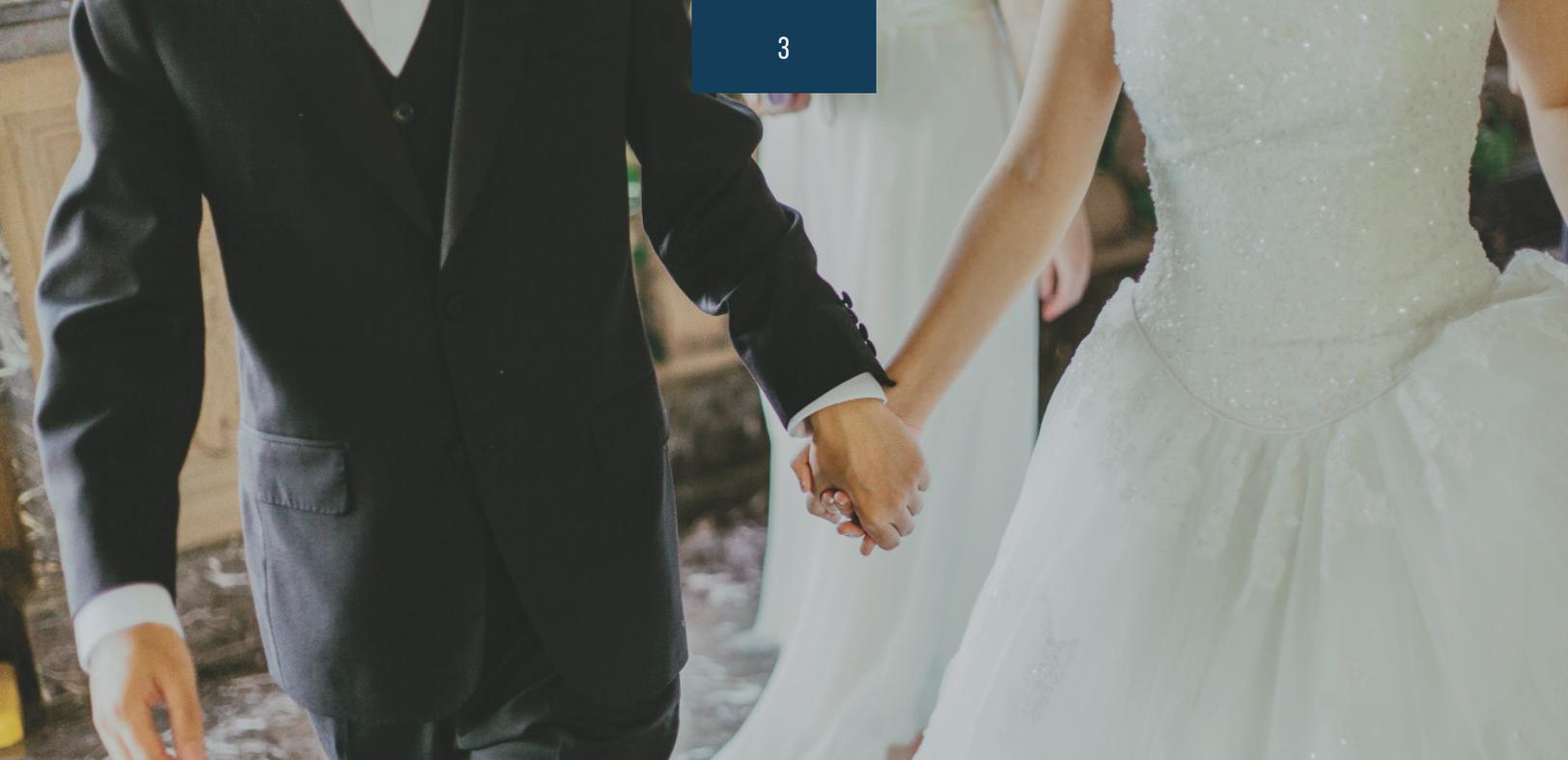




SHOULD YOU SIGN A PREMARITAL AGREEMENT?

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I. WHAT IS A PREMARITAL AGREEMENT?

A premarital agreement is a written contract between two people who intend to marry that affects their financial rights and obligations while they are married, if they separate or divorce, or when one of them dies. In a premarital agreement, a couple can agree to alter the rights and obligations they otherwise would have to each other as spouses. A premarital agreement is also known as a prenuptial agreement (a prenup) or an antenuptial agreement.

II. WHAT SUBJECTS CAN BE COVERED IN A PREMARITAL AGREEMENT?

State law dictates what subjects can be addressed in a premarital agreement. The specifics can vary from state to state so it's important to consult an attorney in your state to determine what provisions your state courts will uphold. Furthermore, each party should have a separate attorney at all stages of drafting and signing a premarital agreement. A premarital agreement is more likely to be upheld if each party had an independent attorney.

As a general rule, in a premarital agreement prospective spouses can:

- Relinquish rights to the other spouse's income and property that they would typically acquire as a result of the marriage.
- Relinquish the right to inherit from a deceased spouse.
- Determine how property and liability for debts will be distributed between them should the marriage fail.
- Relinquish the right to alimony or agree on how much alimony one spouse will pay the other.

- Determine whether one spouse will or will not be obligated to pay the other's attorneys' fees if they separate or divorce.

Provisions for custody and support of children born during the marriage are sometimes included in premarital agreements. However, a court will not enforce these provisions if they are not in the best interests of the children.

Courts typically refuse to enforce provisions regulating the behavior of the spouses during their marriage. These include provisions for living allowances and household expense accounts, division of chores, maintenance of personal appearance, and sexual activities.

III. WHO CAN BENEFIT FROM A PREMARITAL AGREEMENT?

When you think about premarital agreements, you may imagine the stereotypical situation: a wealthy celebrity or titan of business demands a premarital agreement to protect the family fortune from a fiancée of modest means. However, you don't need to be rich to benefit from a premarital agreement.

You may find a premarital agreement especially valuable if:

- You are an older or mid-life person who has accumulated significant assets that you want to protect if you divorce. The more assets a person owns, the more critical a premarital agreement becomes.
- You want to avoid a contentious and costly fight over property and alimony if you divorce.
- Your prospective spouse has significant debt or money management problems.
- You have children from a prior marriage or relationship to whom you want to leave your estate.
- You own a business.

Some people resist a premarital agreement because they view it as an admission that the marriage is likely to fail. On the contrary, a premarital agreement can increase the likelihood that a marriage will succeed. A premarital agreement presents a couple with an opportunity to have a realistic discussion about how they expect to manage their finances and who they want to inherit their property. False assumptions can be exposed and examined before the marriage. Thus, the chances of marital conflict are reduced.

A young couple will not usually have as great a need for a premarital agreement as a more mature couple or a couple on a second or subsequent marriage. However, even a young couple should consider the issue before foregoing a premarital agreement.

Example: Bret and Sasha married after they graduated from college. Sasha was an art major and could not find a job. A resourceful and energetic person, she created a job for herself. She started cleaning houses in an upscale neighborhood. Sasha had a knack for business and soon had three employees and a successful company.

Although Sasha's business enjoyed success, the same could not be said for her marriage. Bret sued for divorce, spousal support, and half the value of her business. He won. Sasha could have achieved a better outcome with a premarital agreement.

