

## **Prenuptial Agreements and Marriage Contracts**

***If you're thinking of taking the plunge a second time, you should consider whether you need the protection of a prenuptial agreement or marriage contract.***

By Nancy Kurn, CPA, CDFA™, JD, MBA

A prenuptial agreement is a contract that two parties enter into in contemplation of marriage. It can also be referred to as a “premarital agreement,” “antenuptial agreement,” or simply a “prenup”; in Canada, it is called a “marriage contract.” (For more information, see “Canadian Marriage Contracts” at the bottom of this page.)

In most states, until the 1980s, prenuptial agreements were deemed against public policy and not valid to the extent they pertained to divorce or separation. They were considered against public policy because it was thought that they encouraged divorce and allowed the husband to thwart his legal obligation to support his wife. Prior to that time, they were valid to the extent that they pertained to the death of one spouse.

A postnuptial agreement (called a “marriage contract” in Canada) is similar to a prenuptial agreement except that it is entered into after the parties have married. In some states, postnuptial agreements are not valid if either spouse is contemplating divorce or separation.

Canadian law also recognizes cohabitation agreements for couples of the same or opposite sex that currently, or intend to, live together.

First, a brief overview of U.S. law. In community-property states (Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, Washington, and Wisconsin), any assets that are acquired during the marriage are marital assets and divided equally between the spouses upon divorce. In equitable-distribution states, any assets acquired during the marriage are divided between the spouses in a fair and equitable manner. In many states, the appreciation in value of a separate asset during the marriage is a marital asset.

Generally, a prenuptial agreement sets forth how the marital assets will be divided in the event of divorce or either spouse's death. It can also address what assets remain the separate assets of each spouse and what happens to the appreciation in value of the separate assets. For example: Joe has an IRA worth \$200,000 at the time he marries Barb. When they divorce, six years later, the IRA is worth \$500,000. In some states, \$200,000 would be considered Joe's separate property and \$300,000 would be considered a marital asset to be divided between Joe and Barb.

Barb has a home worth \$250,000. Joe moves in after they marry, and they use the home as their marital home. When they divorce, the home is worth \$400,000. The court is very likely to decide that Barb made a gift to the family, classify Barb's home as a marital asset, and split the entire asset. If Joe and Barb created a prenuptial agreement, they could have agreed that Joe's IRA - including any appreciation during the marriage - would have remained his separate property and that Barb's home - including any appreciation - would have remained her separate property.

Although there are limitations in many areas, prenuptial agreements may also cover issues of spousal and child support. The spouses can agree not to contest any estate-planning documents prepared by the other spouse and to give up certain statutory rights upon the death of one spouse. They can also agree to file joint or individual tax returns during the marriage.

Some couples also cover issues that arise during the marriage, such as their children's religious upbringing, how household duties will be divided, how finances will be handled, and sometimes even how often the couple will have sex. These provisions are best left out of the agreement, because a judge has no mechanism to enforce them. In addition, you have to be very careful with these provisions, because if they are too unusual, the entire agreement may be deemed invalid by a judge.

In addition to addressing how the assets will be divided, it is also important to decide how debts, particularly those acquired before the marriage, will be divided.

## **Limitations**

Generally, two parties can agree to anything that does not violate any law or oppose public policy (interest). For example, contractually encouraging someone to divorce would be against public policy and invalidate the agreement. A prenuptial agreement has several limitations; some are unique to prenuptial agreements:

- The parties must fully disclose their assets to the other party. Otherwise, one spouse is giving up rights to assets that he or she knows nothing about.

- Some states do not allow prenuptial agreements to limit or eliminate spousal support. In addition, the agreement may be deemed invalid if the spousal support is very high, because the agreement then encourages divorce and is against public policy. In Canada, spousal support provisions are valid.
- Child support cannot be limited pursuant to a prenuptial agreement. In some states, child-support provisions will be upheld as long as the support is not less than the statutory guidelines. In other states and in Canada, provisions regarding child support are invalid. Anything limiting child support to less than statutory amounts cannot be enforced. Child support is governed by state guidelines in all 50 states.
- In both the U.S. and Canada, any agreement regarding child custody or visitation in a prenuptial agreement is invalid.
- A judge could deem the agreement void based on typical contractual theories such as fraud, misrepresentation, duress or coercion. A unique circumstance with the prenuptial agreement is the timing of the signing of the agreement. If the groom takes the agreement to the bride the night before their wedding, then she could certainly argue that she signed the agreement under duress, or that she was coerced into signing it. To avoid the argument that the agreement was signed under duress, it should be signed long before the wedding takes place. Some would argue at least 30 days and others recommend before the wedding invitations are sent to the guests.
- The prenuptial agreement cannot be unconscionable. If one spouse is left destitute, the court may decide that the agreement is not valid, because it is unconscionable.
- In Canada, any provision in the prenuptial agreement regarding the right to live in the matrimonial home, or the right to sell or transfer the matrimonial home, will be invalid.

