's ex-spouse won't be entitled to inherit any of your client's property under your client's will or be able to serve as executor of your client's estate.

We don't recommend relying on this default revocation statute. In some states, such as New York and California, this doesn't extend to anyone besides the ex-spouse. This means that if your client left all of their property to their spouse, or to their spouse's father if their spouse predeceases them, and they named their spouse as executor with their spouse's father as the successor, their ex-spouse would be ineligible to receive your client's property or serve as executor once the divorce was final, but their former father-in-law would take all of their property and be eligible to serve as executor of the client's estate.[5]

> A divorce decree doesn't automatically void beneficiary designations on life insurance policies or retirement accounts.

However, a divorce decree doesn't automatically void beneficiary designations on life insurance policies or retirement accounts. It's especially important for your client to review the beneficiary designations after a divorce and update them as necessary. The custodians of these accounts are required to distribute the proceeds to whomever is named as the designated beneficiary on file. If your client's children or other heirs contest this, the custodian may hold the funds while the parties attempt to negotiate a settlement. Even if your client's children or other heirs are successful in receiving some or all of the funds instead of your client's ex-spouse, doing so will likely force them to incur legal fees and delay the distribution of the funds. All of this could be avoided by changing the beneficiary to someone other than your client's ex-spouse after the divorce is final.

Protecting Children

My client is concerned that their children may get divorced and the inheritance they might receive from my client's estate will go to their ex-spouses. What can my client do to protect their children? Inheritance received by only one spouse during the marriage from a third party is exempt from equitable distribution during a divorce proceeding.[6] This is the same in states that are categorized as community property states.[7] However, to preserve these assets as separate, it's crucial for the recipient to keep these assets in separate accounts and not commingle them with otherwise marital funds. In addition, if inherited assets are used to purchase a marital asset, such as a second home or a vehicle, absent a written agreement at the time of such purchase to the contrary, the inherited funds used wouldn't be returned to the spouse if the item were sold or distributed during a divorce.

> Prenups allow couples prior to their marriage to contemplate and determine the outcome of certain scenarios that may arise once they're married.

The best way to ensure that your client's assets remain in their bloodline is to establish trusts for the benefit of your client's descendants. Trusts can be established and funded during your client's lifetime or on their death. The trustee should be given the authority to decide when distributions are made and how much is distributed. This ensures that your client's child or grandchild doesn't have control over the trust assets, which in turn means that their spouse can't have control. Once funds are distributed from the trust, however, they may be "fair game." For example, if the trustee is required to distribute income on a quarterly basis, once that distribution has been made to your client's child, it may be considered part of your client's child's income stream for the purposes of establishing spousal and child support.

Your client could also require their children to execute a prenuptial agreement (prenup) before they marry. Prenups allow couples prior to their marriage to contemplate and determine the outcome of certain scenarios that may arise once they're married. In a prenup, the couple may specifically outline how inherited assets will be treated and used during their marriage and what will happen if inherited assets are used for marital purposes, such as returning those funds to the owner spouse on divorce or death if property is then sold.

Endnotes

1. N.J.S.A. 3B:5-3.
2. Fla. Stat. 732.102.
3. R. 5:4-2(f).
4. *E.g.*, N.J.S.A. 3B:3-14; N.Y. E.P.T.L. 5-1.4.
5. *In re Estate of Lewis*, 25 N.Y.3d 456 (2015).
6. N.J.S.A. 2A:34-23(h).
7. *E.g.* Ariz. Rev. Stat. Ann. Section 25-211.