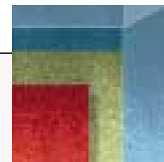
Unwedded Bliss

UNMARRIED COUPLES SHARE MANY OF THE SAME FINANCIAL AND ESTATE-PLANNING CONCERNS THAT MARRIED COUPLES DO, YET THEY HAVE FAR LESS PROTECTION UNDER THE LAW

BY INGRID M. CASE

ILLUSTRATIONS BY FRANCISCO CACERES

Not
Married



Emotion aside, there are plenty of practical reasons why couples choose not to marry. Some stay unmarried because they don't want to upset adult children or interfere with their children's inheritance rights.

Others don't want to jeopardize their eligibility for medical or other insurance, or lose access to Social Security and other government benefits. Still others are philosophically opposed to the institution of marriage. Gay and lesbian couples, of course, can't legally marry in most states; in the states where they can legally marry, the question of how federal law affects same-sex couples is still at issue. "This is an evolving area of law," says Richard Bardy, president of Bardy Law Office in Wayzata, Minn.

But just because two people aren't married doesn't mean they shouldn't seek advice jointly from a planner. In fact, unmarried couples may need a financial adviser more than most married couples do, simply because fewer laws protect their interests while they live together as a couple, when they split, or after the death of one of the partners.

Still, signing on unmarried couples as clients can be more complicated than signing on married couples. The ability to think outside the "married couple" box is one important asset for planners who want to serve these clients. Another is a willingness to put all lifestyle judgments aside. "If a planner is uncomfortable then he or she needs to say, 'This is not my area of expertise,' and refer the client to someone else," says Jill Hollander, owner of Financial Connections in Berkeley, Calif.

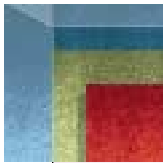
Planners who truly want to attract nontraditional couples as clients should also consider changing the language in their marketing material to include all potential clients. "We don't use the words *husband*, *wife*, or *spouse*. We use *client* and *coclient*, or *client* and *partner*" in brochures and questionnaires, says John LeBlanc, co-owner of Back Bay Financial Group in Boston.

Once unmarried couples become clients, the adviser's main task is to examine those situations in which married couples have the protection of laws or customs but unmarried couples do not—for example, common property, inheritance, custody, power of attorney, ability to make medical decisions, and divorce protections. You'll need to identify alternative solutions that fit each unmarried couple's individual needs in these categories.

Begin by finding out how the couple currently structures their financial lives. Do they mix their money? And how much? This can be a complex issue for unmarried couples; for some, combining finances may seem too much like marriage. But it's important they understand that sharing money is not mandatory to be considered a couple. "It's not wrong if you don't make that choice," says Richard Salmen, a senior adviser at GTrust Co. in Overland Park, Kan. "It's an evolutionary process." If couples don't choose to pool their money, their financial affairs can be viewed as essentially the same as those of two single people. But if the couple does share their money, it's a good idea to get them to draft a domestic-partnership agreement spelling out the extent of that sharing.

A partnership agreement, says LeBlanc, can cover anything the couple wants it to, from who will do the laundry to who will raise the children. Essentially, it says, "These are the ground rules by which we'll run this relationship." But if the partners plan to own real estate or other things in common, the agreement should state the date from which all purchases are considered joint property. Also, the agreement should reiterate or reinforce the beneficiary arrangements spelled out in any retirement plans or life insurance policies.

In addition to identifying how couples plan to share money, a partnership agreement should also state what will happen to assets in the event of a death or a romantic breakup. Though some ownership issues can be handled through wills, trusts, and titles, a partnership agreement makes verbal agreements explicit, thereby protecting both partners. LeBlanc remembers one gay couple who went to court over certain stock options. The options had been granted to one partner, but the other felt he also had a right to them because the two had been together for a long time. "A partnership agreement would have saved them thousands in court costs," LeBlanc says.



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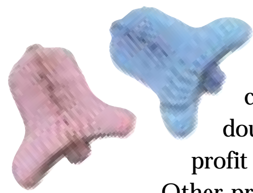


If a partnership agreement is to hold water, however, each partner should have his or her own lawyer review the agreement. Use the same lawyer, says Nancy Frank, founder of Frank Advisory Services in New York, and "it probably won't hold up in court longer than a dimpled chad."

