Divorce, Recession Style

The way that couples – and the professionals assisting them – are dealing with divorce has had to change dramatically to keep up with today's financial realities.

By Diana Shepherd, CDFA™

As the economic situation worsens, many couples across North America are re-examining their wedding vows. When they promised to love each other "for richer or for poorer", most couples didn't envision owing more on their mortgage than the house was worth, or jobs and retirement assets evaporating. So can love withstand a recession? Currently, there are two contradictory trains of thought.

The first is the argument that worry and anxiety over money will lead to greater strains in marriages. Indeed, according to Nobel prize-winning economist Gary Becker, when the economy goes down, the divorce rate goes up. On the other hand, a lack of financial resources may force more couples to stay together – at least temporarily – or perhaps forego the expensive services of a lawyer in favor of "pro se" or "do it yourself" (DIY) divorce.

What we can say with certainty is that the current economic climate is having an impact on divorce in some unexpected ways. Although the jury's still out about whether or not there will be a rise or fall in divorce rates during these tough economic times, two recent surveys of Certified Divorce Financial Analysts (CDFAs) shows that the way couples – and the professionals assisting them – are dealing with divorce has had to change dramatically to keep up with today's financial realities.

There's an old joke: "Why is a divorce so expensive? Because it's worth it!" In today's economy, some couples are finding that divorce isn't "worth it" in the sense that they can't afford to divorce – or move out of the family home – until their financial situation improves. Some couples are staying together for financial reasons – or, if they decide to move forward with their divorce, they are being forced to get creative in terms of their living arrangements and property division.

According to a survey of CDFAs conducted in April 2009, 68% of respondents said they had seen clients who could not afford to get divorced because of recession-related financial problems.

- 63% said that this represents an increase over previous years
- 35% said that the number had remained constant
- only 2% reported a decrease in the number

The survey also revealed that the ways in which assets are divided has changed significantly. With housing prices and retirement account values plummeting, divorcing couples are looking for settlements of liquid assets only: they want cash rather than stocks, investments, real estate, or retirement plans.

Traditionally, there have three sources of money that might be available to an individual as a result of his/her divorce: child support, spousal support, and marital property. Let's take a look at the effect the recession has had on some of these potential sources of income.

Child and Spousal Support

Child support is determined by guidelines that are mandated by the state or province. Before the recession, CDFAs used to caution parents that the child support formula did not take into consideration the child's actual expenses: for example, extra-curricular activities, private school tuition and college funding are not factored into the formula. Today, we're seeing cases in which the support does not cover basic necessities such as food, clothing, and shelter.

Many courts are seeing a surge in the number of divorced parents coming back to request that their child and/or spousal support be modified due to a change in their circumstance – such as being laid off from work or losing their homes to foreclosure. Payors are asking that the amount be reduced, and recipients that the amount remain the same or be increased.

In areas hard-hit by the recession, the number of payors seeking reductions in their child or spousal support obligations has skyrocketed. The Honorable Kathleen M. McCarthy, who serves in the Family Division of the Wayne County Circuit Court, Michigan, says that most of the motions she sees in her courtroom now are motions for modification to spousal or child support. And in the last year, the number of Franklin County, Ohio residents asking the court to reduce their child-support payments has jumped by 80%.

Having the child support reduced or even eliminated can have a devastating effect of the family. Some custodial parents depend on this income to feed and clothe their children; if the payments are reduced or eliminated, it puts the burden on the custodial parent to come up with funds another way.

Child support payments take precedence over spousal support, so if the child support is being reduced or eliminated, it's safe to assume the same is happening to spousal support.

The Matrimonial Home

In many divorces, the biggest financial question is who gets the matrimonial home. Should the wife keep it, should the husband, or should they sell it and split the proceeds? What if the house is "underwater" – meaning that the householders owe more on their mortgage than their house is worth? The answer is not always easy or clear.

In a normal economy, couples typically build equity in their homes; if they decide to divorce, they would usually divide the equity they had built by selling the house or by one partner buying out the other's share. But after the recent boom-and-bust cycle, many couples own houses that neither spouse can afford to maintain on his/her own, and that they cannot sell for what they owe.

First American CoreLogic, a real estate data company, has calculated that 7.6 million properties in the USA were underwater as of Sept. 30, 2008, while another 2.1 million were in striking distance. That is nearly a quarter of all homes with mortgages. The 20 hardest-hit ZIP codes are all in four states: California, Florida, Nevada, and Arizona.

