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Insurance Concerns of Divorcing Couples

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Prepared for:
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Insurance Concerns of Divorcing Couples

Few life changes are of more consequence than a divorce. In addition to the financial and emotional difficulties, you'll face special concerns about your insurance coverage. Planning for these changes should begin long before the divorce is final. The selection of life and health insurance beneficiaries may have to be revised. If you have children, many of your insurance concerns will center on whether you are granted custody. And because it's common while married for one spouse to maintain health insurance for the family, the breakup of a marriage can have serious insurance consequences for the other spouse, especially if he or she was not employed outside the home.

Protecting alimony and child support payments

The spouse given custody of the children (custodial parent) should make sure that the life of the noncustodial parent is insured. If you're the custodial parent, you don't want to end up in a position where child support payments suddenly end because your ex-spouse dies. The same thing applies to alimony payments. Life insurance can protect you and your children in case of untimely death. Some agreements require the noncustodial parent to pay for a policy on his or her life and to name the custodial parent as beneficiary. Your agreement should also state that you periodically receive proof that the policy is still in force.

If you're the custodial parent

If you're receiving alimony or child support payments, purchasing a life insurance policy on your former spouse is the easiest way to protect yourself and your children. If you can't get new insurance on your former spouse, have his or her existing policies transferred to you as the new policyowner and beneficiary. This can be planned as part of the divorce agreement. Make certain that you are designated as the outright policyowner or as the irrevocable beneficiary. If you have trouble paying the policy premiums, you can petition the court to have alimony and child support payments increased to cover the cost of insurance. The court may even require your former spouse to pay the premiums. In this case, monitor the policy periodically to make sure that the payments are being made.

If you're the noncustodial parent

Even though you don't have custody of your children, you'll want to ensure that they are protected financially. You may also have certain responsibilities to your former spouse. Insure your obligations by paying for a new policy on your life for the custodial parent. That way, you can keep any policies you currently have and protect your children's future at the same time. The policy can be given to your former spouse free from gift tax if given either before or as part of the divorce agreement. If the policy is entirely in your former spouse's name, any premiums you pay will likely be considered alimony for income tax purposes and are tax deductible. You should also insure the life of your former spouse. Remember that if he or she were to die, you would most likely gain custody of the children, increasing your expenses dramatically.

Naming life insurance beneficiaries at divorce

Changing the beneficiary on a life insurance policy is as easy as calling up the insurer and requesting the appropriate paperwork. You can designate any person or entity to be the beneficiary, although some states require that the beneficiary have an insurable interest in your life (i.e., someone to whom you have a financial obligation). But during or after a divorce, your choices may be somewhat limited.

If a court has ordered, for instance, that you must continue an existing policy with your former spouse as beneficiary, you cannot change it. If you're under no such constraints, however, your choice usually boils down to either your estate, your ex-spouse, or your children. Designating your estate as beneficiary will tie up the insurance proceeds in probate. And unless you need to protect alimony or child support payments, you probably have no need or desire to name your ex-spouse. Designating your children as beneficiaries may be your best course, but doing so can be very complicated if they are minors. One solution is to create a trust for the children and name the trust as beneficiary.

Note: Divorce laws may differ from one state to the next, so consult an experienced legal professional before proceeding.

Health insurance coverage and divorce

Often, one spouse participates in a group health insurance plan at work that provides coverage for both spouses. When a divorce occurs, coverage for the nonemployee spouse will often end, unless the divorce decree requires continuation of coverage. If there is no such requirement, temporary protection may be provided by the Consolidated Omnibus Budget Reconciliation Act (COBRA). This federal law protects employees of companies with 20 or more workers and their dependents from losing group insurance coverage as a result of job loss or divorce. Certain governmental and nonprofit enterprises are exempt. If your former spouse maintained family health coverage through work, you may (at your own expense) continue this group coverage for up to 36 months, or until you remarry or get coverage under another group health plan. Several states have enacted laws that may provide a former spouse with more generous rights than those under COBRA.

Disability income insurance and divorce

If you receive alimony or child support, another risk to your income may arise if your former spouse becomes disabled. If he or she has no disability insurance and is unable to work, the court may modify the alimony and child support obligation, reducing or eliminating payments to you. With a disability policy, your ex-spouse will receive benefits each month and may be capable of paying the same amount of alimony and child support. Planning for disability insurance should be completed before the divorce is final. Unlike life insurance, you can't own a disability policy on someone else. So, the divorce decree may require that your ex-spouse pay the premiums on a policy and that you are entitled to regularly receive proof that the policy is in force.

Property insurance and divorce

Real and personal property must be insured by the actual owner of the property (e.g., a car registered in your name must be owned by you). So, property insurance policies must be modified or rewritten to reflect the proper owner as the insured. Also, if a husband and a wife enter into an agreement covering their property rights, and divorce occurs within a specified period, all transfers of property are considered made for full consideration and are not subject to gift tax. With respect to married homeowners, the house can be sold immediately and the proceeds divided. Or, both spouses can continue to own the house jointly with a view toward a future sale. Another alternative is for one spouse to keep the house and buy out the other's interest. Or, the court may award the house to one spouse without trading assets while the title is held by both spouses. If the ownership is changed, a new deed should be drawn up to reflect the new arrangement, and the homeowners policy should be updated.

If you move into an apartment (even temporarily), you should buy renters insurance to cover your possessions.

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