

Prenuptial Agreements Part 1 of 2

What issues are addressed in a prenuptial agreement?

A prenuptial agreement should include you and your spouse's decisions in four basic areas:

1. **Assets and liabilities**--What assets are you each bringing into the marriage? How much are they worth? Who owns them? Which ones will become marital property and which ones will continue to be owned by you or your future spouse individually? Will gifts and inheritances be shared or kept separate? What liabilities do you each have, such as back taxes or other debt?
2. **Divorce**--Will there be alimony or a lump-sum payment? Will you divide or exempt appreciation of assets brought to the marriage? How will you divide assets purchased from joint funds?
3. **Estates**--What will go to children from a previous marriage or children you may have in the future? Who gets what after either spouse dies?
4. **The contributions of each partner**--How will you compensate for special contributions, such as one spouse limiting a career or losing pension benefits due to childrearing responsibilities? How will you compensate for one spouse bringing in more liabilities to the marriage?

Some of the Strengths of this agreement?

1) Protects your premarital property

If you combine your assets with those of your spouse after you get married, you risk losing them in the event of divorce. To preserve your premarital property, keep all of your assets in your own name after you are married and designate ownership of your property in a prenuptial agreement. Keep in mind that joint ownership can make your assets marital property, which is subject to a property settlement.

2) Enables you to provide for your family members

A prenuptial agreement can give you the security of knowing that your loved ones will be provided for in the manner in which you intend. If you have children and decide to remarry, such an agreement can ease the fears of your children over how your estate is going to be divided. A [trust](#) is a particularly useful tool in remarriage when you want to provide for your spouse after you die, but make sure your money ultimately goes to your own children, not your spouse's children. When used in conjunction with a prenuptial agreement, a trust eliminates or greatly reduces the possibility of a challenge by your spouse or other heirs, reduces legal costs, and avoids scrutiny by the court.

3) Reduces or avoids litigation costs

Considerable amounts of money can be lost by both spouses when divorce proceedings turn into a long, messy battle. By explicitly stating how property should be divided in the event of [divorce](#), however, both sides can greatly reduce the fees charged by attorneys, expert witnesses, and appraisers. A prenuptial agreement can also reduce litigation costs associated with contesting the will of a deceased spouse. Caution: Litigation costs may be a factor, however, if there is a breach of contract claim associated with the prenuptial agreement during divorce proceedings.

4) Offers you protection against your future spouse's creditors

If your future spouse incurred substantial debt prior to marriage, you may wish to protect your assets from his/her creditors. This can be accomplished in a prenuptial agreement by having your future spouse waive any claims to your assets, except in the event of divorce or death. Another option is to set up a trust in conjunction with a prenuptial agreement. Assets placed in the trust prior to your marriage would not be owned jointly with your spouse and could not be considered marital property. Your spouse's creditors would therefore have no claim on your assets, but your own creditors might be able to go after them.

5) Enables you to protect your business assets

In cases where a business is owned by a small number of parties (e.g., a closely held business or a partnership), the owners may wish to prevent a spouse from obtaining voting rights or claims against the business. In such cases, the owners can enter into an agreement that requires each, in the event that they marry, to execute a prenuptial agreement in which the prospective spouse waives all rights to the owner-spouse's interest in the business in the event of divorce or death.

The co-owners may also wish to enter into a [buy-sell agreement](#), whereupon the death of a shareholder or partner, the remaining owners would be required or given the first option to purchase the decedent's interest in the business for a specified amount over a specified period of time.

What is a prenuptial agreement?

A prenuptial agreement (also known as a premarital agreement, ante marital agreement, or prenupe) is a binding contract executed by prospective spouses to define the rights, duties, and obligations of the parties during marriage and in the event of legal separation, annulment, divorce, or death.

When should it be considered?