A premarital agreement presents a couple with an opportunity to have a realistic discussion about how they expect to manage their finances and who they want to inherit their property

IV. HOW MARRIAGE AFFECTS PROPERTY OWNERSHIP

To understand why premarital agreements are important, you need to understand who owns the property in a marriage and how it would be divided on divorce absent an agreement between the spouses. When you get married, what was once yours can become “ours.”

In a marriage, property is typically classified into one of three categories: separate property; marital or community property; and mixed property. These classifications become important if a divorce occurs because they determine what property is part of the marital estate that is divided between the spouses.

A. Separate Property

Separate property is property that you own when you enter the marriage and property that is given to you (and not also to your spouse) as a gift or inheritance during the marriage. If you divorce, you are entitled to all of your separate property.

B. Marital or Community Property

Property that is acquired during marriage other than by gift or inheritance is marital property or community property if you live in a community property state. Both spouses own an interest in the property. The efforts of one spouse are considered to be the efforts of the marital team.

Property has a broad definition. It includes everything of value a person can own. Real estate, personal property, salaries, income from investments, and retirement accounts can all be marital property.

Example 2: Consider Sasha and Bret from Example 1. Bret was not involved in Sasha's cleaning business. However, the cleaning business is marital property since Sasha started it during the marriage. Her hard work is a marital asset that was used to increase the cleaning business's value.

Similarly, income earned by either spouse during the marriage is marital property as is property purchased with such income.

Example 3: Derek and Marta are married. Derek is employed as a high school teacher. His income is marital property. If he uses his paycheck to buy a sofa, the sofa is marital property that belongs to both Derek and Marta.

C. Mixed Property

Separate property can become mixed property if it increases in value during the marriage. The property's value when you entered the marriage remains separate, but any increase in value can become marital property. Property can increase in value for one or two reasons, passive appreciation or active appreciation.

1. *Passive Appreciation*

Passive appreciation occurs due to market forces with no use of marital assets.

Example: Before her marriage, Lisa bought a painting by an unknown painter for \$200. When Lisa marries Ethan, the painting was consigned to their attic. Two years have passed and the formerly unknown painter is now the rave of the art world. The painting is worth a small fortune. The painting's value increased because of market forces, not because marital funds or assets were used. Therefore, the increase in the painting's value is passive appreciation and generally not marital property.

2. *Active Appreciation*

Property can increase in value due to active use of marital assets. Remember, one spouse's efforts are considered an expenditure of marital resources.

Example: Morgan purchased an old hotel that was built during the 1860s. The hotel was vacant and in poor condition. However, it was a piece of history and Morgan wanted to restore the hotel and make it a viable business.

After purchasing the hotel, Morgan married Patrick. Morgan and Patrick used money each earned during the marriage to restore the hotel. The decrepit building became a tourist attraction. The hotel is now a thriving business. The hotel's increase in value is due to the active effort of both partners. The hotel is mixed property.

Suppose instead that Patrick did not put any money or effort into the hotel. Morgan invested her sweat equity and money from a few investors in restoring it. The hotel is still mixed property because marital assets were used in restoring it. The assets were Morgan's labor and efforts to attract investors.



D. When a Divorce Occurs

When a couple divorces, their marital or community property is divided between them. They can agree on how to divide the property. If they can't agree, a court will decide for them.

In community property states, a court is usually required to make an equal division. In non-community property states, the court may order an unequal division to achieve a fair result. The court may consider various factors such as the length of the marriage, how much separate property each spouse has, and each spouse's age, health, earning capacity and ability to be self-supporting. When one spouse has unfairly dissipated marital assets (e.g., gambling debts or gifts to a paramour), the court may make an unequal division in both community property and equitable division states.

Example: Sasha started her cleaning business during her marriage to Bret. Her labor and wages were marital resources. Consequently, the business is marital or community property. If Sasha and Bret divorce, Bret can be awarded a share of the company's value.

Example: Lisa purchased her painting before the marriage. No marital funds or efforts increased the painting's value. The painter achieved fame without Lisa's help. The painting was Lisa's separate property. The increase in value is passive. Lisa receives the painting's full value when she and her husband divorce.

Example: Morgan is entitled to the \$25,000 she spent on buying the hotel when she and Patrick divorce. However, the increase in the hotel's value due to her efforts during the marriage could be classified as marital property. So, assume the hotel is now valued at \$500,000 due to the renovations.

The arithmetic could work this way if the marital or community portion of the property is divided equally:

- + \$500,000 (Value of hotel)
- - \$25,000 (Amount Morgan paid for the hotel before the marriage, separate property)
- - \$200,000 (Amount due investors)

\$275,000 (Marital property).

This means when the court divides the property, Morgan receives the following amount.

- \$25,000 (Hotel's value when she entered the marriage)
- + \$137,500 (Half the marital property value of the hotel \$275,000/2)
- \$162,500 (Morgan's share of the hotel after property division by the court)
- \$137,500 (Patrick's share of the hotel in property division by the court.)

There are two ways to look at Morgan's share of the hotel after the court divided the property. Morgan invested \$25,000 and walked away with \$162,500, not bad. On the other hand, she lost \$137,500 that Patrick was awarded by the court. Certainly, Morgan would have preferred to keep the \$137,500 that Patrick received as a share of the hotel's value, which she might have been able to do with a premarital agreement.