According to Housing in Crisis: When Will Metro Markets Recover?, a comprehensive new study from Moody's Economy.com, by the end of this unprecedented downturn, house prices will have declined by double digits peak to trough in nearly 62% of the USA's 381 metro areas. In about 10% of metro areas, price declines will exceed 30%; house prices in California and Florida, for example, have descended by 50% or more from peak.

The housing downturn is causing divorcing couples, their lawyers, and their financial advisers to come up with creative alternatives to traditional divorce settlements. According to the Institute for Divorce Financial Analysts (IDFA) survey, the most common solution is for ex-spouses to retain joint ownership and continue to live in the house (often, one person moves into the basement while the other lives upstairs) until the market improves, agreeing to postpone final division of assets until after the house is sold.

Other common solutions include:

1. Renting the house to a third party until it can sell for more than the debt

2. One ex-spouse stays in the house and pays rent to the other until the market improves
3. “Birdnesting”: the ex-spouses retain joint ownership of the home, they also rent a small apartment nearby, and each one alternates living in the house with the kids and in the apartment on his/her own
4. Structuring two levels of spousal support: before and after the house sells
5. Agreeing to sell the home at a loss, share the loss, and move on with their lives
6. Short-sale, foreclosure, or bankruptcy.

Judge McCarthy has seen a number of people coming back to court to try to modify their property settlement when the house fails to sell. “When they divorced, they agreed to maintain the status quo,” she says. “For example, one party might agree to continue to make payments on the house until it could be sold, at which time they would use the money to pay off their credit-card debts.” Three years later, the house still hasn’t sold, the house is now worth less than the mortgage, and one spouse is stuck making payments indefinitely. “Unlike support, property settlements are non-modifiable,” Judge McCarthy points out. “So unless both parties agree to modify the original agreement, they’re locked into it.”

DIY Divorce

In an effort to keep costs down, some couples are also looking outside the legal system for help navigating through a divorce. There are many services and companies who are advertising cheaper alternatives to lawyers – from mediators to divorce kits to virtual alternatives. As the recession deepens, some cash-strapped couples who can’t face the prospect of cohabiting indefinitely are choosing to handle their own divorces rather than hiring lawyers and other divorce-industry professionals to assist them. If the marriage was short, if there are little or no assets to divide, if there are no children of the marriage, then DIY divorce might be an option.

Judge McCarthy says that the number of self-represented litigants is “staggering”. One of the biggest dangers of DIY is that the litigants will be held to the same legal standards as lawyers. “They do not know the specifics of the law, or how to present their best case to the court,” says Judge McCarthy. “Frequently, they are unable to get their point across – or they’re not raising the correct issues.”

Self-representation is also likely to create time-bombs for couples who do not understand the legal and financial implications of the agreement they have created and signed using a kit or online service; down the road, when the agreement they signed proves unworkable or grossly unfair, they may end up spending even more money trying to untangle the legal mess they inadvertently created. Too often, Judge McCarthy sees self-represented litigants locking themselves into unworkable property settlements. “I always ask them ‘Do you understand that this agreement is non-modifiable?’ and they tell me they do. But one or two years later, they’re back in court telling me they didn’t anticipate what could happen if the house didn't sell, for example. A good lawyer would have told them to build in contingencies to avoid being locked into a financially devastating situation."

Even if you've decided that DIY is the way to go, you should consider hiring a lawyer to read over the agreement and explain your rights and responsibilities before you sign on the dotted line. And before you accept a settlement offer, have a CDFA examine it to see whether:

- it is truly equitable
- there are tax or other financial implications that will take big bites out of your savings and investments
- the proposal will meet your short- and long-term needs.

"It's imperative for divorcing couples to keep in mind that the current economic conditions will indeed change, and planning for their future is paramount," says Fadi Baradihi, president and CEO of IDFA. "With people cutting back on legal and other professional fees, it's even more imperative that they understand how to plan for their long-term financial stability. Working with a Certified Divorce Financial Analyst can help to preserve the family's finances – which is crucial in today's economy."

Diana Shepherd is the Marketing Director for the Institute for Divorce Financial Analysts™ (IDFA™). Founded in 1993, IDFA™ is the premier national organization dedicated to the certification, education, and promotion of the use of financial professionals in the divorce arena.

This article was retrieved on 3/21/2011 from the Institute for Divorce Financial Analysts™ website.