Draw up a prenuptial agreement before you get married. Financial planners generally recommend that couples consider entering into a prenuptial agreement before marriage if they have substantial assets (especially if there is an imbalance in their assets), if one or both may inherit substantial assets, or if they have children from previous marriages. Small-business owners and the elderly are also strong candidates for prenuptial agreements, as well as couples in which one spouse will be supporting the other spouse through professional school (e.g., law or medical) so that the supporting spouse will share fairly in the professional's future income. If the prospective spouses are young and have comparable net worths, an agreement may provide little benefit. As a precaution, however, most couples should at least discuss the issue with a financial advisor before getting married.

What are some of the Tradeoffs?

1) Prenuptial agreements can become outdated

What was fair the day you got married could be completely unfair a few years later. The birth of children that requires one spouse to leave work, or a move that is advantageous to one spouse and detrimental to the other, are examples of changes that could affect the fairness of the agreement. Once the balance shifts, a judge is likely to void the contract, and his or her determination of fairness--not yours--will prevail.

The good news is that, like any legal contract, a prenuptial agreement can be amended or modified to meet you or your spouse's needs as conditions change during the marriage.

Tip: As a precaution, review and update your prenuptial agreement every few years or following significant events such as a change in economic circumstances or the birth of children.

2) Relationships between your future spouse or family members may be damaged

Prenuptial agreements are far less likely to damage relationships between couples and their families when they are negotiated for people who have been previously married and who have children from previous marriages. In these cases, each party has loyalties to third parties--usually their children--and each has a legitimate interest in protecting the rights of their children to inherit his or her estate.

A more difficult situation can arise when a prenuptial agreement is negotiated between two people who have never been married before and have no children or third parties they are obligated to support. In such cases, the agreement is often negotiated at the suggestion of the parents, whose concern may be to minimize any financial risk incurred by their child as a result of his or her marriage. In this case, a family's suggestion to create an agreement could be construed as hostility or distrust.

Things to keep in mind when preparing an agreement.

1) **Allow plenty of time between the signing of the prenuptial agreement and the wedding**

In order for a prenuptial agreement to be valid, it should be written only after you and your future spouse have had enough time to negotiate satisfactory terms. If you wait until the night before the wedding to give your future spouse a prenuptial agreement to sign, it probably won't be considered valid later on, should it be contested.

2) **Obtain independent counsel**

It is advisable that you and your spouse be represented by separate attorneys. If one attorney handles everything for both of you, a court will probably rule that your spouse was not adequately represented, and the prenuptial agreement will be disregarded.

3) **Provide full and accurate disclosure of financial information**

It is key to obtain full and fair disclosure of income, assets, and liabilities.

Caution: If you are getting divorced and your spouse uncovers assets that you did not declare in your prenuptial agreement, a court may not uphold the contract. Both parties must also be thorough about disclosing any debts and financial obligations, including child support, alimony, or back taxes.

4) **Make sure the agreement is free of any hint of duress**

The court is likely to throw out any agreement that it determines was made under emotional stress, physical or mental disability, or threat of force.

5) **Be fair**

If your spouse is dependent on you financially, the provisions of your prenuptial agreement cannot leave them destitute in the event of divorce.

The fairness of an agreement, however, varies from state to state. Although several states have adopted the Uniform Premarital Agreement Act's requirement that a prenuptial agreement not be unconscionable at the time it was executed, other courts have held that the agreement must be fair at the time of divorce. Some states require that it be fair both at the time of execution and at the time of divorce.

6) **Distinguish between marital property and separate property**

A prenuptial agreement should clearly differentiate between marital property and separate property. Marital property generally includes all assets that were acquired by either or both spouses during the marriage. Separate property falls into three categories: what you bring into the marriage, what you inherit during the marriage, and what you receive during the marriage as a gift.

7) **Consider including a "triggering event" within the agreement**

When included in a prenuptial agreement, a triggering event (e.g., the sending of a registered letter) could be used to automatically initiate divorce proceedings. It would also distinguish between marital property and separate property as of the date of the event. Such a strategy could work to your advantage, especially if your agreement is based on providing your spouse with a percentage of your wealth and you are anticipating future earnings or an inheritance

Part 2 of this series will address the tax ramifications of this arrangement and some FAQs...