V. PROBLEMS A PREMARITAL AGREEMENT CAN RESOLVE

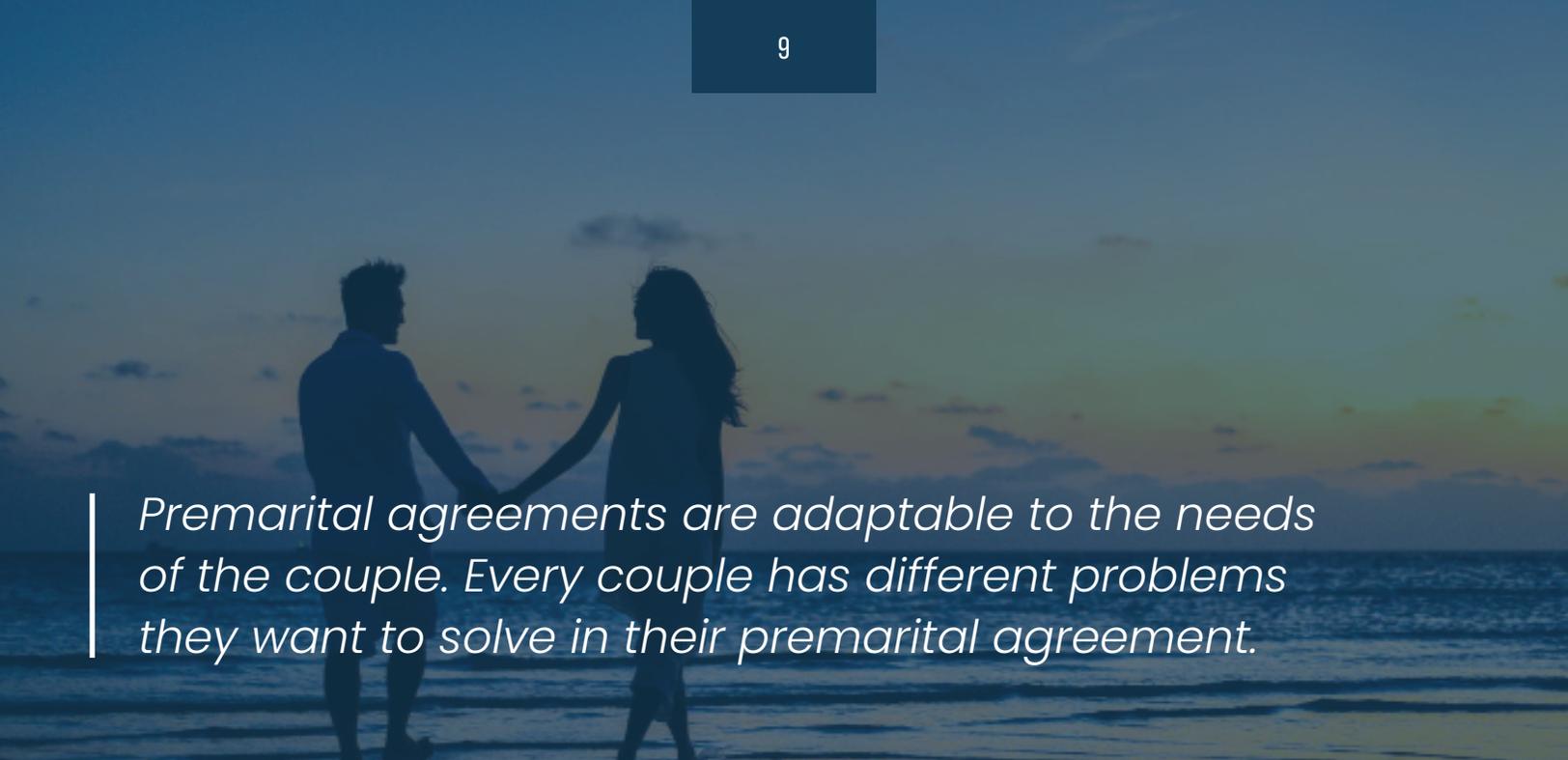
Premarital agreements are adaptable to the needs of the couple. Every couple has different problems they want to solve in their premarital agreement. Here are some of the most common.

A. Preserving Assets during Marriage and on Divorce

Problem 1: You want to avoid an expensive and contentious court fight over property if your marriage fails.

Couples can use a premarital agreement to avoid a court battle over their property division. A court battle can be emotionally exhausting and very expensive. Some divorces cost more than a destination wedding or honeymoon trip. Marital property can be eaten away by attorneys' fees and both spouses are the losers.

Example: Kevin and Phoebe plan to marry. This is Kevin's second marriage. Kevin's divorce was bitter and costly. The combined attorneys' fees for Kevin and his former wife, which Kevin had to pay, topped one-third of the value of their marital property. This time around, Kevin does not want to endure a divorce trial and again see a big chunk of marital assets go to attorneys' fees. Kevin and Phoebe can enter into a premarital agreement that determines their property division if the marriage fails. Kevin and Phoebe can also agree that each will pay his or her own attorneys' fees.



Premarital agreements are adaptable to the needs of the couple. Every couple has different problems they want to solve in their premarital agreement.

Problem 2: You want to keep the assets you entered the marriage with if you divorce.

The average age of first marriages has been rising sharply since the 1980s. Many people have acquired considerable assets by the time they marry—a home, an investment portfolio, artwork, or antiques. Understandably, someone who enters a marriage with significant hard-earned assets would like assurances that they will not be awarded to the other spouse on divorce.

A premarital agreement can contain a list of items that will remain each spouse's separate property. Over the years memories can dim and spouses can dispute whether property was acquired before or during the marriage. The list avoids these disputes. The agreement can also contain a clause that allows appreciation of separate property to remain separate property, even though marital money and efforts created the increase the property's value.

Example: Barbara and Ted are professionals who married in their late thirties. They signed a premarital agreement that provides that the property each owned before the marriage, including appreciation and income earned by the property, will remain separate. At the time of the marriage, Ted owned a rustic lakeside cabin valued at \$80,000. During the marriage, Ted extensively remodeled the cabin to make it a comfortable vacation home. Ted used his salary and sweat equity to pay for the remodel. When Ted and Barbara divorce after 10 years of marriage, the vacation home is worth \$250,000. The vacation home belongs to Ted and he does not have to share the \$170,000 of appreciation with Barbara.

Problem 3: You have income that you regularly invest. You want the investments and any earnings your investments generate to remain your separate property.

A premarital agreement can provide that any income received by a spouse, whether earned income or investment income, is that spouse's separate property. Consequently, the spouse can retain the profits from investing his or her income.

Example: When Linda married Tim, she owned a luxury condo. During the marriage, she rented the condo to tenants. Linda deposited the rent payments in a mutual fund. Their premarital agreement provides that the property each owned before the marriage, any appreciation of that property, and any income earned by that property will remain separate. Their agreement also provides that each party's income is his or her separate property. When the parties divorce, the condo and the mutual fund belong to Linda. Tim is not entitled to a share.

Problem 4: You or your parents have furnished the down payment on a home for you and your spouse. You want to make sure the down payment is returned to you if the marriage fails.

Example: Neil and Kathy are engaged. Kathy's parents want to help them purchase their first home. They give the couple \$80,000 for a down payment. Kathy's parents think Neil will be a good husband and expect the marriage to succeed. But if it doesn't, they want to know that Kathy will leave the marriage with their down payment. A premarital agreement can provide that if Neil and Kathy divorce, the down payment must be returned to Kathy before any remaining equity in the home is divided between them.

B. Alimony

Problem 5: You don't want to pay alimony. Or you are willing to pay alimony, but you want the amount to be predictable. Or you are the less wealthy spouse and want to ensure that you will receive reasonable alimony.

If spouses have unequal wealth, income, or earning power, the poorer spouse may be entitled to alimony (also known as spousal support) from the wealthier spouse if the parties divorce. In deciding whether to award alimony and how much to award, courts consider several factors, such as:

- The recipient spouse's need for support and ability to become self-supporting.
- The length of the marriage.
- The other spouse's ability to pay.
- The lifestyle enjoyed by the parties during the marriage.

Judges have a lot of discretion regarding how much alimony to order. The amount can be unpredictable. In a premarital agreement, prospective spouses can agree on how much alimony one spouse will pay to the other and how the payment is to be made. For example, the payment can be made in a lump sum, or over a specified time. One common measure is to make alimony payable for half the length of the marriage.

Alternatively, the spouses may have roughly equal assets and earning abilities. In this case, they each may want to waive the right to receive alimony from the other in their premarital agreement.

Alimony limitations and waivers are based on the spouses' situation at the time of the marriage. That situation can change dramatically. Thus, courts closely scrutinize alimony provisions in premarital agreements and they may refuse to enforce any that would leave a spouse without sufficient funds to live on. Courts typically refuse to enforce alimony waivers if, as a result, a spouse will be so impoverished that he or she will require public assistance.



C. Debts

Problem 6: You are concerned about your prospective spouse's spending habits and want to protect yourself from liability for his or her debts.

Disputes about money and debt are often at the root of marital discord and divorce. If your intended is bringing a lot of debt to the marriage or you know he or she has extravagant spending habits, you may want to include a provision that deals with debt in your premarital agreement.