Reliable legal representation and a carefully drafted agreement are also important if children are involved. As a rule, stepparents and partners have no custody rights unless they go through formal adoption procedures. But if a partnership agreement addresses custody arrangements, a court will at least take what's written in the document into account, says Bardy, and view it in light of the best interests of the children.

TAX CONSIDERATIONS FOR UNWED couples are generally more straightforward than custody issues. For example, unmarried couples have no choice but to file individual tax returns—a situation that comes with both pluses and minuses. On the downside, if a couple has no children, neither partner will likely be able to get the tax benefits from filing as head of household. But check with an accountant about individual couples' circumstances; there are some rare exceptions to this rule.

On the upside, no marriage penalty can be imposed on two unmarried partners who both work. Also, charitable contributions made by the couple can be credited to whichever partner needs the deduction more.

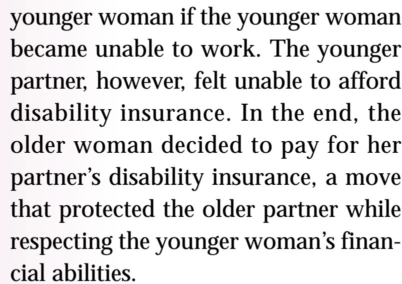
Another possible tax advantage can result if partners share a primary or vacation home. Legally, the ownership of this property can be attributed to whichever partner stands to benefit most from the mortgage deduction—although, admittedly, ceding your ownership interest to your partner for tax purposes requires a great deal of trust. Instead, a pair might want to consider carving the ownership into unequal shares. That way, the partner in the higher tax bracket can get a larger deduction. Or a couple with two houses may choose to each own one outright, so they can take double advantage of the one-time tax-free $250,000 profit individuals can recognize when selling a home.

Other property-sharing options couples might want to consider, especially if one partner already owns a home, include an installment sale of the first partner's interest in the home to the other. Or the first partner might want to consider selling a minority interest in the property to the second partner. A minority holder generally pays a steeply discounted price for his share, Bardy says—typically between 20 and 40 percent of its value.

Whatever the arrangement, it's important that a couple title any property they own jointly in a manner consistent with their individual needs to avoid misunderstandings later. For example, titling the property as a joint tenancy with rights of survivorship allows the home—after the death of one partner—to pass directly to the surviving partner without going through probate. By contrast, titling the home as a tenancy in common allows one partner to buy out the other at some point in the future or sell to a third party, or to leave her share of the property in her will to anyone she chooses.

Regardless of how property is titled, though, Frank notes, to ensure that one partner isn't forced to move out of a house after the death of the other partner, each should have enough money—or carry enough life insurance—to cover any lien on the property. In addition, she says, partners need to make sure that both names are on property and liability insurance and that the amount of coverage is appropriate to the partner with more assets to protect.

Partners should also consider what they will do if one or the other becomes unable to work. Most married people assume that they will care for each other through changing circumstances; it's important that unmarried couples consider the degree of responsibility they want to accept. Peg Downey, a partner with Money Plans in Silver Spring, Md., tells of one lesbian couple who came to see her. One member of the couple was nearly a decade older than her partner, who at the time was just finishing graduate school. The older client was concerned that she wouldn't be able to support the



A domestic - PARTNERSHIP

LAUNDRY TO WHO WILL RAISE THE CHILDREN. ESSENTIALLY,

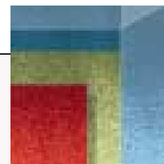
younger woman if the younger woman became unable to work. The younger partner, however, felt unable to afford disability insurance. In the end, the older woman decided to pay for her partner's disability insurance, a move that protected the older partner while respecting the younger woman's financial abilities.

Advance planning is also crucial for unmarried couples who want their partners to make medical decisions for them if they are unable to—particularly if their extended families are not fully in support of the relationship. Sometimes couples don't even realize the extent to which their families disapprove, Hollander says. "Frequently the answer you get is, 'Oh, they have no problem with it,' and then something happens and that's not the case at all," she says.