## **Benefits**

Prenuptial agreements are not just for the wealthy. They are particularly useful in second marriages, where one or both spouses have children from a previous marriage.

Mike and Carol are going to be married. Mike is a widower and has three sons. Carol is a widow with three daughters. Both of them have assets that they are bringing to the marriage, including the death benefits they received upon the death of their first spouses. Mike and Carol are contemplating hiring attorneys to prepare a prenuptial agreement to ensure that the assets they received from their deceased spouses will go to their respective children.

A prenuptial agreement has numerous benefits. Some of these benefits include:

1. The certainty it provides as to what happens in the event of a divorce or the death of either spouse.
2. Protecting children from a prior marriage.
3. It is prepared, in theory, when there is harmony instead of at a point when the relationship is very contentious.
4. The parties can negotiate the terms of the agreement; instead of having a third party (a judge) and state and provincial laws decide how to divide the couple's assets.

## **Challenging a Prenuptial Agreement**

If you're going to have a prenuptial agreement, you should each hire a lawyer to ensure that it is valid and will hold up in court. Do not try to prepare one yourselves! Steven Spielberg and Amy Irving allegedly drafted their prenuptial agreement on the back of a napkin; the court did not recognize it as a valid contract, and it has been reported that Irving received over \$100 million in assets after their four-year marriage ended.

A prenuptial agreement can be successfully challenged in the following ways:

1. If it has not been signed. Most states require the prenuptial agreement to be signed by the party to be charged with the agreement.
2. By proving the other party did not fully disclose their assets.
3. By proving that you were not represented by independent counsel. Each party should be represented by his or her own lawyer. Generally, this alone will not be sufficient to invalidate the agreement.
4. By proving that the agreement was unconscionable when it was signed.
5. By proving that the agreement is now unconscionable based on today's circumstances.
6. The agreement can be challenged based on duress, due to the timing of the signing.
7. It can be challenged on any other typical contractual theory such as fraud, misrepresentation, or coercion.

## **Additional Issues to Consider**

Each spouse should draft their estate plans so that they conform to the terms in the prenuptial agreement. You do not want to force your children and surviving spouse to get involved in litigation involving your estate. The costs could result in everyone getting significantly less.

You may also want to consider using life insurance to replace assets that go to either your children or your spouse. For example: Mike and Carol purchased a new home with the proceeds from the sale of Mike's previous home. Mike wants Carol to have the home upon his death. He can purchase insurance, naming his sons as beneficiaries, to replace the proceeds from the sale of his previous home.

Prenuptial agreements can be amended or revoked at any time. Some couples add a sunset provision terminating the agreement after a certain period of time, such as ten years.

### **Case Study: Sarah and Brad**

Sarah has a technology business that she thinks is worth approximately \$1,000,000. In 2003, it had gross sales of approximately \$750,000 with profits of approximately \$300,000 (including Sarah's compensation). The income has steadily increased at about 20% annually. She is about to marry Brad. This will be the first marriage for both of them, and neither of them have children. Brad's net worth is approximately \$50,000 and his annual income is approximately \$40,000 and increases at about 3% per year. Should Sarah have Brad sign a prenuptial agreement to protect her business?

If Sarah wants to protect her business and its future growth, then she should have Brad sign a prenuptial agreement. Otherwise, any future increase in the value of the business during the marriage would likely be split between both parties. Without a prenup in place, if Brad sometimes helped Sarah with the business, then a judge may find that the business is a marital asset and split the business. Sarah must hire an expert to perform a business valuation; better still, she and Brad could jointly decide on the expert that will perform the valuation, or each of them could hire their own expert and then average the two valuations. If this is done, then Brad would have a difficult time challenging the value of the business.

---

***Nancy Kurn is the former Director of Educational Services for the Institute for Divorce Financial Analysts™ (IDFA™) - the premier national organization dedicated to the certification, education, and promotion of the use of financial professionals in the divorce arena.***