Each spouse is legally responsible for debts incurred before the marriage. The liability of spouses for debts incurred after the marriage depends on whether they live in a community or non-community property state. In a community property state, both spouses are liable for all debts incurred by either, even if the debt is not on a joint account and even if one spouse knows nothing about it. In a non-community property state, both spouses are equally responsible for jointly incurred debts (e.g., a joint credit card or promissory note that each signs) but each spouse is solely responsible for separately incurred debts. However, both spouses are jointly responsible for a separately incurred debt for necessities such as food or clothing.

Your agreement can affirm that premarital debts are to be paid by the spouse who incurred them. It can specify who will pay specific debts during the marriage and on divorce. The agreement can require a party not to take on any new debt without the other party's knowledge and approval.

A premarital agreement won't prevent creditors from coming after you for your spouse's debts. But a premarital agreement will give you the right to make your spouse reimburse you for any debts you pay that were your spouse's responsibility.

D. Retirement Accounts

Problem 7: You want to keep all your retirement savings should you divorce.

When spouses-to-be have similar incomes and earning capacities, they may prefer to provide for their own retirements. A premarital agreement can contain a provision in which each party waives all interest in the other party's retirement accounts that would be acquired by marriage.

A waiver in a premarital agreement may be effective for IRAs and private retirement accounts. You should check with your attorney to see if such waivers have been upheld in your state. But a waiver in a premarital agreement may not be effective for employer-provided ERISA retirement plans. If you have an ERISA plan, the waivers should be executed after you are married because ERISA requires that the waivers be executed by "spouses."

Your attorney can contact your Plan Administrator to get the proper waiver forms to be executed after you are married. Your premarital agreement can contain a promise that you and your spouse will execute the waivers after your marriage, although it's not clear that a court would enforce the provision.

Waiving all interest in a spouse's retirement may seriously disadvantage a lower-earning spouse or a spouse who may take time from the workforce to raise a family. He or she could end up with little retirement security. If you are in this situation, consider carefully whether to sign such an agreement. You and your attorney may be able to negotiate a better arrangement. See VI. Fairness Issues When One Party Has All the Wealth.

E. Keeping Assets in the Family

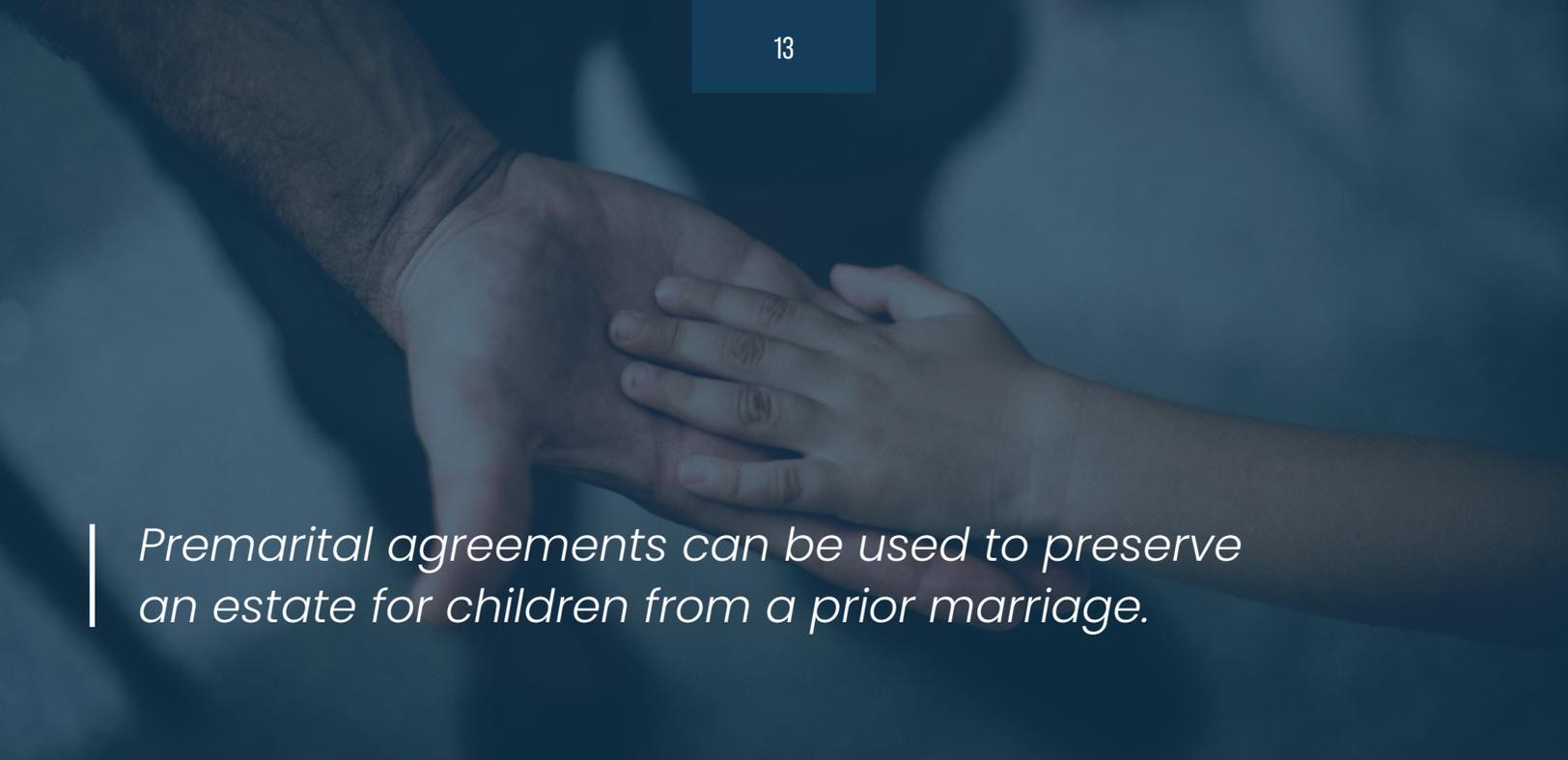
Problem 8: You want to keep an heirloom or other assets in the family should you divorce or die before your spouse.

Example: Alexis and Robert are engaged. Robert has two daughters from his first marriage. Robert wants his home, where he and Alexis will reside, to go to his daughters when he dies. In a premarital agreement, Alexis can waive any property rights she would otherwise acquire in the home because of her marriage to Robert. The agreement can provide that the home and any appreciation in its value will remain Robert's separate property if Robert and Alexis divorce. He can then leave it to whomever he pleases. To further protect his daughters' inheritance, Robert will also want Alexis to waive her state inheritance rights. Waiver of state inheritance rights is discussed in Problem 10 later in this section.

Problem 9: You are expecting to receive an inheritance that you want to pass to your children or other family members.

Premarital agreements can deal not only with assets a person currently has but assets that may be acquired in the future.

Example: Christine's parents own a farm that has been in the family for several generations. Christine expects to inherit the farm on her parent's death. Christine wants the farm to pass to any children she has with Steve, her fiancé. If they are childless, Christine wants her nephew to receive the farm. Through a premarital agreement, Steve can waive any ownership interest in the farm he would acquire by the marriage and any rights he has to inherit from Christine.



Premarital agreements can be used to preserve an estate for children from a prior marriage.

Problem 10: You want to leave all or a substantial portion of your estate to children from a prior marriage or relationship.

