



So You Got the House! Now What?

Points to Keep in Mind During Your Divorce Settlement

Too often, people going through a divorce ignore the long-term financial effects of their settlement decree. Bethesda divorce attorney George Paxton once said, "One of the biggest mistakes people make is not doing long-range planning. Very often they are focusing on the emotional issues rather than how they're going to end up five, 10 or 20 years later."

The key is to meet with a financial planner before the divorce settlement. As noted by the Wall Street Journal, "Pre-divorce financial planning probably makes sense for just about everybody. While a good attorney will know about many of the tax and other financial aspects of a settlement, lawyers often suggest that clients sit down with a financial pro to map out their long-term needs."

In fact, said the Journal, couples who have done proper planning usually reach a settlement faster and with fewer legal fees than those who don't plan. Here are some key points to help you:

Draft your divorce decree carefully, because most agreements cannot be changed later. Thus, it is critical that you think about your needs beyond the next five years.

Be sure you understand the difference between child support and alimony. The former is for the support of children and most jurisdictions have guidelines to determine the appropriate amount. The latter is more discretionary, and largely up to the judge.

Child support payments are not tax-deductible by the spouse paying, nor taxable to the spouse receiving it. The opposite is true for alimony: The payer receives a tax deduction, and the receiver must include it in their gross income for tax purposes. Therefore, it's in the payer's best interest to pay alimony instead of child support, and it's in the recipient's best interest to receive child support instead of alimony.

If you are the recipient of alimony or child support, make sure your decree requires your ex-spouse to buy and maintain life and disability

insurance to ensure that payments to you will continue in the event of your ex's death or disability. Also make sure you have the right to receive information from the insurance company confirming that the policy is in force and maintains you as the beneficiary.

"To give even more security to the beneficiary of the policy, it is better for that person to be the owner," said George. "Say the husband is providing the insurance for his wife. If he's the owner of the policy, he can cancel it or change the beneficiary. He can't do that if she owns the policy, even though he's paying the premium."

If you are the economically dependent spouse, you are entitled to the other's retirement and pension plans. For most people, the two biggest assets they have are their home and their pension. Everyone focuses on the home, but many ignore the pension because they won't see it for 10 or 20 years.

Keep in mind that an ex-spouse keeps his or her rights to the pension even if he or she later remarries. "It's property acquired during the marriage," George explained. "The non-pensioned spouse gets half of a fraction. The numerator is the number of years of the marriage and the denominator is the number of years the spouse with the pension had been earning it. So it's really a matter of giving the ex-spouse half the share of the pension that was acquired during the marriage."

When divvying up your 401(k) or other retirement plans, don't ignore taxes. It's very common for a spouse to withdraw from a retirement plan as part of the divorce settlement and give the money to the ex, assuming the ex has to pay the taxes. But that's not how the IRS sees it. If you withdraw the money, you owe the taxes - and that could be a hefty sum. To make your ex responsible for the taxes, you must fill out a Qualified Domestic Relations Order. According to *Smart Money* magazine, "Most attorneys understand the concept of QDROs, but they often don't know how to follow through on all the paperwork."

A QDRO is kept with your divorce decree or court-approved property settlement and includes the name and address of the plan participant and alternate payee; the name and account number of each retirement plan affected; the amount to be paid by each plan to the alternate payee; and the number of payments or the period covered by the QDRO. It also should state it is being established under the state's domestic relations laws and Section 414(p) of the Internal Revenue Code.

Don't let the spouse who handles the investments determine how the investments are split. Say the couple jointly invested \$25,000 in stocks and \$25,000 in limited partnerships. The assets should be split equally, meaning each spouse gets half the stocks and half of each partnership. Yet, in many cases one spouse keeps all the stocks and the other gets all the partnerships only later to discover the partnerships are worthless. Also, when calculating the value of assets, be sure to factor in the

effects of taxes and transaction costs. For example, \$10,000 in CDs is worth more than \$10,000 in stocks, because when selling the stocks, the owner will have to pay taxes on the gain and transaction costs.

Don't ignore inflation. If an income stream is part of your negotiations, make sure the income is adjusted for inflation over time. Base adjustments on the Consumer Price Index or other independent gauges.

Protect your credit. If you have any joint credit cards or other lines of credit, close them immediately and open new ones in your name only. Many a person has been financially ruined by an ex-spouse's spending.

Should keeping the house really be your primary goal? Too often, divorcing spouses fight over who gets the house, when in reality, you can't afford to keep it. Try to keep your emotions from controlling your actions and focus intellectually on the economic realities of living alone. If your ex-spouse really wants the house, turn that into a negotiating weapon to win other, more financially valuable concessions. Or agree to sell the house as part of the settlement. Then you can share the proceeds and the tax liability.

Be aware that most people can't maintain the lifestyles they had when they were married. Make sure you shape your financial plan to reflect your new life.



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