To fully protect themselves, unmarried couples should grant both durable and medical powers of attorney to their partners. A few states allow someone who holds a durable power of attorney to also make medical decisions; others, such as Kansas, require a specific medical proxy. "If your partner is lying in a coma and needs surgery, you have no say without a durable power of attorney and a medical power of attorney," Salmen says. Such documents should state that this person is the partner of the other and has the right to make medical decisions, determine who may and may not visit, and handle all of the ailing person's financial affairs during the course of an illness. An advance health-care directive, also known as a living will, can further clarify the decision-making process.

Then there's the matter of the will. If one member of an unmarried couple dies without a will, that person's biological family—not the unmarried partner—will almost certainly get any assets that aren't held in joint tenancy. For that reason, it's absolutely crucial for unmarried partners to make ironclad wills. "They're just hung out to dry if they don't do it," Salmen says. What's more, the wills should clearly and explicitly spell out not only how a partner wants the property disposed, but also how he doesn't want the property disposed. For example, Hollander suggests that clients may even want to go so far as to disinherit family members who aren't being included as heirs as well as include a no-contest clause disinheriting anyone who contests the will. Wills should also explicitly describe custody arrangements for minor children.

Even careful planning may not stop determined family members from making legal trouble, however. So whenever possible, efforts should be made to avoid probate. To that end, make sure all insurance policies name a beneficiary, so the money will go directly to that individual. If no beneficiary is named and the estate becomes the beneficiary instead, the money will go through probate, which in turn will give family members a chance to fight over it. Also consider titling other assets so that they pass directly to a partner. Securities and real estate, for example, can be titled under joint tenancy with the right of survivorship (for more information, see "Keep It Simple," page 30), and



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bank accounts can list a pay-on-death beneficiary. These arrangements typically keep the money from passing under the noses of greedy family members.

Another way to avoid probate is for the partners to establish trusts for each other—typically a grantor-retained income trust, a grantor-retained annuity trust, or for the charitably inclined, a charitable remainder trust. The appeal of these trusts is that the money in them passes directly to the beneficiary at the time of the donor's death. Setting up one of these trusts also allows a client to control what happens to the money after his partner dies—an important consideration if the client wants his family or a specific charity to receive his money once his partner can no longer use it. "With a trust you can speak from the grave," says John Henry McDonald, president of Austin Asset Management Co. in Austin, Tex. LeBlanc remembers two gay clients, both HIV-positive. When client A died of AIDS, almost all his assets went into a trust for client B, with client A's family named as the residual beneficiary. Then client B fell ill and died six days after the funeral of client A, LeBlanc says. Instead of the money going to client B's relatives, under the terms of the trust the $1 million estate went to client A's family.

Unfortunately, avoiding probate is not the same as avoiding estate taxes. Unmarried couples are at a particular disadvantage in this area because they don't qualify for the unlimited marital deduction, the rule that allows a married couple to give each other unlimited assets without paying estate taxes. In fact, because estate taxes are governed by federal law, unmarried couples can't even hope for any relief on this front by the passage of domestic-partner legislation in their state. The adviser's job, therefore, is to make sure the estate gets whittled down as close as possible to the applicable exclusion amount—that is, the amount someone can give away during his lifetime or at death without triggering gift or estate tax ($1 million for 2002).

There are a number of ways to accomplish this. You can, for example, encourage wealthy clients to make the largest allowable tax-free gift—currently $11,000—to their partners annually. True, that amount may not make much of a dent in a very large estate or over a short period of time, but over many years this method makes it possible to give a substantial sum to a partner. If a client wants to give some assets to other family members, these gifts should also be made during the client's lifetime, if possible. After all, individuals can give annually an unlimited number of tax-free gifts of $11,000 or less, as long as only one gift goes to each recipient.

And don't forget about life insurance. In particular, make sure your wealthiest clients consider setting up irrevocable life insurance trusts, which can provide a means of keeping the life insurance proceeds out of their taxable estates and give the beneficiaries a pile of cash to pay whatever taxes are due on the rest of the estate. When putting together financial plans for unconventional clients, in other words, sometimes conventional estate-planning tools, like life insurance, can be as effective as more unconventional tools.

Ingrid M. Case is a freelance writer and author of Your Own Two Feet (and How to Stand on Them), *a guide to life after college published by St. Martin's Press.*