Premarital agreements can be used to preserve an estate for children from a prior marriage. State law provides a surviving spouse with a right to a share of the deceased spouse's estate. The specific inheritance rights of a surviving spouse vary from state to state.

A surviving spouse may be entitled to a specific percentage of deceased spouse's estate, a living allowance, a right to live in the family home for years or life, or some combination of these. One spouse cannot deprive the other of his or her state inheritance rights with a will or trust. If the deceased spouse left the surviving spouse less than he or she is entitled to by state law, the surviving spouse can make a claim against the estate for the balance (sometimes known as an election to take against the will).

In a premarital agreement, the prospective spouses can waive their rights to each other's estate. A prospective spouse's waiver of inheritance rights does not mean that he or she cannot receive an inheritance from the other spouse. The spouses are free to provide for each other in their estate plans. The waiver simply means the surviving spouse cannot claim inheritance rights that would provide him or her with more than the inheritance the deceased spouse provided.

Example: Recall Robert and Alexis from a previous example. After he and Alexis marry, Robert executes a will leaving the family home and 90 percent of his estate to his daughters from a prior marriage. The remaining 10 percent of his estate he leaves to Alexis. The law of the state where Robert and Alexis live gives a surviving spouse the right to one-third of the deceased spouse's estate when the deceased spouse left a will. Without a premarital agreement, Alexis can elect to take against the will leaving only two-thirds of Robert's estate for his children. In a premarital agreement, Alexis can waive her state inheritance rights so that Robert's will can be honored.

If you plan to disinherit or partially disinherit a spouse, make sure you follow through with the appropriate estate planning documents once your premarital agreement is signed.

F. Business Owners

Problem 11: You want to be able to manage your business free from your spouse's interference.

A premarital agreement can allow each spouse to operate any business he or she owned before the marriage as separate property. Without a premarital agreement, both spouses may be required to sign business documents such as deeds, contracts, and promissory notes.

Example: Frank owns a tire store. He wants to sell the tire store and open a sandwich shop. Frank owned the tire store before his marriage. The tire store is making money. Frank's wife, Trisha, does not support Frank's desire to open a sandwich shop. She believes that opening a sandwich shop will require more money than Frank can get from selling the tire store.

Although the building that houses the tire store is in Frank's name, he may still need Trisha's signature on the deed to sell the building. A premarital agreement could have allowed Frank to sell his property without Trisha's consent.

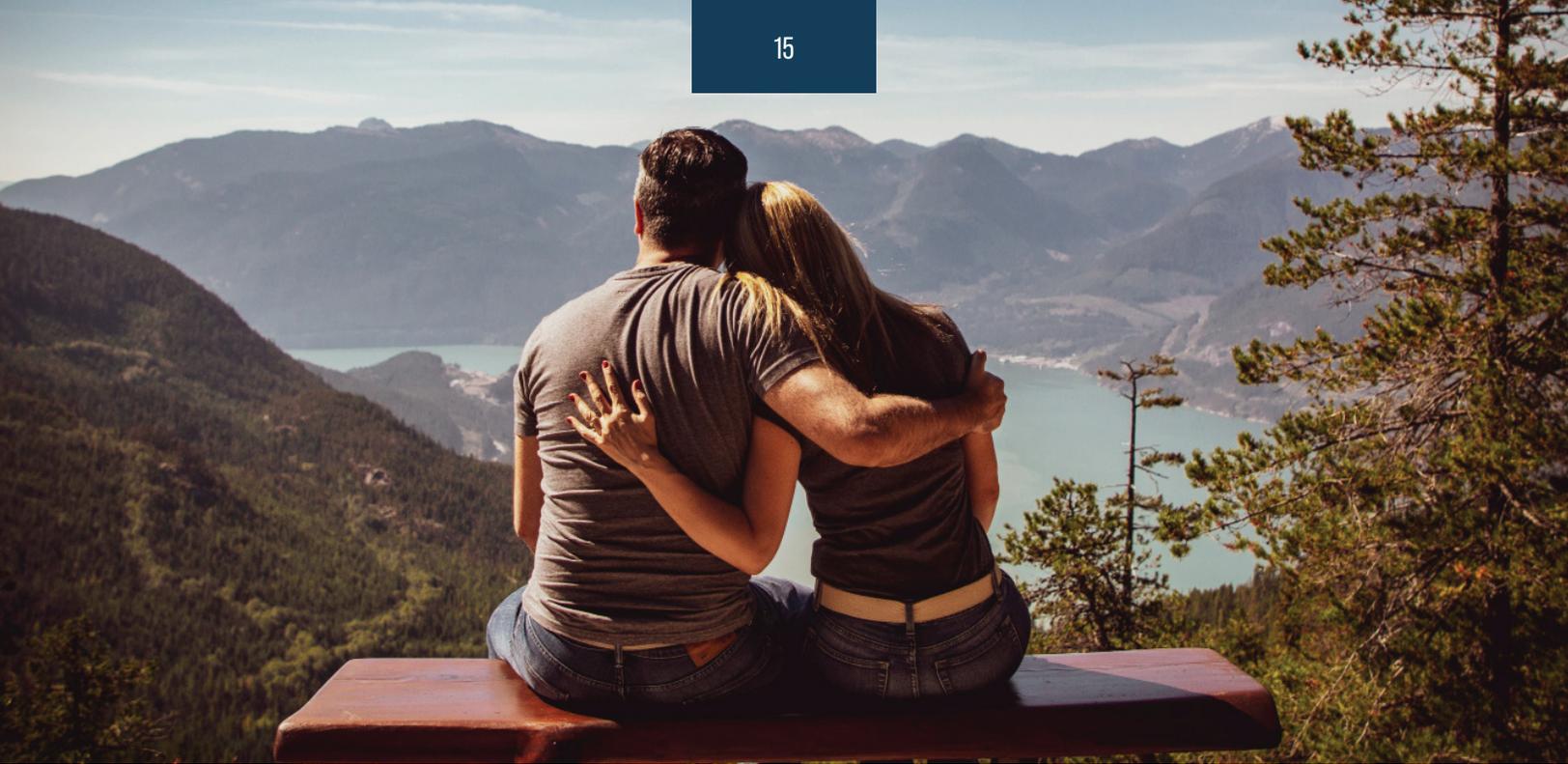
Example: Jane owned a print shop when she married Bob. After her marriage, she continued to run the shop without Bob's involvement. Unfortunately, the shop suffered a fire and insurance proceeds did not cover the entire loss. Jane wants to borrow money to cover the additional expenses of repairing the print shop. The bank requires Bob's signature on the loan. Bob sees no future in the print shop and refuses to sign the bank loan.

A premarital agreement might have solved two problems for Jane and Bob. If Bob had waived his interest in the print shop in a premarital agreement, Bob would not need to sign the loan. Only Jane's signature would be needed. Additionally, a potentially marriage ending conflict could have been avoided. Bob would have known before he married Jane that Jane intended to run the business independently and that he would have no say in it.

Problem 12: You want to prevent your spouse from acquiring an interest in your business that you will have to buy out if you divorce.

A business can be devastated when business assets are lost during a divorce. In a premarital agreement, the non-owner spouse can agree that he or she will acquire no interest in the business through the marriage even if he or she works in the business.

