

Financial Mistakes to Avoid in a Divorce Settlement

It's common for both parties to focus on immediate financial concerns during a divorce settlement. Yet, it is the long-term financial consequences of divorce that frequently are more devastating. Here are some of the most frequent financial mistakes and how to avoid them.

Taking the house. The spouse who will have custody of the children typically wants to keep the family home. While this may be desirable emotionally, it can be financially problematic.

A home is an illiquid asset that costs money to pay for and maintain. The parent with the children—often the woman—may not have the income resources to take care of both the home and the children, particularly if the woman gives up other financial resources in return for the house. Consequently, it may be better financially to sell the home and split the proceeds.

Assuming equal is equitable. The family home is a good example of the mistake divorcing couples often make by "dividing things down the middle." Frequently, the wife takes the house and the husband keeps his pension or retirement accounts. Say both are valued at \$400,000. The home is a cost-burden, while the retirement account is a liquid asset that can continue to grow, tax deferred, and probably at a faster growth rate than the home.

Not examining earnings potential. Often, one spouse has minimized a career in order to raise children. The settlement needs to take this into account, perhaps by providing extra money to the homemaking spouse to pay for additional career training or education.

Not thinking about taxes. Say it's proposed that one spouse keeps a \$150,000 individual retirement account and the other keeps a \$150,000 taxable investment account. Sounds fair. But it's not. The owner of the IRA will have to pay taxes on that money when it's withdrawn, so the two accounts are not truly equal in value.

Not following through with your attorney on the QDRO. A spouse who will be receiving part of his or her spouse's qualified retirement accounts, such as a 401K or 403b, will need a court order called a QDRO, or Qualified Domestic Relations Order. (Nonqualified plans such as IRAs, deferred compensation, or stock options do not need a QDRO.)

To avoid mistakes that cause major headaches, be sure your attorney is aware of each spouse's retirement accounts and that the attorney examines what rules govern each plan's QDROs, as they vary from plan to plan.

Not including survivor's benefits in the QDRO. If you will be receiving retirement benefits from your former spouse's pension, be sure the QDRO includes Survivor's Benefits, if the plan allows them. Otherwise, those benefits could stop if your spouse dies before you do.

Not paying attention to Social Security benefits/

Not including Social Security benefits in the QDRO. If your spouse makes significantly more money than you do and you've been married ten years or more, you will be eligible for Social Security benefits based on your spouse's work history. That may mean higher benefits than relying on your own work history.

Not insuring the divorced spouse. If you will be relying on your ex-spouse for child support, retirement benefits, alimony, or other financial benefits such as a commitment to pay for your children's college education, take out a life insurance policy on your spouse to ensure the funds will be there should your ex-spouse die. You should be the policy owner, so you will be notified immediately if your ex-spouse is not making the payments. And buy the policy before the settlement is final, so you know whether your ex-spouse is insurable.

Only using a lawyer and an accountant. Hire a Certified Financial Planner™ professional trained in divorce financial issues to work alongside your attorney and CPA. A Certified Financial Planner™ can objectively examine long-range issues such as budgeting, appreciation, and tax ramifications of the proposed settlement assets; as well as the long-term costs associated with settlement proposals. A financial planner, working alongside your attorney and CPA, can help ensure the divorce settlement is financially fair to you.

Sigman Financial Fitness Tip: We all know that divorce creates a huge emotional upheaval for both parties. But this does not excuse you from taking an active role in understanding your finances before, during, and after the divorce. If you need to hire a therapist to work through your emotional issues, so you can effectively address your financial concerns in a calm and objective fashion—it's money well spent. After all, you will live with the financial consequences of your divorce long after the papers are signed. Make sure your judgment isn't clouded by emotion and a desire to "get it over with."

*Lauren Sigman is a Certified Financial Planner™ and President of **Sigman Financial Fitness™**. This column was produced in part by the Financial Planning Association, the membership organization for the financial planning community, and is provided by Sigman Financial Fitness™, a member of the FPA. To learn more about Sigman Financial Fitness™, visit www.sigmanf2.com.*