Example: Recall hotel owner Morgan from an earlier example. Before her marriage, she purchased an old hotel. After the marriage, she built it into a successful business. Now that she and her husband Patrick are divorcing, she has to pay him \$137,500 for his interest in her business. This payout puts a significant crimp in Morgan's business plans. She was planning to open a day spa for her guests. She now has to put her plans on hold. If Morgan doesn't have the cash on hand to pay Patrick, she may have to borrow against her business. She could have trouble securing a loan because she already owes her investors \$200,000. She may get the loan, but not with the best terms. The extra debt could endanger her business if an economic downturn occurs. In the worst-case scenario, she could have to sell her business. A premarital agreement could have provided that Morgan's business and any appreciation of it remained her separate property. When she and Patrick divorced, Patrick would have had no claim to it.



VI. FAIRNESS ISSUES WHEN ONE PARTY HAS ALL THE WEALTH

A premarital agreement need not provide as little as the law permits for the less wealthy spouse. A more balanced agreement may be a better choice for the health of the marriage and may prove more effective in the long run.

A premarital agreement allows the parties to waive the rights they would otherwise have to marital or community property and support on divorce or the death of one of them. When the parties' financial situations are comparable, a mutual waiver of these rights can be a win-win situation. Each party protects his or her separate property, investments and retirement savings, business interests, family heirlooms, and the inheritance of children from prior marriages.

The result is different when one party has far less wealth than the other. A premarital agreement can put the poorer party in a much more precarious financial situation than he or she would otherwise experience. Consider the less wealthy spouse's position if the agreement:

- Waives alimony regardless of the wealthy spouse's ability to pay and the less wealthy spouse's contributions to the marriage (e.g., raising children, making a home, supporting the other spouse's career).
- Waives appreciation on the wealthy spouse's separate property, even appreciation due to the efforts of the less wealthy spouse.
- Waives any interest in the wealthy spouse's retirement benefits.
- Provides that the earnings of the wealthy spouse remain his or her separate property and need not be shared with the less wealthy spouse.
- Provides that the couple will not accumulate any marital property or that any marital property that they do acquire will be disproportionately awarded to the wealthy spouse.

- Waives inheritance rights so that the wealthy spouse can completely disinherit the less wealthy spouse.

An agreement that disadvantages the less wealthy spouse is enforceable. Some courts will refuse to enforce an unconscionable (very unfair) agreement especially if one spouse is left with so little he or she requires public assistance. However, many courts will enforce a one-sided agreement if the wealthier spouse fully disclosed his or her finances to the poorer spouse and the poorer spouse was independently represented by an attorney. The agreement may even be enforced if the poorer spouse had an opportunity to seek legal advice and declined to do so. See VII. Creating an Enforceable Premarital Agreement below.

If you are the less wealthy spouse, think seriously before signing such an agreement. You deserve and are entitled to financial security even if you bring fewer assets to the marriage. Making a home, raising children, and providing love and companionship for a spouse are as important to a marriage as money. The law recognizes that these contributions have significant value.

If you are the wealthier spouse, consider the consequences of handing your spouse-to-be a one-sided agreement. This is the person you love. Doesn't he or she deserve a reasonable measure of financial security that you can easily provide if your marriage fails or you die? Presenting your spouse-to-be with a one-sided agreement is not an auspicious way to begin a marriage. Your fiancée may sign it to placate you, but he or she may harbor lingering resentments that can poison your relationship.

If you divorce, your spouse and his or her attorney are likely to challenge an ungenerous agreement. Your attorney may have done everything possible to make it iron-clad, but nothing is certain with litigation. The agreement could be overturned. A challenge to your premarital agreement, even an unsuccessful one, will make your divorce expensive, long, and acrimonious—exactly what you were trying to avoid. On the other hand, a spouse who feels he or she was treated fairly by the premarital agreement is far less likely to challenge it.

There are many ways you can make your agreement more generous while still protecting your interests. Your agreement could give your fiancée some financial benefits in exchange for waiving an interest in your business and separate property. For example, you could agree to pay a reasonable amount of alimony and provide your spouse with a home or other specified property if you divorce. You may want to include a formula that increases the financial benefits based on the length of the marriage or the birth of children. Your agreement could include a sunset clause. A sunset clause provides that the agreement, or certain parts of it, expire after a specified number of years. If you divorce after that time, your assets are split according to your state's rules.

A balanced agreement will promote the success of your marriage. If the marriage fails, a balanced agreement is more likely to serve its intended purpose of protecting your assets.

VII. CREATING AN ENFORCEABLE PREMARITAL AGREEMENT

Most state laws and court decisions establish similar requirements for an enforceable premarital agreement. The most important requirements are:

- The agreement and any subsequent changes to it must be in writing.
- Before the agreement is signed, each party must fully disclose his or her financial information to the other.
- Each party must sign the agreement voluntarily after having sufficient time to review it and obtain legal advice.
- Each party should be represented by a different attorney. The parties should not use the same attorney or law firm.

A. The Agreement Must Be in Writing

Premarital agreements and any modifications to them must be in writing. In a few rare instances, courts have recognized an unwritten modification to a premarital agreement based on the spouses' conduct.

Example: Jim and Pam signed a premarital agreement. Pam owned a restaurant and Jim owned a construction business. Their premarital agreement provided that each would own and operate their respective businesses as their separate property. Things went well in their marriage and businesses for about 12 years. Then the economy went bad.

Jim and Pam did not have the resources to keep both businesses running. They decided to sell Pam's restaurant and use the money to keep the construction company afloat. It worked. The economy improved and business for the construction company picked-up.

Unfortunately, Jim and Pam's marriage developed problems. Jim filed for divorce and claimed due to the premarital agreement Pam was not entitled to any part of the construction company. Pam claimed their premarital agreement was amended by their behavior and a court agreed.

Although Pam was successful, you should never count on an oral agreement being enforceable. Always consult an attorney before agreeing to deviate from your premarital agreement.

B. Each Party Must Fully Disclose All Assets and Liabilities to the Other

If prospective spouses do not fully disclose their assets, income, and indebtedness to each other, they cannot make an informed decision on whether to sign the premarital agreement. Without full disclosure, you and your attorney cannot evaluate the fairness of the agreement.

Full disclosure is especially important if the premarital agreement provides for an unequal division of marital assets. If both parties do not disclose all their assets and liabilities to each other, a court may refuse to enforce a premarital agreement as fraudulent.

Example: Kyle owns a commercial horse stable and he rents stalls out to local horse owners. Kyle also owns an interest in a racehorse. Kyle failed to disclose his interest in the horse when he entered into a premarital agreement with his fiancée Brenda, who did not know about the horse. In the agreement, Brenda waived alimony and any interest in Kyle's business. After the marriage, the horse is successful on the track and its value soars. Kyle receives a share of the horse's winnings, which he deposits in a secret account. When Brenda and Kyle divorce, Brenda's attorney hires a forensic accountant who discovers the hidden account and the horse. Brenda asks the court to invalidate the premarital agreement, award her alimony, half the horse's winnings, and half its value. The court agrees.

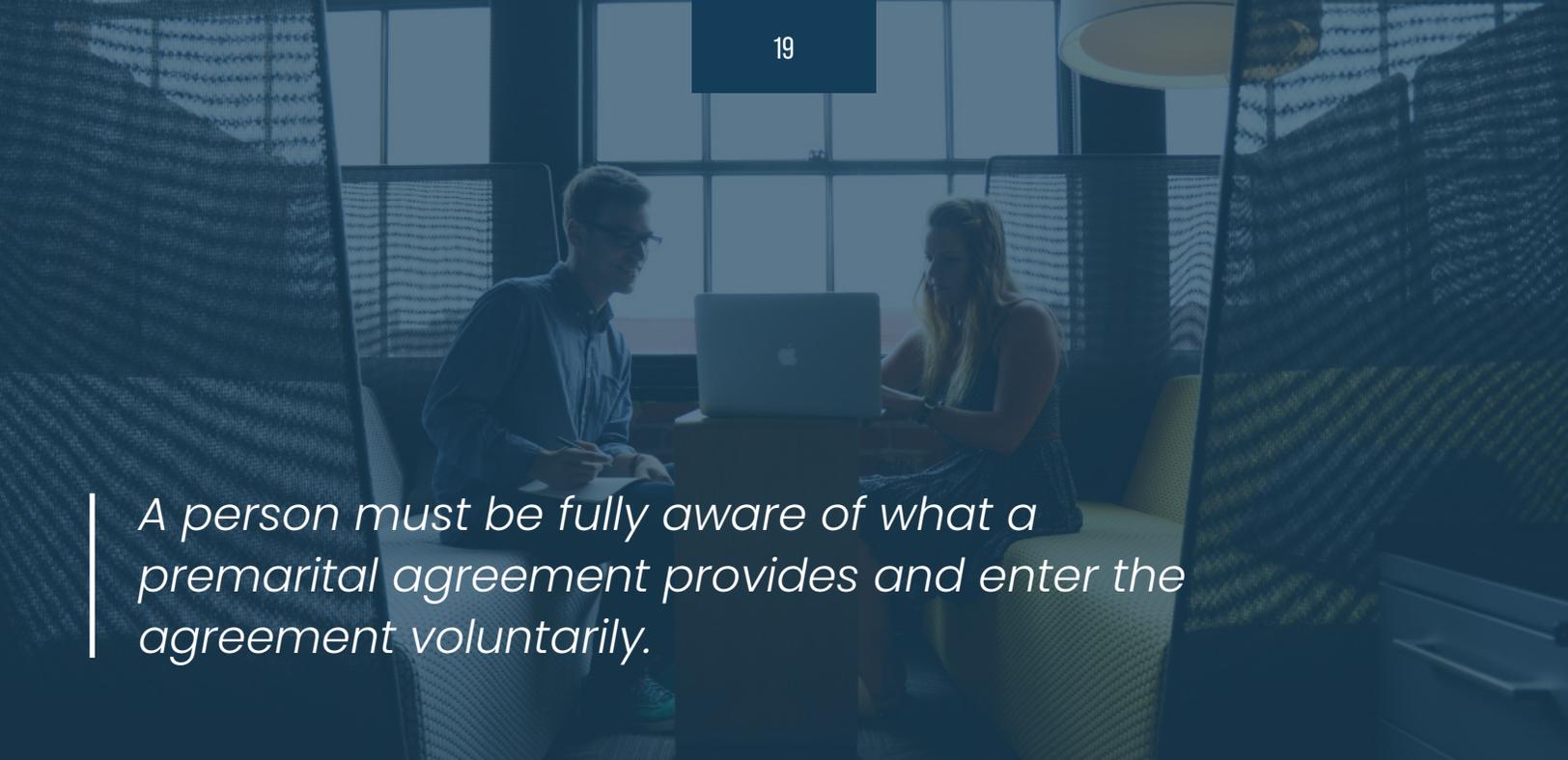
A court may refuse to invalidate an agreement based on lack of full disclosure if the party contesting the agreement knew about the undisclosed information. For example, Brenda may have seen the ownership papers for the horse if she worked in Kyle's business or lived with him before they married. Perhaps they had a joint account into which the horse's winnings were deposited. In these situations, Kyle's failure to include his part ownership of the horse with his disclosure materials probably would not invalidate the agreement.

Some states allow prospective spouses to waive disclosure. Waiving disclosure is a bad idea. You cannot understand the impact of the agreement on your rights and obligations unless you are completely informed about your spouse's finances.

C. What to Disclose: a Checklist

Here's a list of the materials you should exchange with your prospective spouse before entering into a premarital agreement:

- Last three years of tax returns, with all schedules and attachments. You need three years of tax returns to get an accurate picture of the other party's finances. A person's income may fluctuate from year to year. Annual fluctuations can be deliberately manipulated to make the person seem less prosperous.
- Current statements for all financial accounts.
- Identification of all real estate owned, how title is held, the current mortgage balance, home equity loans or lines of credit, appraised value, and appraisals, if any. Property in which you have an interest but that is not in your name, such as property held in a trust of which you are a beneficiary, should be included.
- Car titles, loan balances and estimates of values.
- Most recent retirement account statements, along with loan balances and projected retirement benefits.
- Jewelry and personal property appraisals for art, antiques, and collections.
- Identification of family heirlooms, particularly any gifted to the fiancée for which return will be provided in the agreement.
- Business tax returns, profit and loss statements, balance sheets for the past three years. Copy of the owner's stock certificate, or similar designation of ownership percentage or interest. If business valuation appraisals have been done, provide those as well.
- Life insurance policies, including loan information.
- Monthly statement from credit card, installment or other debts and obligations.



A person must be fully aware of what a premarital agreement provides and enter the agreement voluntarily.

- The judgment for dissolution of marriage, marital settlement agreement, and parenting agreement from any prior marriage pursuant to which obligations or entitlements still exist.

D. Each Party Must Understand the Agreement and Sign It Voluntarily

A person must be fully aware of what a premarital agreement provides and enter the agreement voluntarily. Whether a premarital agreement was voluntary can be a point of contention. For example, if a person signs the agreement under threat of physical violence, the person did not voluntarily sign the agreement. If a person signs under emotional duress or the undue influence of another person, the agreement may not be voluntary, but these situations are less clear and harder to prove.

Conditioning the marriage on the execution of a premarital agreement generally does not constitute duress or coercion.

Courts addressing voluntariness have also considered whether a party had sufficient time to study the agreement and consult with an attorney before signing it. An agreement that is prepared and executed well in advance of the wedding suggests to a court that the parties know what they were doing. An agreement executed a day or two before the wedding without advice from counsel raises questions about full disclosure and informed consent.

Example: Edward presented Karen with a prenuptial agreement the day before their wedding. Karen did not have the opportunity to consult with an attorney and she signed the agreement without reading it. The court invalidated the agreement holding that Karen did not sign it voluntarily.

E. Each Party Should Have an Attorney

Couples who are contemplating marriage often share many things. An attorney should not be one of them. When considering a premarital agreement, both parties need to look out for their own interests. The best way to do that is with separate attorneys.

Courts are less likely to enforce an agreement against a party who was not represented by an attorney. They will closely scrutinize whether the unrepresented party understood the agreement and had the opportunity to hire an attorney. For example, California requires the court to find the agreement was not voluntarily executed unless the party against whom it is sought to be enforced (1) had independent counsel or (2) waived the right in a separate writing, was given the agreement at least seven days before executing it, and received a written explanation of the agreement.

A premarital agreement should not be a do-it-yourself project. The internet and legal self-help books offer many examples of premarital agreements. You may want to use one as a starting point for discussion with your spouse-to-be and your attorney. However, the final agreement should be professionally drafted by a family law attorney who knows the requirements in your state. If your prospective spouse's attorney drafts the agreement, your attorney will review it and advise you on the consequences of signing it. If the agreement unfair to you, you have the opportunity to negotiate more favorable terms.

The best policy is for each party to choose and pay for his or her own counsel. Even if you provide funds to pay for your fiancé's attorney, do not choose the attorney or suggest any attorneys to him or her. A court may be skeptical of advice provided by an attorney who has been chosen and paid for by the opposing party.

VIII. KEEPING YOUR AGREEMENT UP TO DATE

You should review your premarital agreement from time to time to make sure it reflects your family's current circumstances. A premarital agreement is based on the situation of the parties at the time it is married. The future is unpredictable and much can change during a marriage. A spouse can acquire new job skills or start a business. A spouse can become disabled and unable to work. A business can flourish or fail. An unexpected windfall or inheritance can appear. A special needs child can be born. These and other major developments could require a modification of your agreement. Remember that an oral modification of your agreement is usually not enforceable. Any changes that you and your spouse agree to make must be put in writing.

IX. OUTLINE OF A TYPICAL PREMARITAL AGREEMENT

Here is an outline of provisions that are often included in premarital agreements. It is provided to give you an overview of a typical premarital agreement and a summary of what it can accomplish. You may not need all these provisions in your agreement and you may need additional provisions.

The clauses that are appropriate for your premarital agreement and how they should be worded depend on your state's law and the problems you and your spouse want to address. Provisions that are appropriate for a second marriage, couples with similar net worth, or a late in life marriage may not be appropriate for a young couple in a first marriage or a couple with widely disparate wealth.

A. Introductory Statements

Premarital agreements may begin with some introductory statements or recitals that reflect the reasons for the premarital agreement and the parties' acknowledgments that all the requirements for a valid agreement have been met.

- **Prior marriages and marital obligations.** Here the parties acknowledge prior marriages, children from prior marriages, and any financial obligations and entitlements stemming from those marriages, for example, the obligation to pay or right to receive alimony and child support.
- **Full disclosure.** The parties acknowledge that they are satisfied that each has fully disclosed all assets, income, and debts to the other.
- **Intention to keep separate property separate.** The parties express their intention to keep the property that they enter the marriage with and appreciation on that property separate.
- **Inheritance rights.** The parties state they understand the inheritance rights that they are entitled to under state law and that they are waiving with the agreement.
- **Review of agreement.** The parties state that they have read and studied the agreement and have considered the consequences of signing it.
- **Independent representation.** The parties provide the names of their attorneys and represent that they have had independent counsel from them concerning the subject matter of the agreement.
- **Voluntary agreement.** The parties acknowledge that they entered the agreement voluntarily without any coercion or duress.

B. Property

- **Waiver of interest in other party's separate property.** Each party can list the property that he or she owns at the time of the marriage either in the agreement or in schedules attached to it. The agreement can then provide that each waives any interest in the other's property that he or she would otherwise acquire because of the marriage.
- **Property to remain separate.** The parties can agree that the property they own on entering the marriage will remain their separate property and, if the marriage ends, the property will remain each spouse's property free from any claims of the other.
- **Appreciation in separate property to remain separate.** The parties can agree that appreciation, both active and passive, of separate property or any property acquired in exchange for separate property will remain separate property.
- **Facilitation of sale or encumbrance of separate property.** Each can agree that the other has a right to sell or borrow against his or her separate property and that the other spouse will sign whatever documents are necessary to complete the transaction.
- **Wedding gifts.** The parties can provide for the distribution of wedding gifts between them should the marriage fail within the first few years. For example, they could provide that each party receives the gifts given by that party's family and friends if the couple ends the marriage within five years.
- **Waiver of inheritance rights.** Each party can waive any rights he or she may have under state law to inherit from the other. The agreement can clarify that the waiver does not extend to any inheritance that one spouse may leave the other in a will, codicil, or trust to protect the surviving spouse's right to an inheritance that the deceased spouse intended to provide him or her.
- **Waiver of interest in retirement accounts.** Each party may agree to waive any interest they would otherwise acquire by marriage in the other party's retirement accounts. However, to waive an interest in an employer-provided retirement plan subject to ERISA, the parties should execute written waivers after the marriage as only spouses can execute ERISA waivers.
- **Marital property.** The parties can agree on how they will divide any marital or jointly owned property that they acquire if the marriage ends in divorce. The division may or may not be equal.
- **Down payment on marital home.** If one party provided the down payment from separate property, the agreement can provide that, if the parties divorce, the down payment will be returned to the party who provided it before any remaining equity in the home is divided.

C. Alimony and Support

- **Specification of alimony or waiver of alimony.** Each party can waive the right to receive alimony or spousal support from the other. Alternatively, the parties can agree that one party will pay the other a specified amount



The parties can provide for the distribution of wedding gifts between them should the marriage fail within the first few years.

of alimony. The alimony may be payable as a one-time lump sum or periodically for a specific period, for example, \$30,000 per year for a number of years equal to one-half of the years that they were married.

- **Waiver of attorney's fees.** Each party can waive the right to seek attorneys' fees from the other for a separation or divorce.
- **Child support for children of prior relationships.** The parties can agree that neither is obligated to pay child support for the other's children and that any child support received by one spouse is that spouse's separate property.

D. Income and Debts

- **Income to remain separate.** The parties can agree that each party's income earned during the marriage will remain the separate property of the person earning it.
- **Premarital debts.** The parties can agree to remain solely responsible for any debts that they have at the time of the marriage including child support for children from prior relationships.
- **Debts incurred during marriage.** The parties may want to agree that neither spouse will obligate the other on any debt after the marriage without that spouse's express approval and neither will sign the other's name to any obligation.
- **Allocation of debts on divorce.** The parties can specify how they will divide their debts on divorce. For example, they may provide for an equal (or some other percentage) division of debts for joint credit card and other joint debt. They could further provide that debt incurred in one spouse's name will be the sole responsibility of that spouse.

E. Business Interests

- **One spouse's waiver of interest in the other's business.** If one spouse owns a business, the non-owner spouse can waive any right or claim to the business that he or she would otherwise acquire because of the marriage.
- **Non-owner spouse's employment in the business.** If the non-owner spouse works or may work in the business, he or she can agree that the work does not entitle him or her to any ownership interest in the business or additional compensation.
- **Owner spouse's salary is fair compensation.** In this provision, the non-owner spouse agrees that the owner spouse was adequately compensated by the business. It is intended to preclude the non-owner spouse from claiming that the marital unit was unfairly deprived of income and thus, he or she is entitled to a larger share of the property in compensation.

F. Miscellaneous Provisions

- **Governing law.** This provision specifies which state's law governs the interpretation of the agreement.
- **Entire agreement.** This provision states that the parties have no promises or understandings that are not set forth in the agreement.
- **Amendment or rescission.** This provision states that the premarital agreement can be changed or canceled only with a subsequent written document.
- **Severability.** This provision states that if any part of the agreement is determined to be unenforceable, the rest of the agreement remains in effect.
- **Effective date.** The agreement becomes effective when the parties marry. If the parties don't marry, the agreement is void.
- **Sunset provision.** A sunset clause provides that the agreement or specified parts of it are no longer enforceable if the marriage lasts for a specified period.